Handbook on Professional Opportunities in Internal Audit

The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

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Internal Audit Standards Board

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Foreword

In today's rapidly changing and expanding environment, internal audit plays an essential role within an organization by looking beyond processes and controls. It helps the organization to improve business performance by identifying enterprise-wide cost efficiencies, providing strategic insights that improve performance and also by providing key insights that focus on the risks that matter.

To meet the need for increased scope and improved execution, internal auditors must play a more meaningful role in the broader value delivery agenda of organisations. The challenges would lie in building consensus for internal audit's expanded role and delivering upon those expectations. The Institute reinforces its ongoing commitment to support the professional development of internal auditors through all of their opportunities and challenges by providing best technical material.

I am glad that the Internal Audit Standards Board of the Institute has decided to bring out a Handbook on Professional Opportunities on Internal Audit. This comprehensive handbook discusses the evolving opportunities for the members in internal audit and serves as a useful tool for the future of the internal auditors. I wish to place my deep appreciation to CA. Rajkumar S. Adukia for his continued efforts to develop literature for the benefit of the members and other readers.

I am sure that the members will use this comprehensive Handbook to seize opportunities in the internal audit field and make the most of it.

October 24, 2011 — **CA. G. Ramaswamy**

New Delhi — *President, ICAI*

Preface

Trends which have the greatest impact on the internal audit profession in the coming years are globalization, changes in risk management, advances in technology, talent and organizational issues and changing internal audit roles. By understanding these trends, the internal auditors can seize the hidden opportunities and can become strategic players in the organizations. Central to internal audit's strategic repositioning is the ability to adopt an all inclusive, conceptual approach to audit, risk assessment and risk management that extends well beyond a focus on financial controls.

Now, internal auditor has new opportunities to both expand its traditional value preservation role and leverage its skills in new ways to support value creation. Considering this dynamic scenario, the Internal Audit Standards Board has brought out the Handbook on Professional Opportunities in Internal Audit which assimilates latest trends and thinking, opportunities in the field. When the Internal Audit Standards Board conceived the idea of bringing out this publication on Professional Opportunities in Internal Audit, the basic objective behind the same was to bring out a comprehensive publication on current trends in the field of internal audit and the various opportunities available for the members in internal audit. This publication is quite comprehensive, providing a step by step guidance on every aspect of internal audit. It is divided into various parts. This publication contains guidance on aspects such as history, definition, scope, need, overall planning, internal audit programme, report and management of internal audit function. This publication provides guidance regarding the internal audit of internal control framework, stock audit/ credit audit, concurrent audit, due diligence, corporate governance, social audit, industry specific audit, management audit and assurance management. For better understanding of the readers, the publication also contains internal audit letters, documents and checklists.

While preparing the basic draft of the Handbook, I have tried to incorporate all the challenges facing the internal auditors now and in the near future. However, I am also of the view that whereas on the one hand bringing out such publications by the Institute is necessary to keep the members upto date, it is equally essential for the members to be proactive and make liberal use of technology to harness the various sources of information and knowledge to remain abreast with the significant developments impacting their profession.

At this juncture, I wish to thank CA. G. Ramaswamy, President and CA. Jaydeep N. Shah, Vice President for their continuous support and encouragement to the initiatives of the Board. I must also thank my colleagues from the Council at the Internal Audit Standards Board, *viz*., CA. Rajendra Kumar P., CA. Amarjit Chopra, CA. Shiwaji B. Zaware, CA. Ravindra Holani, CA. Anuj Goyal, CA. Nilesh Vikamsey, CA. Vijay K. Garg, CA. Atul C. Bheda, CA. J. Venkateswarlu, CA. Abhijit Bandyopadhyay, Shri Prithvi Haldea, Smt. Usha Narayanan, Smt. Usha Sankar, Shri Manoj Kumar and Shri Sidharth Birla for their vision and support. I also wish to place on record my gratitude for the co-opted members on the Board, *viz*., CA. Madhu Sudan Goyal, CA. Rohit Choksi, CA. Ketan Vikamsey, CA. Pankaj Kumar Adukia and CA. Umakant Balkrishna Joshi as also special invitees on the Board, *viz*., Mr. Anil Kumar Jain, CA. Ajay Minocha, CA. Sumit Behl and CA. R.Subramaniam for their invaluable guidance as also their dedication and support to the various initiatives of the Board.

I am sure that this publication would be warmly received by the interested readers and would be recounted in landmark publication of the Institute.

October 25, 2011
Mumbai

CA. Rajkumar S. Adukia
Chairman,
Internal Audit Standards Board

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Introduction

1. A calm mind is better focused than a turbulent one. Internal auditor exhibits supremacy with his systematic and a well laid out approach, which offers him clarity and edge in whatever he undertakes. There is no limit on his accomplishments. One can never tie him down for that is the power of his knowledge, proactive thought process and experience.

Internal Auditing has gained so much importance that conducting it has been made mandatory by regulators for listed and other specified companies.

2. Internal Audit began in modest manner during the Second World War when organisations found it difficult to maintain operational efficiency and control. Companies appointed special staff (i.e., present day internal auditors) to review operations and report to them. The task assigned to internal auditors varied from routine check on finance and operations to appraisal of financial and operational activities.

3. Earlier, internal audit was largely voluntary, management appointed internal auditors when they felt the need. With increased complexities in business, frauds and scams, internal audit has become essential for organisations. Be it Securities and Exchange Commission (SEC) in United States or Securities and Exchange Board of India (SEBI) in India, regulators are prescribing mandatory internal audit. The range of activities undertaken by internal audit teams has increased. They cover a whole gamut of operations ranging from review of finance and operations to providing assurance and consulting services.

4. The history of auditing provides the basis for analyzing the changes that have taken place in the audit objectives and techniques. A significant recent trend is towards increased reliance on internal controls and a decrease in detailed testing. The futuristic auditing process is said to be more of a procedural review together with the analysis of the effectiveness of internal controls, thereby offering a platform for the procedural appraisal of the system in place. Various factors that contribute to this development are rising cost of public accounting, expectations of the users of the financial statements, increasing complexity of the business enterprise and finally, the latest developments in the communication and information systems

Accounting System in the World – A Brief Introduction

5. Accounting dates back tens of thousands of years. In the days before computers, before pen and paper, even before numbers and writing were

invented, merchants used tokens and a clay ball called a bollae to keep track of their goods after they were shipped. As time passed, the tokens and bollae evolved into symbols and writing. Merchants would draw symbols on a clay tablet representing the goods in their shipment which they found easier instead of using tokens and the bollae. As with the bollae, the tablet was included with the shipment to be given to the recipient. The concept is the same - the tablet represented what was included in that shipment.

6. During the Renaissance era, (around 1300 to 1500), the Romans and Italians increased their trade tremendously. Accurate records were necessary to ensure the successful transportation and sales of their goods. Borrowing from Arabic numbers that existed during that time, the Romans and Italians used the Arabic numerical system and the Arabic basis of math to develop their own detailed accounting system. This evolved into the double-entry bookkeeping system that is used today.

The double-entry accounting system became the standard for accounting, largely due to an Italian Monk and mathematician named Luca Pacioli. In 1494, Luca Pacioli wrote a book entitled "*Summa de Arithmetica Geometria Proportioni et Proportionalita* which translates to "*Everything About Arithmetic, Geometry and Proportion".* This was his fifth book written about mathematics though it later became known as the first accounting text book.

Within the 36 chapters of his book, Pacioli detailed the use of journals, ledgers and accounts. The first 16 the chapters about double-entry accounting described the formation of the accounts and ledgers within the double entry system. The remaining chapters covered general business issues such as deposits and withdrawals, closing the books, and balancing the books. Pacioli warned that the most important thing a person could do with regards to double-entry accounting was *always make sure debits equaled credits!*

It was in Pacioli's chapters that the terms **Debit** and **Credit** came to be. Debit and Credit originated from the Latin word ***Debitore*** and ***Creditore*** which means "shall give" and "shall have", respectively. Debit and Credit, as they are known today, are also abbreviated as Dr. and Cr. The abbreviations stem from the Latin forms rather then the English forms. That is why Debit is abbreviated as "Dr". Within the double entry method of accounting, Pacioli stated that debits were always noted on the left side while credits were always noted on the right side. Pacioli's ledger and notes also included the major accounts used in accounting today - assets, liabilities, income (revenue), capital (equity) and expense. Within Pacioli's chapters, year end closing entries and trial balances were also documented. It was Pacioli who proposed that a trial balance be used to prove a balanced ledger (and therefore, balanced books). In addition to writing about the double-entry accounting system, Pacioli also included topics such as cost accounting in his chapters.

7. The double-entry accounting method also led to the creation of financial statements that are instrumental to accounting today. The only difference between Pacioli's writing and the modern-day accounting system is the introduction and use of computers (as compared to paper ledgers) and the words Debit and Credit written in English instead of Latin.

Financial Statements and Accounting Standards

8. The process of budget, accounts and audit was initiated in 300 years BC in India by guru of governance –"Arya Chanakya".

Budget

Revenue Budget

9. The chancellor shall first estimate the revenue [for the year] by determining the likely revenue from each place and each sphere of activity under the different heads of accounts, total them up by place or activity, and then arrive at a grand total.

10. Actual revenue shall then be estimated by adding receipts into the treasury for the current year and receipts on account of [delayed] payments due from the previous year and deducting from this the following:

- Expenditure on the king,
- Standard rations for other,
- Exemptions granted [by the king] by decree or orally, and
- Authorised postponments of payments into the treasury.

Outstanding revenue shall be estimated by taking into account the following: works under construction from which revenue will accrue only on completion, unpaid fines and penalties, dues not yet recovered, dues defiantly withheld and advances to be repaid by the officials; outstanding of little or no value shall be ignored.

[The net resources available to the state was thus calculated by estimating revenue during the year, adding outstanding dues of the previous year collected during the current year and subtracting from this total committed crown expenditure, remissions, uncollectables and loans and advances.]

Income, Expenditure and Balance

11. Actual income is to be calculated under the following headings:

(i) current income;

(ii) transferred income and

(iii) miscellaneous revenue.

12. *Current income* consists of receipts due and paid in the same year.

Transferred income is income from outstanding of earlier year as well as income earned [by one department] transferred to another.

Miscellaneous income is of three kinds:

(i) Recovery of debts and dues which were earlier written off, fines paid by government servants, additional income (from surcharges and unanticipated revenue), compensation collected for loss or damage, gifts, confiscated property, intestate property and treasure trove.

(ii) The following deductions from [anticipated] expenditure [are to be treated as income]: savings due to demobilisation of [a part of] the army, works abandoned before completion and economies made in [actual] investment as against original [planned] budget.

(iii) Income due to profit, on sales: increase in the price of a commodity at the time of sale, profit from the use of differential weights and measures and increased income due to competition from buyers.

13. Actual expenditure shall be shown under the following headings:

(i) budgeted day-to-day expenditure,

(ii) unbudgeted day-to-day expenditure,

(iii) foreseen periodic (fortnightly, monthly or annual) expenditure.

The [net] revenue is to be calculated after deducting expenditure from income, taking into account the actuals as well as deffered amounts (as referred to in "Kautilya - The Arthashastra" by L.N. Rangarajan and Verses 2.613-16, 2.617-27, 2.6.12, by R.P.Kangla).

14. In Europe around the year 1600, profit and loss statements and statements of balances began to emerge. These statements were created from the records kept within the double-entry accounting system that Luca Pacioli documented in his writings. The main reason for creating the financial statements was to obtain additional information about the business when merchants and businessman at the time were looking for more money

to fund their operations. Surprisingly, the purpose and concepts of financial statements has not changed much since that time.

15. Businesses continued to evolve and expand over the next hundred years. Soon the United States began conducting business with England. The increase in business transactions, especially between the two countries meant that more information was required about the businesses. In 1845, corporations were established in England. The development of corporations, including investors, stockholders, and involvement by others created the need for more accounting information. This led to the development of Accounting Standards and laws to ensure that corporate, officers are acting ethically and to provide those involved with the corporation the information they need to make sound business decisions. At the same time, the Industrial revolution occurring within the United States also required more formal practices and regulations as well as professional standards.

PART I
OVERVIEW OF INTERNAL AUDIT

History and Background of Internal Auditing

1.1 Auditing has been around since the beginning of human civilization. As the business world grew, auditing began to play more important roles. In the late 1800's and early 1900's, people began to invest money into large corporations. The Stock Market crash of 1929 and great depression demonstrated problems with capital markets, business practices, and yes, considerable deficiencies in accounting practices.

1.2 In 1930s, growth and expansion made it increasingly difficult for organizations to maintain control and operational efficiency. The World War further expanded organizations' responsibilities for scheduling, managing with limited materials and labourers, complying with government regulations, and an increased emphasis on cost finding. It was difficult for management to observe all the operating areas or be in touch with everybody. Then, special staff was appointed to report on happenings in the company who later came to be known as 'Internal Auditors'.

1.3 In 1958, the Institute of Chartered Accountants of England and Wales issued a statement entitled 'Accounting by Electronic Methods'. This statement referred to E.P.D. as "...the method of analyzing, marshaling, recording and reporting business information by means of equipment, the central feature of which is an electronic digital computer."

1.4 The evolution of auditing is a complicated history that always changed through historical events. Auditing always changed to meet the needs of the business environment of that day.

The internal auditing function varied greatly between organisations and a number of internal auditors pushed vigorously for greater understanding and recognition of the internal auditing function. One such person was John B. Thurston, head of the internal auditing function at the North American utility company. He is credited with being the person most responsible for the creation of The Institute. He was joined by Robert B. Milne, general auditor of the Columbia Engineering Corporation, and Victor Z. Brink, a former auditor and Columbia University educator who authored the first major book on internal auditing. They gathered friends and associates from the utilities industries, public accounting firms, and other industries, 25 of whom agreed to participate in forming a new organization for internal auditors.

1.5 The historical development of auditing can be reviewed into the following five chronological periods:

(i) Prior to 1840;

(ii) 1840s-1920s;

(iii) 1920s-1960s;

(iv) 1960s-1990s; and

(v) 1990s–present.

Prior to 1840

1.6 The process audit, timely submission of accounts and audit, was initiated by Arya Chanakya in 300 BC.

Accounts [in the accounts books,]

Every entry shall have the date of transaction. On the receipt side, the revenue shall be classified according to the major heads of accounts as given below:

- cost price, share {bhaga},
- transaction tax {vyaji},
- monopoly taxes,
- fixed taxes, manufacturing charges,
- fines and penalties.

On the debit side, expenditure shall be classified according to the major heads as given below:

- Worship (of gods and ancestors) and charitable expenses.
- The place [expenditure of the king, queens, princes etc.]
- Administration.
- Foreign affairs.
- Maintenance of granary, ordnance depots and warehouses for commodities and forest produce (under separate subheads).
- Manufacturing expenses.
- Labour charges.
- Defence (with separate subheads for each of the four wings).
- Cattle [and pastures].
- Forests and game sanctuaries.
- [consumables like] firewood and fodder.

Form of Accounts

Income side

Place	Period of accounting	Date and time of receipt	Head of account	Current year of outstanding dues	Quantity received	Name of payer	By whose order	Received by	Recorded by
1	2	3	4	5	6	7	8	9	10

Expenditure Side

Place	Period of accounting	Date and time of payment	Head of expenditure	Counter value received	Occasion	What was paid	Amount paid	For what use	Authorising payment	Stores withdrawn	Delivered by	Received by
1	2	3	4	5	6	7	8	9	10	11	12	13

Balance Columns

Place	Date and time	Head of account	O/s dues left	Form in which balance received into treasury	Quality	Amount received	Details of container	Delivered to
1	2	3	4	5	6	7	8	9

Proper Maintenance of Account Books

All accounts shall be maintained in the proper form and legibly written without corrections. Failure to do so shall be a possible offence.

Timely Submission of Accounts

Monthly Accounts

Day-to-day accounts [to be submitted once a month] shall be presented before the end of the following month and late submission shall be penalised.

Accounts of Specific Transactions

if the net balance to be remitted to the treasury is small, a grace of five days shall be allowed for making the remittance. If the accounts are delayed [beyond five days], the net balance shall first be remitted to the treasury and then a thorough audit done taking into account the rules of business, [relevant] precedents, the circumstances and the calculations: a physical verification of the work shall be carried out. Whether the smallness of the remittance was justified or not shall then be judged by interfence [supplemented] by information from secret agents.

Audit

Responsibility of Account Officers

1.7 Accounts officers shall:

- Present themselves for audit at the appointed time bringing with them their account books and the income to be remitted to the treasury;
- Be ready for audit when the auditor officer calls him;
- Not lie about the accounts [when questioned during audit]; and
- Not try to interpolate an [omitted] entry as if it was forgotten [inadvertenly.]
- Failure to confirm to any of the above is a punishable offence.
- In case a discrepancy is discovered during audit:
    - the official concerned shall pay a penalty if the discrepancy has the effect of either showing a higher actual income or a lower actual expenditure[in both the state being the loser].
    - the official shall keep the difference for himself in the converse case [where a lesser amount than the one shown by the official is actually due to the state].

Responsibility of Auditors

1.8 An auditor shall be ready when an accounts officer presents himself for audit; otherwise, he shall be punished.

Responsibility of High Officials

1.9 High officials shall be responsible for rendering the accounts in full for their sphere of activity without any contradiction in them. Those who tell lies or make contradictory statements shall pay the highest level standard penalty.

(As referred to in "Kautilya - The Arthashastra" by L.N.Rangarajan. Verses 2.7.35, 2.7.26.27, 2.7.28.29, 2.7.21-23.39.40, 2.7.19,20, 2.7.22, 2.7.25. (by R.P.Kangla)

Generally, the early historical development of auditing is not well documented. Auditing in the form of ancient checking activities was found in the ancient civilizations of China, Egypt and Greece. The ancient checking activities found in Greece (around 350 B.C.) appear to be closest to the present day auditing.

1.10 Similar kinds of checking activities were also found in the ancient Exchequer of England. When the Exchequer was established in England during the reign of Henry 1(1100-1135), special audit officers were appointed to make sure that the state revenue and expenditure transactions were properly accounted for. Likewise, the existence of checking activities was found in the Italian City States. The merchants of Florence, Geneo and Venice used auditors to help them to verify the riches brought by captains of sailing-ships returning from the Old World and bound for the European Continent. Again, auditing in this period was concerned about detection of fraud. The audit found in the City of Pisa in 1394 was somehow similar to those found in the Italian City State. It was meant to test the accounts of government officials to determine whether or not defalcation had taken place.

1.11 According to Porter, auditing had little commercial application prior to the industrial revolution. This is because industries during this period were mainly concerned with cottages and small mills which were individually owned and managed. Hence, there was no need for the business managers to report to owners on their management of resources. The concept of testing or sampling was not part of the auditing procedure. The existence of internal control is also unknown. In a nutshell, in the period pre-1840, the auditing at the time was restricted to performing detailed verification of every transaction.

Period from 1840s-1920s

1.12 The practice of auditing did not become firmly established until the advent of the industrial revolution during the period 1840s-1920s in the UK. According to Brown, the large-scale operations that resulted from the industrial revolutions drove the corporate form of enterprise to the foreground. Large factories and machine-based production were established. As a result, a vast amount of capital is needed to facilitate this huge amount of capital expenditure. The emergence of a "middle class" during the industrial revolution period provided the funds for the establishment of large industrial and commercial undertakings. However, the share market during this period was unregulated and highly speculative. As a consequence, the rate of financial failure was high and liability was not limited. Innocent investors were liable for the debts of the business. In view of this environment, it was apparent that the growing number of small investors was in dire need of protection. Hence, the time was ripe for the profession of auditing to emerge.

1.13 In response to the socio-developments in the UK during this period, the Joint Stock Companies Act was passed in 1844. The Joint Stock Companies Act stipulated that "Directors shall cause the Books of the Company to be balanced, and a full and fair Balance Sheet to be made up". In addition, the Act provided the appointment of auditors to check the accounts of the company. However, the annual presentation of the balance sheet to the shareholders and the requirement of a statutory audit were only made compulsory in 1900 under the Companies Act 1862 (UK).

1.14 According to Porter, et al (2005) the accountant particularly in the early years of this period, was normally the company manager and his duties were to ensure proper use of the funds entrusted to him. The auditors during this period were merely shareholders chosen by their fellow members. The auditors during this period were required to perform complete checking of transactions and the preparation of correct accounts and financial statements. Little attention was paid to internal control of the company.

1.15 The objectives of auditing were:

(i) the detection of fraud;

(ii) the detection of technical errors, and

(iii) the detection of errors of principles.

It can be concluded that the role of auditors during the period of 1840s-1920s was mainly on fraud detection and the proper portrayal of the company's solvency (or insolvency) in the balance sheet.

Period from 1920s-1960s

1.16 The growth of the US economy in the 1920s-1960s had caused a shift of auditing development from the UK to the USA. In the years of recovery following the 1929 Wall Street Crash and ensuing depression, investment in business entities grew rapidly. Meanwhile, the advancement of the securities markets and credit-granting institutions had also facilitated the development of the capital market in this period. As companies grew in size, the separation of the ownership and management functions became more evident. Hence to ensure that funds continued to flow from investors to companies, and the financial markets function smoothly, there is a need to convince the participants in the financial markets that the company's financial statement provide a true and fair portrayal of the relevant company's financial position and performance.

In view of the economic condition, the audit function was mainly to provide credibility to the financial statements prepared by company managers for their shareholders. Consensus were generally achieved that the primary objective of an audit function is adding credibility to the financial statement rather than on the detection of fraud and errors. Such a change in audit objective is evidenced in successive edition of Montgomery's Auditing text issued during this period which stated "An incidental, but nevertheless important, objective of an audit is detection of fraud." "Primary responsibility…for the control and discovery of irregularities necessarily lies with management." Hence, it can be witnessed that the shift of the focus of an audit function from preventing and detecting fraud and error towards assessing the truth and fairness of the companies' financial statements began at this period.

1.17 The concept of materiality and sampling techniques were used in auditing during this period. The development of material concept and sampling technique was due to the voluminous transactions involved in the conduct of business by large corporations operating in widespread locations. It is no longer practical for auditors to verify all the transactions. Consequently, sampling and the development of judgment of materiality were essential. The use of sampling technique during this period can be proven from the following statement of Short "… it is not necessary to make a detailed examination of every entry, footing, and posting during the period in order to get the substance of the value which resulted from an audit".

Corresponding to the use of sampling techniques, auditors need to rely on internal control of the company to facilitate the use of such research approach. The fundamental principles of auditing during this period were influenced by some major auditing cases such as the case of McKesson and Robbins. The verdict of this case had resulted in the emphasis of physical observation of assets such as cash and stock, and the use of external evidence. In addition, the Royal Mail case highlighted the need of audit for the profit and loss statements. However, the audit of profit and loss account was only made mandatory with the enactment of Securities and Exchange Commission Act 1934 in the USA and The Companies Act 1948 in the UK.

In short, the social-economic condition in the period had highly influenced the development of auditing. As highlighted by Porter, the major characteristics of the audit approach during this period, among others, included:

(i) reliance on internal control of the company and sampling techniques were used;

(ii) audit evidence was gathered through both internal and external source;

(iii) emphasis on the truth and fairness of financial statements;

(iv) gradually shifted to the audit of Profit and Loss Statement but Balance Sheet remained important;

(v) physical observation of external and other evidence outside the "book of account".

Period from 1960s to 1990s

1.18 The world economy continued to grow in the 1960s-1990s. This period marked an important development in technological advancement and the size and complexity of the companies. Auditors in the 1970s played an important role in enhancing the credibility of financial information and furthering the operations of an effective capital market. Similar description on the auditors' role was found in *The New York Times* on 6 April 1975 that the duties of auditors, among others, were to affirm the truthfulness of financial statements and to ensure that financial statements were fairly presented. Hence, the role of auditors with regard to the audit of financial statement generally remained the same as per the pervious period.

1.19 Despite the overall audit objectives remaining similar, Davies (1996) opines that auditing had undergone some critical developments in this period. In the earlier part of this period, a change in audit approach can be observed from "verifying transaction in the books" to "relying on system". Such a change was due to the increase in the number of transactions which resulted from the continued growth in size and complexity companies where it is unlike for auditors to play the role of verifying transactions. As a result, auditors in this period had placed much higher reliance on companies' internal control in their audit procedures. Furthermore, auditors were required to ascertain and document the accounting system with particular consideration to information flows and identification of internal controls. When internal control of the company was effective, auditors reduced the level of detailed substance testing.

1.20 In the early 1980 there was a readjustment in auditors' approaches where the assessment of internal control systems was found to be an expensive process and so auditors began to cut back their systems work and make greater use of analytical procedures. An extension of this was the development during the mid-1980s of risk-based auditing. Risk-based auditing is an audit approach where an auditor will focus on those areas which are more likely to contain errors. To adopt the use of risk-based auditing, auditors are required to gain a thorough understanding of their audit clients in term of the organization, key personnel, policies, and their industries. Hence, the use of risk-based auditing had placed strong emphasis on examining audit evidence derived from a wide variety of sources, i.e. both internal and external information for the audit client.

1.21 Most of the companies in this period had introduced computer systems to process their financial and other data, and to perform, monitor and control many of their operational and administrative processes. Similarly, auditors placed heavy reliance on the advanced computing auditing tool to facilitate their audit procedures. In addition to the auditing of financial statement, auditors at the same time were providing advisory services to the audit clients.

Period from 1990s - Present

1.22 The auditing profession witnessed substantial and rapid change since 1990s as a result of the accelerating growth at the world economies. It can be observed that auditing in the present day has expanded beyond the basic financial statement attest function. Present-day auditing has developed into new processes that build on a business risk perspective of their clients. The business risk approach rests on the notion that a broad range of the client's business risks are relevant to the audit.

1.23 Many business risks, if not controlled, will eventually affect the financial statement. Furthermore by understanding the full range of risks in business, the auditor will be in a better position to identify matters of significance and relevance to the audit profession on a timely basis. Since the early 1990s, the audit profession began to take more responsibility to detect and report fraud and to assess, and report more explicitly, doubts about an auditee's ability to continue in conformance with society's and regulators' increasing concern about corporate governance matters. Adoption of the business risk approach in turn enhances auditor's ability to fulfill these responsibilities.

1.24 Presently, the ultimate objective of auditing is to lend credibility to financial and non-financial information provided by management in annual reports; however, audit firms have been largely providing consultancy services to businesses. By 2000, consulting revenues exceeded auditing revenues at all the major audit firms in the USA.

1.25 Regulators of the auditing profession and the investing public began to doubt whether audit firms could remain independent on audit issues when the firms were so dependent on consulting revenues. The quality of audits is being placed under scrutiny after a series of financial scandals of public companies such as Sunbeam, Waste Management, Xerox, Adelphia, Enron and WorldCom. The collapses of these giant corporations had brought about a crisis of confidence in the work of auditors.

1.26 As a consequence of the high level of litigation and criticism against the auditors, nearly all large accounting firms split their consulting arms into separate companies and made announcements on their more stringent rules and measures to ensure better independence and audit quality. In addition, a spate of radical reforms was undertaken in various countries by the accounting bodies, governments, stock exchange commissions and academics to strengthen the audit practice. Some of the key reform activities include:

(1) *The Sarbanes Oxley Act (The US)*: In response to the fall of Enron 'the Sarbanes'-Oxley Act was implemented. It outlines the rules on auditor independence, for example, the control of audit quality, and the rotation of audit partners as well as the prohibition of conflict-of-interest situation. Furthermore, the act also requires auditors to report to the audit committee those significant matters. The Public Company Accounting Oversight Board which oversees audit firms and their procedures and the enforcement of accounting standards is also established as a result of this act.

The Sarbanes-Oxley extended the duties of auditor to audit the adequacy of internal controls over financial reporting. This is in view of the fact that a number of commissions recognized the importance of internal control in preventing financial statement misstatement.

(2) *Ramsay Report (Australia)*: As a result of the collapse of HIH Insurance Ltd, the Australian Government Commission engaged professor Ian Ramsay to investigate the issue of auditor independence. It was recommended that auditor independence can be improved through the following ways:

- Include a statement in the Corporations Act that auditors are to be independent;
- Require auditors to declare to the Board of Directors that their independence is maintained;
- Prohibit special relationships between the auditor and client;
- Establish an auditor independence supervisory board;
- Establish an audit committee to oversee the issue of non-audit services, audit fees, scope disagreements and auditor-client relationships.

Although the overall audit objectives in the present period remained the same, i.e., lending credibility to the financial statement, critical changes have been made to the audit practice as a result of the extensive reform in various countries. Such reform has implicated the auditing profession in the following ways:

(i) The role of auditors is expected to converge, refocusing on the public interest, redefining audit relationship, ensuring integrity of financial reports, separation of non-audit function and other advisory services;

(ii) The audit methods revert to basics i.e., risk attention, fraud awareness, objectivity and independence, and

(iii) Increase attention on the needs of financial statement users.

In summary, the review of the historical development of auditing has evolved the audit function through a number of stages. Auditing first emerged in the form of ancient checking activities in the ancient civilizations of China, Egypt and Greece. However, the practice of modern auditing did not become firmly established until the advent of the industrial revolution in the mid nineteenth century in the UK. The audit practice in the mid 1800s to early 1900s can be regarded as "conformance role of auditing" as auditing was mainly concerned with ensuring the correctness of accounts and detecting frauds and errors.

1.27 Over the past 30 years or so, the auditor played an "enhancing role" by enhancing the integrity and credibility of financial information. Today, auditors are expected not only to enhance the credibility of the financial statement, but also to provide value-added services, such as, reporting on irregularities, identifying business risks and advising management on the internal control environment. However, extensive reforms were implemented in various countries as a result of the collapse of big corporations; it is expected that the role of auditors will converge. It is claimed that the role of auditors has moved from "mere conformance through an enhancing role to a convergence role". It is evident that the paradigm of independent auditing has shifted over the years. It is believed that it may continue to shift in the future.

1.28 A review of the historical development of auditing has shown that the objective of auditing and the role of auditors are constantly changing as they are highly influenced by contextual factors, such as, the critical historical events (e.g., the collapsed of big corporations), the verdict of the courts, and technological developments (e.g., advancement of computing systems and CAATs). It can be observed that any major changes in these contextual factors are likely to cause a change in the audit function and the role of auditors. As a result, auditing is seen to be evolving at all times.

The business environment is constantly changing and new threats and vulnerability emerge every day.

Definition of Internal Audit

1.29 *Preface to the Standards on Internal Audit,* issued by the Institute of Chartered Accountants of India, amply reflects the current thinking as to what is an internal audit:

"Internal audit is an independent management function, which involves a continuous and critical appraisal of the functioning of an entity with a view to suggest improvements thereto and add value to and strengthen the overall governance mechanism of the entity, including the entity's strategic risk management and internal control system."

Highlights of the Definition

- Internal audit is a management function.
- Independence permits internal auditors to render impartial judgments.
- The role of internal audit is a dynamic one.
- Internal Audit assists board in governance responsibility.
- Internal auditor assures the effectiveness of internal audit.
- Internal audit as a function is a component of internal control, ensuring the other controls are designed and adhered to.

Committee of Sponsoring Organisations (COSO)

1.30 The Committee of Sponsoring Organizations' (COSO) mission is to provide thought leadership through the development of comprehensive frameworks and guidance on enterprise risk management, internal control and fraud deterrence designed to improve organizational performance and governance and to reduce the extent of fraud in organizations.

COSO's vision is to be a recognized thought leader in the global marketplace on the development of guidance in the areas of risk and control which enable good organizational governance and reduction of fraud.

Scope of Internal Audit

1.31 The scope of internal auditing within an organization is broad and may include areas, such as, the efficacy of operations, the reliability of financial reporting, deterring and investigating fraud, safeguarding assets, and compliance with laws and regulations:

- Internal audit is playing a significant and critical role in evaluating the adequacy of internal controls and assessing the extent of compliance with the applicable laws and regulations, policies and procedures and suggesting ways to reduce the costs and promote efficiency.
- Internal audit began as an extended arm of an external/ statutory audit of financial statements. The main, but rather restricted, function of the internal audit at this stage was verifying the reliability of the financial information included in the financial statements. The internal audit function in this stage of evolution could not understandably add much value to functioning of the entity.
- With the evolution of new concepts in the field of auditing, internal audit was also required to test non-financial information and transactions in terms of their correctness and compliance with the laid down policies and procedures.
- Internal audit slowly emerged as an inevitable service that could assist management in decision making, moving away from being merely a police on financial transactions.
- Internal audit is undeniably the backbone of a sound corporate governance system today.
- While external auditors start with financial statement ending result, internal auditors start with the basic activities and work forward to achieve organisational objectives.
- Co-ordination of internal and external audit work increases economy, efficiency, and effectiveness of the overall audit process.

Need for Internal Audit

1.32 The need for Internal Audit arises because of the following:

- Increased complexity of businesses
- Enhanced compliance requirements
- Focus on risk management and internal controls to manage them
- Unconventional business models
- Intensive use of information technology
- Stringent norms mandated by regulators to protect investors

- An increasingly competitive environment

Internal Audit Cycle

- Pre engagement activity
- Understanding the work
- Assurance plan
- Substantive work
- Report

PART II
PROCEDURAL ASPECTS OF INTERNAL AUDIT

Organizing Internal Audit Function

2.1 The internal audit function may be carried out by in-house staff or an outsourced team. Whether internal audit is a part of the organisation or not, would depend on:

- Business of the organisation
- Geographical locations
- Culture of the organisation
- Control risks
- Environment

2.2 To be effective, it needs a strong leader who has the support of both the authorising body, i.e., audit committee, in most cases, and senior management. The Chief Audit Executive must be a person who understands the overall organisation and has the qualities of a leader:

- Keeps the vision clear
- Co-ordinate activities
- Mediate conflicts
- Identify needed resources
- Manage the budget
- Assure that goals are achieved on time and on budget

2.3 The first step, a chief auditing executive should take, to establish an internal audit system is to reach an understanding with management and the board of directors on the rules that will apply to the internal audit system. This understanding should be in writing in the form of a charter.

Managing Internal Audit Function

2.4 Internal Audit needs a mission statement or audit charter outlining the purpose, objectives, organisation, authorities, and responsibilities of the internal auditor, audit staff, audit management, and the audit committee. A big part of the management profession is creating and enforcing policies and procedures. Policies interpret and tailor laws that apply to an organisation; serving as a written record for good practices the management wants to emphasize and enforce in the organisation, whether or not there are legal implications. While policies are general, procedures are specific.

Internal Audit Planning

2.5 Every audit assignment should be planned carefully prior to its start. Circumstances may occur which might call for unscheduled reviews or there might be pressures to begin special audit without delay. However, a properly planned audit will almost always have better audit results. A long-range audit plan should be developed which should be reviewed at regular intervals.

Pre Engagement Activity

Matters to be considered before accepting new assignment would be:

(i) Gathering information on the integrity, competence of the management.

(ii) Past experience, if any, with the management.

(iii) Communication with previous auditors.

(iv) Significant accounting policies of the client.

(v) Assessment of Management's ability to have effective and efficient internal control.

(vi) Financial viability of the entity.

The auditor should consider the following matters while planning:

(i) Nature of work

(ii) Knowledge of business

(iii) Policies and procedures of the entity

(iv) The methods used by the entity to process significant accounting information, including the use of service organisations, such as outside service centers.

(v) Preliminary judgment about materiality levels for audit purposes.

(i) Understanding the Nature of Work

The various sources would be:

- Likely impact of applicable accounting and auditing pronouncements.
- Financial statements of the entity.
- Prior internal audit reports, external audit reports and reports of any special audits or investigation of the area assigned.
- Discuss with auditee:
- Changes in accounting methods or policies.

- Changes in information processing methods.
- Timing of preliminary audit work, confirmation procedures.
- Assistance required from client personnel.
- Records required.
- Facilities required like physical space, computer systems etc.

(ii) Knowledge of Business

- Review the prior audit reports
- Policy and procedure manual, org chart, flowcharts etc.
- Review financial statements or reports filed with various agencies or regulatory bodies
- Minutes of meetings of stockholders, the board of directors and relevant committees
- Effect of various laws and regulations on financial statement of auditee
- Information about nature of entity's business
- Client correspondence file
- Gain an understanding of type of business, products & services, capital structure, offices/branches/factories
- Obtain knowledge of auditee's industry like economic condition, government regulations, competition, financial trends.
- Other external sources such as industrial publications, ICAI standards and guidance etc.

(iii) Methods used by Entity to Process Information

The methods used need to be considered as the methods influence the design of internal control. The extent of computer processing and the complexity of processing will influence nature, timing and extent of audit procedures.

(iv) Determining Audit Objectives

Objectives based on management's needs, nature of prior work, available resources and time is an important aspect of planning. General objectives would be part of audit plan and they should be re-examined before each audit and defined in detail before each audit.

(v) Audit Scheduling

On the basis of annual plan and preliminary survey the manpower requirements and time budgets need to be fixed. The following factors need to be considered:

- Nature of audit
- Complexity of work
- Staff availability
- Special skills required
- Audit period

(vi) The auditor should consider whether specialized skills are needed for any area, such as, the effect of computer processing on the audit, to understand the controls, or to design and perform audit procedures. If specialized skills are needed, the auditor should seek the assistance of a professional possessing such skills.

Annual Audit Plan

1. Prepare Annual Internal Audit Plan

- Conduct a preliminary risk assessment in cooperation with the senior and line management.
- Prepare a Draft Annual Internal Audit Plan based upon the results of the risk assessment process.
- Discuss with audit committee and get a formal approval.
- Review the plan on a quarterly basis to ensure that focus remains on high risk areas.

2. Communicate Annual Internal Audit Plan

- Distribute the Annual Internal Audit Plan to senior and line managers.
- Keep senior and line managers informed of any changes to the Annual Internal Audit Plan.

Specific Audit Plan

- Issue notice to auditee and arrange a meeting.
- Identify information or documents required initially.

- Find out whether there are areas which management would like to be included in the audit.
- Discuss, finalise and inform auditee:
  - Audit period
  - Estimated start date and duration
  - Names of audit staff
  - Facilities required like space, computer systems, etc.

Importance of Effective Internal Control Process

2.6 A company's system of internal control has a key role in the management of risks that are significant to the fulfillment of its business objectives. A sound system of internal control contributes to safeguarding the shareholders' investment and the company's assets.

Internal control facilitates the effectiveness and efficiency of operations, helps ensure the reliability of internal and external reporting and assists compliance with laws and regulations. Effective financial controls, including the maintenance of proper accounting records, are an important element of internal control. They help to ensure that the company is not unnecessarily exposed to avoidable financial risks and that financial information used within the business and for publication is reliable. They also contribute to the safeguarding of assets, including the prevention and detection of fraud.

A company's objectives, its internal organisation and the environment in which it operates are continually evolving and, as a result, the risks it faces are continually changing. A sound system of internal control, therefore depends on a thorough and regular evaluation of the nature and extent of the risks to which the company is exposed. Since profits are, in part, the reward for successful risk taking in business, the purpose of internal control is to help manage and control risk appropriately rather than to eliminate it.

Business Related Knowledge

2.7 Standard on Internal Audit (SIA) 15,.***Knowledge of the Entity and its Environment*** issued by Institute of Chartered Accountant of India states that ***in performing an internal audit engagement, the internal auditor should obtain knowledge of the economy, the entity's business and its operating environment, including its regulatory environment and the industry in which it operates, sufficient to enable him to review the key***

risks and entity-wide processes, systems, procedures and controls. The internal auditor should identify sufficient, appropriate, reliable and useful information to achieve the objectives of the engagement. *Such knowledge is used by the internal auditor in reviewing the key operational, strategic and control risks and in determining the nature, timing and extent of internal audit procedures.*

Acquiring Knowledge of Entity's Operations and Environment

2.8 ***Prior to accepting an engagement, the internal auditor should obtain a preliminary knowledge of the industry and of the nature of ownership, management, regulatory environment and operations of the entity subjected to internal audit, and should consider whether a level of knowledge of the entity's business adequate to perform the internal audit can be obtained.***

Following the acceptance of the engagement, further and more detailed information should be obtained. To the extent practicable, the internal auditor should obtain the required knowledge at the commencement of the engagement. As the internal audit progresses, that information should be assessed, enhanced, updated, refined and validated as the internal auditor and the engagement team obtain more knowledge about the entity's business

2.9 ***The internal auditor should obtain sufficient, appropriate information about the entity, specifically the following aspects:***

(a) ***Relevant industry, regulatory, and other external factors including the applicable financial reporting framework.***

(b) ***Relevant industry factors include industry conditions such as the competitive environment, supplier and customer relationships, and technological developments. Relevant regulatory factors include the regulatory environment. The regulatory environment encompasses, among other matters, the applicable financial reporting framework and the legal and political environment.***

(c) ***The nature of the entity to enable the internal auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements.***

(d) ***Business operations.***

(e) ***Investments and investment activities.***

(f) ***Financing and financing activities.***

(g) ***Financial reporting***

(h) ***The entity's selection and application of accounting policies, including the reasons for changes thereto. The internal auditor should evaluate whether the entity's accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry.***

(i) ***The entity's objectives and strategies, and those related business risks that may result in risks of material misstatement. The entity conducts its business in the context of industry, regulatory and other internal and external factors. To respond to these factors, the entity's management or those charged with governance define objectives, which are the overall plans for the entity. Strategies are the approaches by which management intends to achieve its objectives. The entity's objectives and strategies may change over time.***

(j) ***Business risk is broader than the risk of material misstatement of the financial statements, though it includes the latter. Business risk may arise from change or complexity. A failure to recognise the need for change may also give rise to business risk. Business risk may arise, for example, from:***

- ***The development of new products or services that may fail;***
- ***A market which, even if successfully developed, is inadequate to support a product or service; or***
- ***Flaws in a product or service that may result in liabilities and reputational risk.***

An understanding of the business risks facing the entity increases the likelihood of identifying risks of material misstatement in the information subject to internal audit.

Knowledge of Processes

2.10 When an organization sets corporate objectives and goals, it must follow the appropriate procedures to make sure those goals are reached. Internal auditor reviews operations closely, confirming that the correct protocol is being followed and the goals are being met. This is vital to the organization's health and well-being.

2.11 The internal auditors must be well versed with the objectives of their organization and have the ability to examine and analyze to make sure operations are effective. After investigating the process, they report their findings and recommend appropriate courses of action. They may also have to establish criteria, based on their objective opinion, for meeting their organization's goals.

2.12 Competent professional internal auditors accurately interpret facts and figures of the organizational process quickly and strive for continuous improvement. Through a strong commitment to the organization's corporate values and goals, their understanding of the "big picture" plays a crucial role in the overall success of the organization.

2.13 Today, internal auditors work closer than ever with their customers. By doing so, they can be more accurate in their recommendations and help the organization adhere more closely to its objectives. As valuable resources for internal processes and operations, internal auditors continue to prove themselves as vital.

Field Survey

2.14 This is very critical step as it allows auditor to determine the scope and extent of audit effort. It is done prior to detailed testing and analysis. The auditors can familiarise themselves with the system and control structure. Typically, the audit team would consider:

- The organizational structure and the responsibilities of key members.
- Manuals of policies and procedures and applicable regulations.
- Management reports and minutes of meeting.
- Walkthrough of activity
- Discussions with key personnel

The field survey is the initial contact point and might take one or two days depending on the size of the audit.

The completion of field survey helps the auditor to understand key systems and processes. If the information during preliminary audit planning is imperfect, the audit team can make adjustments to planned audit scope.

Internal Audit Programme

2.15 After the conclusion of preliminary survey, the auditor has a fair idea of the audit objectives and the control systems. At this stage, the audit programme should be made providing the proposed procedures, budgeting and basis for controlling the audit. The audit programme will prevent the auditor from going off the scope pursuing irrelevant items and help in completing the audit project in an efficient manner.

Things to be Considered while Preparing Audit Programme

- Needs of potential users of the audit report.
- Legal and regulatory requirements.
- Management controls.
- Significant findings and recommendations from previous audits that could affect the current audit objectives. Also determine whether corrective action has been taken and earlier recommendations implemented.
- Potential sources of data that could be used as audit evidence and consider the validity and reliability of these data.
- Consider whether the work of other auditors and experts may be used to satisfy some of the audit objectives.
- Provide sufficient staff and other resources to do the audit.
- Criteria for evaluating areas under audit.

Framing the Programme

- Review the results of preliminary survey with audit supervisor.
- The audit team holds a meeting with the audit supervisor to decide on the priority / high risk areas and tests to be conducted.
- Provide a general overview of the auditee's operations. Include in the narrative statistical and monetary information, locations, authority, staffing and main duties and responsibilities.
- The programme should consist of detailed directions for carrying out the assignment.
- Prepare draft audit programme and document transaction flows.
- Audit programmes should be consistent. Some organisation’s may have standardised audit programmes.
- It should contain an estimate of the time necessary to complete the project
- Number the audit programme steps consecutively.

- Have the final programme reviewed by Audit supervisor and Audit manager.
- All major changes must be documented in writing and the reason documented.
- The audit programme should contain a statement of the objectives of the area being reviewed. These objectives would be achieved through the detailed audit programme procedure. Objectives should fit within the overall scope of the audit.
- Every audit procedure should help answer one of the objectives and every objective should be addressed in the procedures or steps.
- The tests have to be designed in such a manner that they achieve their objectives. Use imagination, ingenuity and intelligence in creating audit steps responsive to objectives.
- The goals should be made amply clear by prefacing major steps with : to test whether . . .; or to determine that . .

Time Budget

2.16 At the planning phase, an estimated time budget should be prepared to control the audit and complete it efficiently. The detailed project time budget should be completed at the conclusion of the preliminary review. The time budget should be approved by the audit manager and audit administration. This budget will include all time necessary to complete the audit, from assignment through issuance of the final report.

Planning should continue throughout the audit. Audit objectives, scope, and methodologies are not determined in isolation. They have to be determined together, as the considerations in determining each often overlap.

Audit Evidence

2.17 Evidential matter obtained during the course of the audit provides the documented basis for the auditor's opinions, findings, and recommendations as expressed in the audit report.

Types of Audit Evidence

Evidence may be categorized as physical, documentary, testimonial, and analytical.

Test of Evidence

Internal auditors are obligated by professional standards to collect *sufficient, competent, relevant*, and *useful* information to provide a sound basis for audit findings and recommendations.

They would usually hold true but they might not be valid in all cases.

a. Evidence obtained from a credible third party is more reliable than that secured from the auditee.

b. Evidence developed under an effective system of management controls is more competent than that obtained where such controls are weak or nonexistent.

c. Evidence obtained by the auditors themselves through direct physical examination, observation, computation, and inspection is more competent than evidence obtained indirectly.

d. Original documents provide more competent evidence than copies.

e. Person providing the evidence: Information obtained from a person having knowledge of the area would be more reliable

f. Objective evidence would be more reliable than the evidence which require judgment.

The sufficiency, competence and relevance of evidence depends on the source of information.

Audit Procedure

2.18 Programme step procedures should be in enough detail so that an experienced auditor could carry out the task with normal supervision. An audit causes disruption and interruptions in the day-to-day operations of an enterprise and it is advisable that the auditors provide a tentative schedule of the planned audit work (unless it is a surprise audit). Documentation should be kept for each step that would generally be in the form of working papers.

Review and Evaluation of Internal Control Environment

2.19 The auditor will have to review the internal control structure .The effectiveness and efficiency of the internal control will determine the extent of tests to be performed. This evaluation will also provide assurance on whether the systems are functioning properly. The auditor should provide for tests in the audit programme which could be in the form of interviews, internal control questionnaires, checklists, audit tests.

Matters to be Considered while Evaluating Internal Controls:

- Identification of risks.
- Internal control structure put in place to prevent, detect, correct undesired events.
- Whether the control structure is functioning as desired.
- Identification of weaknesses in the structure and their effect on auditing procedures.

Procedures to Evaluate Internal Controls

- Description of system of internal control.
- Flowcharts.
- Internal Control Questionnaires.
- Tests of compliance are performed to obtain sufficient evidence that the system is operating in accordance with the understanding the auditor obtained from the review. The nature, timing, and extent of tests of compliance are closely related to the control procedures and methods studied by the auditor.

Communication of Internal Auditor with Management

2.20 *Standard on Internal Audit (SA) 9,* ***Communication with Management*** issued by the Institute of Chartered Accountant states that ***the internal auditor while performing audit should:***

a. ***Communicate clearly the responsibilities of the internal auditor, and an overview of the planned scope and timing of the audit with the management;***

b. ***Obtain information relevant to the internal audit from the management;***

c. ***Provide timely observations arising from the internal audit that are significant and relevant to their responsibility as described in the scope of the engagement to the management; and***

d. ***Promote effective two-way communication between the internal auditor and the management.***

Matters to be Communicated

The Internal Auditor's Responsibilities in Relation to the Terms of Engagement

2.21 The internal auditor is responsible for performing the internal audit in accordance with the terms of engagement.

Planned Scope and Timing of Internal Audit

2.22 Communication regarding the planned scope and timing of the internal audit may:

a. Assist the management:

- *to understand better the objectives of the internal auditor's work;*
- *to discuss issues of risk and materiality with the internal auditor; and*
- *to identify any areas in which they may request the internal auditor to undertake additional procedures;*

b. Assist the internal auditor to understand better the entity and its environment.

2.23 When communicating to management about planned scope and timing of the internal audit, the internal auditor would need to ensure that such communication does not reduce the effectiveness of internal audit. For example, communicating the nature and timing of detailed audit procedures may make those procedures predictable.

2.24 Matters communicated may include:

- *How the internal auditor proposes to address the significant risks of material misstatement, whether due to fraud or error.*
- *The internal auditor's approach to internal control relevant to the internal audit.*
- *The application of materiality in the context of an internal audit.*

2.25 Communication with management may assist the internal auditor to plan the scope and timing of the internal audit. It does not, however, change the internal auditor's sole responsibility to establish the overall internal audit strategy and the internal audit plan, including the nature, timing and extent of procedures necessary to obtain sufficient appropriate audit evidence.

2.26 Clear communication of the internal auditor's responsibilities, the planned scope and timing of the internal audit, and the expected general *content of communications helps establishing the basis for effective two-way communication.*

2.27 Effective communication may involve structured presentations and written reports as well as less structured communications, including discussions. The internal auditor may communicate matters other than those described in the terms of engagement, either orally or in writing.

Relationship Management

2.28 In today's world, the internal auditors need to have a variety of skills to be successful. Not only they have to be good in their traditional area of competency like financial and governance expertise, analytical skills, risk assessment but also be business savvy, have an eye towards creating value, and provide a larger perspective. Soft skills are becoming crucial. Operating managers are requesting assistance from internal audit staff to improve effectiveness and efficiency of operations. Findings are not treated as deficiencies but as practices that can be improved by modification jointly developed by client and auditor working together.

To top it all and ensure that internal audit is effective, communication is most crucial. Sound governance requires effective interaction among the board, management, the external auditor, and the internal auditor.

Information Request List

The following information is requested to facilitate our understanding of your departmental operations and activities. This list is not intended to be all-inclusive. Additional information or questions may be required throughout the course of the audit. Please feel free to advise us of any additional information/ documentation not listed below that may be useful to us in the conduct of this audit:

- Departmental organizational chart.
- List of all accounts (numbers and account titles) maintained by the unit.
- Statement of Account and annual statements for the three fiscal years for the department.
- Operating and/or comparative analysis reports prepared or issued by your department on an annual basis for the past three fiscal years.
- Key departmental productivity and performance measures for the past three fiscal years, i.e., productivity measures used for budgeting purposes, etc.
- Description of significant departmental processes (include flowcharts if available).
- Internal policies and procedures manual.
- Copies of external regulations applicable to the department.
- Reports, surveys, etc., issued by external entities to the department.

Audit Notification to Auditee

<On the letterhead of Chartered Accountant >

June 20, 20XX

Mr. <Name>

CEO, <Company Name> Limited

<Address>

Dear Mr. <CEO>

A routine conformance audit of <Company Name> is scheduled for the period <dates>, 200X. This audit will include the main office at <office name>as well as the two sub-branches at <location1> and <location2>.

The objective of this audit is to conduct an analysis of <Company Name> Limited's policies and procedures to ensure that legislative requirements are met and an acceptable level of internal control is maintained. Standard audit procedures will be used including interviews with key personnel, facility inspections and a review of your company's approved programmes and manuals. A detailed audit plan, including the estimated hours required and names of audit team members and their areas of responsibility will be sent prior to the actual review.

We would like to schedule a pre-audit meeting with your management personnel before June XX at a time and date convenient to you and an exit meeting 20 days from the beginning of the review process. The pre-audit meeting will help in introducing the audit team to company management, provide a review of the audit process and inform the management of the audit process and regulatory responsibilities. The exit meeting will summarize the audit results and identify specific post-audit responsibilities where applicable.

The review will emphasise on the controls in the recently implemented financial system. We will need to access your financial accounting system and its reports. We plan to use some automated testing on your files. Please arrange for the system access and working space for our audit team.

Should you require any further information or clarification, please contact the audit manager<name>, at <number>.

Yours truly,

<Name>

<Designation>

Membership No. <Number>

Specimen Audit Report Cover Letter

<On the letterhead of Chartered Accountant >

July 14, 20XX

Report No. <Number>

Mr. <Name>

CEO, <Company Name> Limited

<Address>

Dear Mr. <CEO>

The audit team has concluded an operational review of the internal control structure and the recently implemented financial system SAP. The objective of our review was to evaluate controls in the financial system, compliance with policy & regulations and the effectiveness and efficiency of the current organisation authority structure.

The review covered operations of the period <date> to <date>. Please find enclosed two copies of the Audit Report of <Company Name> Limited completed on June XX, 200X. I am pleased to inform you that the review found that the financial department is well managed with generally good controls. However, controls need to be strengthened in few areas and documentation policies need to be more strictly enforced for travel expenses. A summary of the most significant audit findings are provided in Part II of the report.

The company must respond in writing to each audit finding. The proposed Corrective Action Plan should detail both short term corrective action to correct the specific deficiencies cited and, where applicable, long term corrective action. Long term corrective action should focus on modifying the system to prevent recurrence of similar deficiencies in the future.

We wish to express our appreciation for the co-operation extended to the audit team by you and your staff during the audit.

Yours truly,

<Name>

<Designation>

Membership No. <number>

Specimen Internal Audit Report

AUDIT NAME

AUDIT REPORT

TABLE OF CONTENTS **Page**

AUDIT NAME

DATE

Introduction

Background

Audit Perspective

Present audit status -

Recent past audits -

External audit coverage –

Scope & Objectives

The scope of the (audit or review)

The scope statement should be brief and should include the timing, type and purpose of the work and the standards used when conducting the audit. Types of audits or reviews are financial, operational, compliance and EDP.

(E.g., The scope of the audit was financial and operational in nature .This routine audit was conducted on AAA Foods Limited during the period of (month) (year). The audit covered the period from dd-mm-yyyy to dd-mm-yyyy . The audit was performed to ensure that financial data was properly recorded and adequate operational procedures exist in all the operational areas. The audit was conducted in accordance with the applicable Standards on Auditing. including reviews in the following areas:

(a) Royalty payments;

(b) Rent received from sub tenants;

(c) Compliance with Food safety and hygiene regulations ;

(d) Cash receipts; and

(e) Credit card receivables .

The last day of fieldwork was ____________________.)

The objectives of the audit were as follows:

- Determine that cash receipts were recorded correctly as to account, amount and period and are deposited promptly (recording, safeguarding).
- Verify that credit card receivables were correctly accounted, applied and payments received from the credit card company.
- Determine whether food safety inspections have been regularly carried out at various locations and appropriate hygiene levels are maintained.
- Review inspection reports- internal and external and steps taken to correct shortcomings, if any.
- Whether royalty has been calculated correctly and has been paid to the brand owners timely.
- Whether contract has been drawn up with sub tenants and floor space, rent and facilities has been has been agreed upon.

Note: Audit is used in the report when actual tests are performed to corroborate the opinion. Review is used in the report when no tests are performed to corroborate the opinion. Comment should speak directly as to what was done, i.e., if a test was performed, the word test should be used. If a review was performed, the word review should be used.

Company - General

AAA Foods Limited

Provide information on background of company and its operations. Provide details of functions and personnel in departments. Mention whether any major change in the organisation since the last audit. (E.g. the company has opened new food centres at 12 more locations. The staff strength has risen to 15,000. The company is now undertaking a massive exercise to centralize its processing and accounting at the main office).

Audit Synopsis

Mr. R. XYZ, senior partner of XYZ associates was in charge of the audit. The audit was conducted in accordance with auditing standards and policy and procedures detailed in the AAA Food Limited's manual. These techniques included interviews with key personnel, review of approved documents, sampling of relevant files, and random inspections throughout AAA Food Limited's system.

The audit entry meeting was held in AAA Food Limited's main office on <date>. During this meeting, the audit manager briefed the operator's management on the audit process and the team's audit plans. The officials of the company were regularly updated on audit progress and of all audit findings submitted. The audit was completed and the exit meeting was held in AAA Food Limited's main office on <date> with the senior officials namely<name>.

Corrective Action Plan

Audit Findings identify a situation where a company policy, procedure, or activity does not conform to policies & procedures specified in the company's internal audit manual or to the applicable regulatory standard. The company must respond in writing to each audit finding, detailing short term corrective action to correct the specific examples listed, and long term systemic corrective action to prevent recurrence of similar situations.

XYZ Associates will monitor implementation of AAA Food Limited's Corrective Action Plan through the audit follow-up process

Executive Summary

Purpose and Limitations

The executive summary is intended to provide an overview of the audit process, and summarise the significant findings (discussed in the detailed audit report) and the conclusions reached. The reader should not frame an opinion solely on the basis of this summary. The detailed report should be read to obtain the complete understanding of the background, ramifications, and recommendations.

General

The audit examined AAA Foods Limited's operations and finance divisions using applicable checklists referenced from the *Internal Audit Manual.* A total of xx operations and xy finance audit findings are reported. . These findings identified examples of non-conformance to the standards, regulations AAA Foods Limited's policies or procedures. A number of the findings were administrative in nature and can be easily corrected, whereas others were systemic and will require particular attention to ensure that corrective actions are effective in addressing the identified system faults.

Audit Opinion

As discussed more fully in our opinion on page ______ of this report.

Relevant Findings

- List a summary of each finding (without ramification/implication statement). Cross reference to detail section of report.

Audit Name

Internal Audit Opinion

In our opinion, we found the ________________________________ to be adequate, or inadequate (detail of inadequacies to follow the word inadequate).

We have identified opportunities to improve the controls of the (offices/areas/departments) involved in the... as discussed in this report.

AUDITOR-IN-CHARGE **DATE**

(E.g. **In our opinion, we found the financial transactions were properly recorded and the operational procedures adequate for the period under audit. However, there is still some scope for improving operating efficiency and effectiveness which are discussed in this audit report.**

In our opinion, we found the financial transactions to be properly recorded, but the operational procedures inadequate for the period under audit. We have made some recommendations on improvement of efficiency and effectiveness of certain operating procedures as discussed in this audit report.

The areas requiring immediate attention are: <area>, which currently lack some essential elements; <area>, which require a detailed system to ensure that all requirements have been met; and procedures to monitor and report on <area> activities.

The above deficiencies notwithstanding, the review revealed that AAA Foods Limited is maintaining strict quality control standards and that a knowledgeable, competent management team has been assembled to oversee its staff and employees that have the ability and desire to operate within the regulatory framework. The company's response upon learning of any deficiency was immediate and indicative of their focus on quality control.

Audit Name

Detailed Report

Overview

Pages X through XX outlines the **specific findings** resulting from our substantive audit testing. These issues are discussed in detail in our report and are categorized first on the basis of departments. Within each division, the major primary findings (significant internal control deficiencies and items potentially having a significant or adverse effect on the unit's operations) are mentioned first and then other matters (items of a lesser nature requiring attention, but not likely to have a significant or adverse effect on the unit's operations).

Primary Findings

I. COMMENT

Insert summary of the finding included in the Executive Summary

Finding

Ramifications/Implications

Recommendation(s)

Auditee's Response

Other Matters

II. COMMENT

Insert summary of the finding included in the Executive Summary

Finding

Ramifications/Implications

Recommendation(s)

Auditee's Response

PART III

CHANGE IN BUSINESS TRENDS AND PRACTICES

Industrial Services

Classification of Industry

3.1 There are four key industrial economic sectors:

- the primary sector, largely raw material extraction industries such as mining and farming;
- the secondary sector, involving refining, construction, and manufacturing;
- the tertiary sector, which deals with services (such as law and medicine) and distribution of manufactured goods; and
- the quaternary sector, a relatively new type of knowledge industry focusing on technological research, design and development such as computer programming, and biochemistry.

A fifth, quinary, sector has been proposed encompassing nonprofit activities.

The economy is also broadly separated into public sector and private sector, with industry generally categorized as private. Industries are also any business or manufacturing. Industries can be classified on the basis of raw materials, size and ownership.

Industrial Development

3.2 The industrial revolution led to the development of factories for large-scale production, with consequent changes in society. Originally, the factories were steam-powered, but later transitioned to electricity once an electrical grid was developed. The mechanized assembly line was introduced to assemble parts in a repeatable fashion, with individual workers performing specific steps during the process. This led to significant increases in efficiency, lowering the cost of the end process. Later automation was increasingly used to replace human operators. This process has accelerated with the development of the computer and the robot.

3.3 The main purpose of having an internal audit system in an organisation is to verify and review the activities of all cost centres so as to assist them in seeing that the assets of the business are properly protected and accounted for, that current transactions are promptly and completely recorded, that faulty, inefficient or fradulent operations are revealed and that the business is adequately protected against waste, fraud and loss. The purpose of this form of control is to assure early detection and rectification of errors to minimise their recurrence in future, to achieve economy in expenditure and all-round efficiency.

3.4 With growing complexities and inter-relation of activities between various agencies, modern industries allover the world have realised the pressing need to have internal audit to help the management at all levels in controlling the activities in the right direction

3.5 The main duties and functions of Internal Audit, *inter alia*, are broadly classified as under:

(i) Systems Audit

(ii) Operational Audit including Efficiency Audit

(iii) Management Audit

3.6 Business models around the world are changing dramatically from "Source Local" to "Source Anywhere and Build Anywhere" model. Firms have shifted away from a hierarchical, one-dimensional supply chain entity to a fragmented network in favor of strategic partnerships with external entities. Many businesses facing such model are experiencing challenges and are struggling to compete in this new landscape.

3.7 Most companies are already feeling the heat of the current financial meltdown, putting CPOs, Supply Chain Manager and their teams under intense pressure to reduce costs and improve cash flow while simultaneously managing an increasingly vulnerable supply base. Supply chain disruptions or discrepancy in supplier quality can significantly reduce company's revenue, impact market share, increase production cost, threaten brand image and reputation, and lead to high Cost of Poor quality (COPQ).

Financial Services

3.8 Consolidation, technology advances, and global commerce have intensified the competition for profit and market share in the financial services industry. As the demand for innovative products and services continues to increase, time-to-market and brand differentiation become key factors for success. Furthermore, responsiveness to the customers' needs and agility in adapting to today's challenges will determine tomorrow's financial leaders.

In India, the onset of globalization in July 1991 changed the financial scenes in the realms of banking, insurance and Mutual fund.

Banking

3.9 A landmark was registered in the Indian banking sector when the major banks were nationalized in 1969. Though nationalization was enforced as a flashy political gimmickry by the then government at the centre, its real gain was reaped by the citizens of India only in 2009-when the banks of developed nations tumbled down, the Indian banks stood strong- there was no public panic at all at the time of global financial crisis which shook the world during 2008-2009.

Insurance

3.10 The life insurance business has come a long way since independence, and Indian consumers till recently had been dealing with one life insurance player, i.e., the LIC in the public sector. After the liberalization of the insurance sector, a dozen companies have entered the insurance business. The insurance sector had the reforms with the passing of Insurance Regulatory and Development Authority (IRDA) bill in December, 1999. The privatization process commenced by forming the Insurance Reforms Committee. The 12 private life insurers have already grabbed 9% of the market in terms of premium income. The insurance premiums of these 12 players have crossed ₹ 1,000 crore over the last year. Innovative products, smart marketing and aggressive distributition, that is, the triple whammy combination has enabled fledgling private insurers to sign up Indian consumers. While the state owned companies still dominate segments like endowment and money back policies, the private companies have a virtual monopoly in the unit linked insurance schemes.

Mutual Funds

3.11 In India, mutual funds play a dominant role by mobilizing savings and investing them in the capital market, thus establishing a link between savings and capital market. The main objective of investing in mutual fund scheme is to diversify risk. Mutual funds made an opening in 1963 under the enactment of Unit Trust of India which launched its first scheme named US 1964, which is continuing even today.

In 1986, the Government amended the Banking Regulation Act and permitted public sector commercial banks like SBI, PNB, Canara bank and so forth to set up mutual funds. Government allowed insurance companies in the public sector General Insurance Companies (GIC) in 1989 and Life Insurance Companies (LIC) in 1991, to set up mutual funds.

In 1993, New Economic policy of liberalization opened the gates to the private sector to set up mutual funds. In March 1991, the government entrusted the function of regulating mutual funds to Securities and Exchange Board of India (SEBI) which issued guidelines in October, 1991 for regulating the Indian capital market. Interest rate future was launched in National Stock Exchange on 31st August, 2009.

It is a contract to buy or sell a debt security (10 year government bond bearing interest rate of 7% payable half yearly) at a price decided in advance for delivery at a future date. The contract helps to eliminate the interest rate risk.

3.12 Among the companies that have maintained a track record of success over time, certain characteristics are evident:

- Superior customer service and innovative products
- Ability to respond to shifts in the market
- Getting the product to market faster (time-to-market)
- Staff and cost reduction
- Increased employee satisfaction
- Return on investment (ROI)
- Creating ease and convenience of business transactions (e-business)

Internally, a company can achieve some of these goals by streamlining operations through reorganization and elimination of inefficiencies. Moreover, companies should take advantage of technology's offerings to further reduce excess cost and staff.

Companies must also focus on retaining and building lasting relationships by adapting a customer-centric culture. Customer demands for greater convenience in transactions, online support, and call centers should be addressed

E Finance

3.13 In recent years electronic finance, especially, online banking and brokerage services has reshaped the financial landscape around the world. E-finance is dramatically changing the structure and nature of financial services

E-finance will lead to much lower costs and greater competition in financial services through both new entry from outside today's financial sector and greater competition among incumbent financial service providers. These developments will force banks to lower fees and commissions because providing e-finance is much cheaper than providing traditional financial services. As a result incumbent financial institutions will likely experience a sharp decline in revenue.

3.14 Internet and related technologies are more than just new delivery channels—they are a completely different way of providing financial services.

Using data mining techniques, for example, providers can tailor products without much human input and at very low cost. They can also better stratify their customer base and allow consumers to build preference profiles online—enabling far more personalized pricing of financial services and much more effective identification of credit risks.

The Internet also allows new financial service providers to compete more effectively for customers. All these forces are delivering large benefits to consumers of financial services at the retail and commercial levels.

3.15 Technological advances are also changing the face of the financial services industry. New providers are emerging within and across countries, including online banks, online brokerages, and companies that allow consumers to compare financial services such as mortgage loans and insurance policies. Nonfinancial entities are also entering the market, including telecommunication and utility companies that offer payment and other services. Vertically integrated financial service companies are growing rapidly and creating synergies by combining brand names, distribution networks, and financial service production.

Trading systems—for equities, fixed income, and foreign exchange—are consolidating and going global. Trading is moving toward electronic platforms not tied to any location. Electronic trading and communication networks have lowered the costs of trading and allow for better price determination.

3.16 The Internet and other technological advances have shrunk economies of scale in the production of financial services. Lower scale economies have increased competition, particularly among financial services that can easily be unbundled and commoditized through automation—including payment services, mortgage loans, insurance, and even trade technology. Competition is further fostered by declining up-front costs. In contrast, network externalities—exhibited by financial services such as payment services, trading systems, and exchanges—tend to hamper competition.

3.17 It is clear that many aspects of financial services industry in India have changed since the 1990's. With the reforms of financial services industry, the economy has been opened up and several significant developments have been taking place in all the segments of the financial services sector. As per the survey of Central Statistical Organization, the Indian economy has grown at 6.1% in the first quarter of 2009-2010 against 5.8% growth in the previous quarter despite the global financial crisis impacting manufacturing and services sectors like trade, hotels and communication.

Service Industry

3.18 Service sector has emerged as the largest and fastest growing sector in the global economy in the last two decades, providing more than 60 per cent of global output and, in many countries, an even larger share of employment. The growth in services has also been accompanied by the rising share of services in world transactions.

3.19 The emergence of India as one of the fastest growing economies in the world during the 1990s is attributable to the rapid growth of its services sector to a great extent. The sector has been experiencing double-digit growth during the two years (2004-05 and 2005-06), importantly, a strong growth of 10 per cent in 2005-06 has been instrumental in providing an impetus to overall real sector activity in the economy and propelling it to record a sturdy growth of 8.4 per cent (at 1999-00 prices).

3.20 In line with the global trend, service sector in India has also grown rapidly in the last decade. Its growth has in fact been higher than the growth in agriculture and manufacturing sector. It now contributes around 51 percent of GDP. Subsequent to this, the sector has continued to exhibit vibrant growth (10.6 per cent) during the first quarter of 2006-07 over the corresponding period of the previous year, mainly propelled by growth in 'trade, hotels, transport and communication' (13.2 per cent) followed by 'finance, insurance, real estate and business services' (8.9 per cent).

Due to the structural transformation of the Indian economy in the new millennium in favour of a service-dominated economy from an agrarian one, the share of the services sector in the total GDP has increased notably from 49.8 per cent in 2000-01 to 54 per cent in 2005-06.

The remarkable sectoral performance of the services sector as a whole has been reflected in the select lead indicators of the services sector.

However, though the growth of service sector in India is in line with the global trends, there are two unique characteristics of India's service sector growth. First, the entire decline in the share of agriculture sector in GDP, i.e., from 32 % in 1990 to 22 % in 2003, has been picked up by the service sector while manufacturing sector's share has remained more or less the same.

3.21 In general, such a trend is mainly experienced by high-income countries and not by developing countries and second, in spite of the rising share of services in GDP and trade, there has not been a corresponding rise in the share of services in total employment. This jobless growth of India's service sector, with no corresponding growth in the share of manufacturing sector, has raised doubts about its sustainability in the long run.

Further, it is found that growth pattern in the service sector has not been uniform across all services in India. Some services have grown fast in terms of their share in GDP and also in terms of their share in trade and FDI (e.g., software and telecommunications services). But there are some services, which have grown fast but have not been able to improve their share in international transactions (e.g., health and education) while there are some services that have in fact witnessed a negative growth and also a low share in international transactions (e.g., legal services).

3.22 One of the probable reasons for this lopsided growth in services is the fact that reforms in India at the sectoral level have evolved in an ad-hoc way rather than as part of a coherent overall strategy. Though there exists an overall industrial policy and agricultural policy in India, there is no integrated service policy. Consequently, the pace of reforms and their impact lacks uniformity across sectors. Moreover, most of the services have for a long time been in the public domain and they suffer from both external constraints in terms of high barriers to trade, as well as domestic constraints in terms of being highly regulated services with state monopolies. These services consequently suffer from inefficiencies and low growth.

3.23 Performance of key-drivers of the Service Sector:

- Travel and Tourism
- Retail Sector
- Services Inflation

PART IV

VARIOUS TECHNIQUES INLCUDING COMPUTER ASSISSTED AUDIT TECHNIQUES

Computer Assisted Audit Techniques

4.1 Internal Auditors make use of computer-assisted audit techniques (CAATs) to improve audit coverage by reducing the cost of testing and sampling procedures that otherwise would be performed manually. With the widespread use of computerized financial and other record keeping, using CAATs has now become a necessity for audit of most organisations. CAATs provide reasonable evidence required to support audit conclusions in paperless environment. They provide a more efficient and reliable method to review items recorded in computer files.

4.2 CAATs may be used in performing various audit procedures like:

- Tests of transactions and balances, such as recalculating interest;
- Analytical review procedures, such as identifying inconsistencies or significant fluctuations;
- Compliance tests of general controls and application controls;
- Sampling programs to extract data for audit testing;
- Penetration testing.

Determining the Need for CAAT

4.3 One thing, however, needs to be considered- CAATs might not always increase audit efficiency or be cost effective. Certain processes may not be right for CAAT.

4.4 Need for CAAT depends on:

- Audit Objective
- Nature of data to be reviewed
- Availability of requisite CAAT tools
- Availability of skilled audit staff

Types of Computer Assisted Audit Techniques

4.5 CAATs include many types of tools and techniques, such as, generalized audit software, utility software, test data, application software tracing and mapping, and audit expert systems. CAATs may be:

- Developed by internal programming staff or by outside programmers with audit department supervision;

- Purchased generalized audit software, e.g., audit packages offered by CPA firms or software vendors;
- Developed by IT auditors; or
- Acquired from equipment manufacturers and software houses to analyze machine, programmer, and operations efficiency.

Whatever the source, audit software programs should remain under the strict control of the audit department. For this reason, all documentation, test material, source listings, source and object program modules, and all changes to such programs, should be strictly controlled. In installations using advanced software library control systems, audit object programs may be catalogued with password protection. Computer programs intended for audit use should be documented carefully to define their purpose and to ensure their continued usefulness and reliability.

Types of Computer Audit Software

4.6 The types of computer audit software are as follows:

- Generalised audit software tools
- Specialised audit test and analysis software
- Utility software
- Test data techniques
- Expert systems
- Embedded audit procedures

With the use of audit software, auditors can directly obtain evidence to the quality of records produced and maintained by client's systems. Various software whether off the shelf, specialized or customized are a useful tool in the hands of the auditor to gain access to manipulate the data maintained in the computer systems to achieve audit objectives.

Reasons for using Generalised Audit Software

4.7 Computerized information systems faced by auditors may be different. Companies have different hardware, software, record functions, and different processing functions. With the resource required for customized programs, it is not possible to develop specific programs to extract, manipulate, process and report on the data.

Audit objectives are constantly changing. New areas may be required to be audited; different approach may have to be used.

Auditor may have a broad understanding of systems but they do not have specific knowledge or experience with particular hardware, software being used.

Functions of Audit Software

4.8 The functions of Audit Software are as follows:

- **100% data**
- **File access :**The file access functions enable different file structures to be accessed.
- **File reorganization:** Sorting data, merging data, comparing data can be done
- **Selection:** Extraction of data based on certain criteria.
- **Statistical:** Selection of random data for different types of sampling
- **Arithmetic:** Checking arithmetic accuracy of data, control totals etc.
- **Stratification and frequency analysis** Different types of Stratification, frequency and ageing analysis can be undertaken.
- **Detection of Fraud**
- **File creation and updating**
- **Reporting:** Comprehensive reports can be produced with the data automatically.

Specialised Audit Test and Analysis Software

4.9 Specialised Audit test and Analysis software are used due to following reasons:

- Used to review specialised computer files
- Manufacturing, production & material scheduling software packages contain reporting sub systems
- CASE
- Test data techniques
- Series of test transactions are checked with copy of live production system to determine if controls are adequate
- Helps in general understanding of complex system
- Tests whether valid transactions are correctly processed

- Tests whether invalid transactions are identified and flagged

Audit tasks

4.10 Audit software can help in the accomplishment of various audit tasks:

- Examining the quality of data
- Examine the system processes
- Do analytical reviews

PART V

STANDARDS ON INTERNAL AUDIT

Internal Audit Standards Board (IASB)

5.1 Internal Audit Standards Board was constituted as the Committee on Internal Audit in the year 2004, with the mission of reinforcing the primacy of the Institute of Chartered Accountants of India (ICAI).

Framework for Assurance Engagement (Effective from 1st April, 2008)

- Framework defines the elements and objectives of an assurance engagement.
- Frame of reference is offered to:
    i. Practitioners
    ii. Other involved in assurance engagements
    iii. AASB Board in the development of SAs, SREs and SAEs
- The framework distinguishes the assurance engagements from other engagements like consulting engagements.
- Assurance engagements include internal audit and due diligence audits.
- Definition of Assurance Engagement under the Framework.
- "Assurance engagement" means an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria."
- Framework identifies 5 elements of assurance engagements namely:
    i. A three party relationship
    ii. A subject matter
    iii. Criteria
    iv. Evidence
    v. Assurance Report

Standards on Internal Audit

1. Standard on Internal Audit (SIA) 1, Planning an Internal Audit
2. Standard on Internal Audit (SIA) 2, Basic Principles Governing Internal Audit

3. Standard on Internal Audit (SIA) 3, Documentation
4. Standard on Internal Audit (SIA) 4, Reporting
5. Standard on Internal Audit (SIA) 5, Sampling
6. Standard on Internal Audit (SIA) 6, Analytical Procedures
7. Standard on Internal Audit (SIA) 7, Quality Assurance in Internal Audit
8. Standard on Internal Audit (SIA) 8, Terms of Internal Audit Engagement
9. Standard on Internal Audit (SIA) 9, Communication with Management
10. Standard on Internal Audit (SIA) 10, Internal Audit Evidence
11. Standard on Internal Audit (SIA) 11, Consideration of Fraud in an Internal Audit
12. Standard on Internal Audit (SIA) 12, Internal Control Evaluation
13. Standard on Internal Audit (SIA) 13, Enterprise Risk Management
14. Standard on Internal Audit (SIA) 14, Internal Audit in an Information Technology
15. Standard on Internal Audit (SIA) 15, Knowledge of the Entity and its Environments
16. Standard on Internal Audit (SIA) 16, Using the Work of an Expert
17. Standard on Internal Audit (SIA) 17, Consideration of Laws and Regulations in an Internal Audit

Standards on Assurance Engagements

5.2 Tracing the history of Auditing and Assurance Standard Board (AASB), it dates back to the year 1955 when Auditing Sub-Committee of Research Committee (ASRC) constituted. In 1963, ASRC issued the Statement on Auditing Practices. Later in 1983, the Auditing Practices Committee (APC) was constituted which issued the first Auditing Standard in the year 1985. In July 2002, APC was converted into Auditing and Assurance Standard Board (AASB).

5.3 The Institute of Chartered Accountants of India is a member of the International Federation of Accountants. Therefore, as a matter of policy, the auditing standards issued by the ICAI are in harmony with the International Standards on Auditing. Till date, the IAASB of the IFAC has issued forty four Engagement Standards, comprising one Standard on Quality control (ISQC), thirty six ISAs, two International Standards on Review Engagements (ISREs), three International Standards on Assurance Engagements (ISAEs) and two

International Standards on Related Services (ISRSs). The AASB of ICAI has issued forty three auditing standards corresponding to the Engagement Standards issued by the IAASB of the IFAC.

5.4 There are 43 Standards on Audit and Assurance work including those related to quality control, assurance engagement and related services issued by ICAI.

Two standards have been issued on the review of Financial Statements. While SRE 2400 deals with "Engagements to Review Financial Statements" performed by an auditor of the entity be it internal or external, SRE 2410 ***"Review of Interim Financial Information performed by the Independent Auditor of the Entity****" applies only to the Independent/ Statutory Auditor.*

PART VI
INTERNAL AUDIT REPORTING

Contents of a Good Internal Audit Report

6.1 The assurance report should include the following basic elements:

- A Title;
- An addressee;
- An identification and description of the subject matter information and, when appropriate, the subject matter;
- Identification of the criteria;
- Where appropriate, a description of any significant, inherent limitation associated with the evaluation or measurement of the subject matter against the criteria;
- When the criteria used to evaluate or measure the subject matter are available only to specific intended users, or are relevant only to a specific purpose, a statement restricting the use f the assurance report to those intended users or that purpose;
- A statement to identify the responsible party and to describe the responsible party's and the practitioner's responsibilities;
- A statement that the engagement was performed in accordance with SAEs;
- A summary of the work performed;
- Practitioner's Signature;
- The assurance report date;
- The place of signature – the report should name specific location, which is ordinarily the city where the report is signed.

Audit Reporting Cycle

6.2 It is desirable that during the course of the audit, a framework of the final report is developed so that the needed information is obtained on time. This will prevent delays in the report writing process. Important and sensitive findings should be shared with responsible managers immediately upon verification by the audit staff; memo reports may be used in this process.

6.3 As findings are completed, they are inserted in the proper sections of the report. The audit report is a process in itself, which starts with identification of findings, preparation of draft report, discussions of findings with the concerned people, management responses to audit findings and issuance of final report. An internal audit function may alter or skip any of the steps outlined below to suit its needs and purpose:

- Outline Audit findings
- Preparation of Audit report - First draft
- Discussion with client
- Preparation of Final Audit report draft
- Closing conference
- Issuance of Final report

A. Outline Audit Findings

a. Document all findings

b. Determine whether there is sufficient support for all findings

c. Determine whether there is pattern of deficiencies, which could mean procedural changes are required.

B. Preparation of First Draft

a. The draft report should state that the findings, conclusions and recommendations set forth are preliminary in nature.

b. The draft report should follow standard format.

c. Ensure that figures and facts have been checked and cross-referenced to relevant workpapers.

d. Review that the workpapers provide adequate support for items of significance

e. Check for tone, spelling and punctuation.

f. Issue report (stamped "DRAFT") to management for review.

C. Discussion with Client

a. Determine whether the management was aware of the issues and taking corrective action on the same.

b. There should be no surprises - everything in the draft should have been discussed during the fieldwork.

c. Be sure you can easily find supporting documentation for findings in the working papers in case questions arise at the meeting.

d. Ascertain the causes for the deficiencies /problems. Find out whether there are any constraints or limitations for the shortcoming.

e. Get the client comment on the draft report, and any inaccuracies or impractical recommendations resolved to the extent possible.

f. Get management's agreement on the facts and wording of the report.

g. Ask management for written responses (give specific due date for responses).

D. Preparation of Final Audit Report Draft

a. Ensure that management's/auditee's viewpoint has been considered.

b. Determine whether the report is well written and in a manner that all intended recipients may understand.

c. Ensure that audit staff who wrote the report agree with the changes made.

d. Make sure that management's /auditee's viewpoint has been rightly stated and adequately rebutted, if necessary.

E. Closing Conference

a. Provide the management or appropriate staff adequate opportunity to study the report.

b. Departmental administrators and managers have the opportunity to informally provide additional information, question findings, or challenge conclusions. On the basis of those discussions, the final report may be modified.

c. Try to anticipate potential questions/conflicts.

d. Inquire from the managers or appropriate staff whether they have any questions about the opinion or background or the audit process.

e. Normally, only the administrators of the department being reviewed attend the closing conference to allow the parties most affected by the report to more freely and confidentially express their views, and to ensure the accuracy of the final audit report.

f. Obtain current plans of follow up from the management /auditee.

F. Issuance of Final Report

a. The final report should include modifications and changes discussed and agreed to at the closing conference, if held, in addition to the auditee's written responses.

b. The auditee's written responses will be reviewed by the staff auditor and the Audit Supervisor and evaluated in writing, if necessary.

c. When differences of opinion persist even after the final draft, the report will be issued although it may be modified to reflect the position of the audited department or higher-level management.

d. Before release, the report will be signed by all those responsible for the audit, which would normally be the Audit Director, Audit Supervisor and appropriate staff auditor.

e. All changes to the report must be documented in the work file and signed off on by the staff auditor, Audit Supervisor and the Audit Director.

f. Try to provide a balanced presentation by including 'departments or units' notable strengths to credit staff for correcting past deficiencies and to recognise superior management.

g. Make a final reading of the report for content, clarity, consistency and compliance with professional standards.

h. File final report in project binders and cross-referenced to supporting working papers; provide explanations for comments deleted or changed significantly since original draft.

G. Dissemination of Report

a. The persons to whom the report is to be delivered will vary from organisation to organisation and from one assignment to another. Some of the recipients could be the Corporate Vice President, for Administration or the Vice President for Business and Finance, the Department Head, the CFO, the CEO, the Board of directors and the Audit Committee.

b. In some organisations the BOD and the Audit committee may be presented with sAudit Committee with periodic summaries of audit findings, with access to summaries or full reports if requested.

c. In certain organisations the report is published on the website. In that case, Copy the report file to the share drive for eventual publication on the web page. Take the original paper copy of the letter to the management and the signature page from the report to the webmaster. Those two pages will be scanned and converted into a PDF format document and inserted into the report posted on the share drive.

Evaluation and Follow Up

6.4 At the completion of each audit, the audit manager will send an evaluation survey form to the primary clients of the audit. These should be completed and returned to the Director of Internal Audit, in order to ensure continuous improvement of these procedures and the internal audit function.

After receiving the response determine whether responses address the issues described in the findings, promise action that will correct the weakness reported, and include a reasonable completion date.

Follow up

6.5 Each organisation /department may have its own time limits for replying to the report and the internal audit department may have its own rules for follow up. Some internal audit function may conduct a follow up after six months or one year to and ascertain the status of open recommendations.

Internal auditing should determine that corrective action was taken and is achieving the desired results, or that management or the board has assumed the risk of not taking corrective action on reported findings.

Role of an Internal Auditor

6.6 Internal Audit is a service to management. Its functions include examining and evaluating internal control and providing assurance to the management. It is a part of the organisation's system of internal control and its scope includes ALL aspects of internal control, not just financial control. The scope of internal audit is much wider than statutory/ external audit as discussed in detail above. It should ideally cover all the organisation’s activities.

The role of an internal auditor can be simply captured in four point:

a. To act as a catalyst.

b. To interface between different groups.

c. To advise on the process.

d. To report the facts of audit results.

Characteristics of an Internal Auditor

Professionalism

6.7 In today’s scenario, the demand for professionalism, knowledge and integrity has increased manifold. To be effective, auditors must serve as objective assurance providers and advisors to the other participants in the governance process like Board of Directors and the audit committee; provide guidance on improving operational efficiency and control; evaluate risk and advise the management on risk identification, risk tolerance and risk management.

The scope on internal audit has widened and may cover the whole gamut of organisation's activities. It is the internal auditor's task to operate within the framework of professionalism to assist the company in achieving the highest-quality results and long-term objectives. This calls for clear and concise guidance that can be readily adopted and followed regardless of the industry, audit specialty, or sector.

Proficiency

6.8 Internal auditors need to have the knowledge and skills to perform their individual responsibilities. If the knowledge, skills, or other competencies needed to perform all or part of the engagement are not available within the internal audit staff, then the chief audit executive should obtain competent advice and assistance from outside the activity.

Though the internal auditors are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud, they should have sufficient knowledge to identify the indicators of fraud.

Due Professional Care

6.9 The internal auditor is expected to apply due professional care which is expected from a reasonably prudent and competent internal auditor. The internal auditor should exercise due professional care by considering:

- Extent of work.
- Adequacy of risk management, internal control procedures.
- Probability of errors, misstatements or irregularities.
- Cost incurred in relation to expected benefits.

Continuing Professional Development

6.10 Internal auditors should enhance their knowledge, skills, and other competencies through continuing professional development.

Professional Behaviour

6.11 Internal auditors need to act professionally and maintain the good reputation of the profession. The organisation should benefit from the internal audit activity in its risk management and internal control process.

An auditor's responsibility is not limited to satisfy the needs of an individual employer. The standards of the accountancy profession are heavily determined by the public interest, for example - Internal auditors provide assurance about a sound internal control system which enhances the reliability of the external financial information of the employer. Accountancy and audit bodies like IIA and IFAC have formulated some important principles of behaviour.

Independence

6.12 Professionalism entails a heavy responsibility. It means subscribing to a Code of Conduct. The professional internal auditor needs to have independence to provide an objective, unbiased opinion. They can never have complete independence but they need sufficient independence.

Code of Ethics of the Institute of Internal Auditors provides internal auditors with sufficient mechanism for reporting of audit results, findings, opinion or information. The auditor can report to the appropriate level of management and there should be no need to report in an unauthorized manner to anyone outside the organisation.

Only if the matter is not resolved satisfactorily, or the services of auditor are terminated due to that, he should secure the advice of outside counsel.

How to Succeed as an Internal Auditor

Following are the ways to be successful as an internal auditor:

- Sharpen dialogue with top management and directors in order to clearly establish the value-added objectives of internal audit (i.e., strategic issues, risk management and protection of company assets).
- Realign to meet key stakeholders' expectations (stockholders, executive management, external auditors and regulators).
- Think and act strategically.
- Expand audit coverage to include "tone at the top," the conduct of executive management in protecting the company.
- Assess and strengthen expertise for complex business auditing.
- Leverage technology in high-risk areas.
- Focus on enterprise risk management capabilities
- Make the audit process dynamic, changing with changed business conditions.
- Strengthen quality assurance processes.
- Measure the enhanced performance against expectations of stakeholders

PART VII

PROFESSIONAL OPPORTUNITIES IN INTERNAL AUDIT

I. Audit of the Internal Control Framework

1. Evaluation of Effectiveness of Internal Audit Function;
2. Providing Assurance regarding Internal Controls;
3. Determination of Adequacy of Internal Control Framework;
4. Internal Audit evaluating the policies and procedures of the organizations;
5. Offering Control Self Assessment;
6. Internal Audit Universe.

Internal Audit Universe				
Sr. No.		**Business Process Cycle**	**Sr. No.**	**Sub-processes**
A.		**REVENUE CYCLE**		
	A.1	Products – Domestic	1)	Sales Forecasting
			2)	Customer masters
			3)	Quote Preparation
			4)	Design & Tooling
			5)	Shipment Scheduling
			6)	Warehousing
			7)	Invoicing
			8)	Accounts Receivable
			9)	Credit Notes & Debit Notes
			10)	Collection from customers
			11)	Sales Returns
			12)	Price increase / decrease
			13)	Sales contribution
			14)	Revenue Recognition
			15)	Warranty Supplies
	A.2	Products – Exports	1)	Sales Forecasting
			2)	Customer masters
			3)	Quote Preparation
			4)	Design & Tooling

			5)	Shipment Scheduling
			6)	Warehousing
			7)	Invoicing
			8)	Accounts Receivable
			9)	Credit Notes & Debit Notes
			10)	Collection from customers
			11)	Sales Returns
			12)	Price increase / decrease
			13)	Sales contribution
			14)	Revenue Recognition
			15)	Warranty Supplies
			16)	Export benefits
			17)	EOU compliances
	A.3	Services	1)	Sales Forecasting
			2)	Customer masters
			3)	Quote Preparation
			4)	Invoicing
			5)	Accounts Receivable
			6)	Credit Notes & Debit Notes
			7)	Collection from customers
			8)	Price increase / decrease
			9)	Sales contribution
			10)	Revenue Recognition
			11)	Export benefits
			12)	STPI compliances
	A.4	Scrap	1)	Vendor Selection
			2)	Scrap pricing
			3)	Scrap segregation
			4)	Scrap shipment
			5)	Scrap Invoicing
			6)	Credit Notes/ Debit Notes
			7)	Collection

			8)	Accounts Receivable
			9)	Tax Collection at source
			10)	Revenue Recognition
B.		**PROCURE TO PAY CYCLE**		
	B.1	Direct Material – Domestic & Import	1)	Vendor Development & Selection
		i) Raw Material	2)	Design & Tooling
		ii) Bought Components	3)	Cost Estimation & Rate fixation
		iii) Sub-Contracting	4)	Share of business
			5)	Material Requisition Planning
			6)	Vendor rating
			7)	Raising purchase order
			8)	Vendor invoice verification & payment
			9)	Advances to vendors
			10)	Debit notes / credit notes
			11)	Returns & Adjustments
			12)	Supplementary vendor invoices
			13)	Material reconciliation - Subcontracting
			14)	Advance Licences/EOU/DEPB compliances
			15)	Accounts Payable
	B.2	Indirect Material - Domestic & Import	1)	Raising of Indent
			2)	Quotation/rate fixation/share of business
			3)	Raising purchase order
			4)	Vendor invoice verification & payment

			5)	Advances to vendors
			6)	Debit notes / credit notes
			7)	Returns & Adjustments
			8)	Advance Licences/EOU/DEPB compliances
			9)	Accounts Payable
	B.3	Services i) Labour Contracts	1)	Raising of Indent
			2)	Quotation/rate fixation/share of business
		ii) Maintenance Contracts	3)	Raising purchase order
		iii) Transportation Contracts	4)	Vendor invoice verification & payment
		iv) Canteen Contracts	5)	Advances to vendors
		v) Insurance contracts	6)	Debit notes / credit notes
		vi) Travel related contracts	7)	Returns & Adjustments
		vii) Clearing forwarding contracts	8)	Accounts Payable
	B.4	Utilities	1)	Consumption of Fuel
			2)	Consumption of Power
			3)	Consumption of water
			4)	Consumption of Compressed Air
	B.5	Tools & machinery Spares	1)	Raising of Indent
			2)	Quotation/rate fixation/share of business
			3)	Raising purchase order
			4)	Vendor invoice verification &

				payment
			5)	Advances to vendors
			6)	Debit notes / credit notes
			7)	Returns & Adjustments
C.		**MANUFACTURING/SERVICES**		
			1)	Production Planning & Control
			2)	Line Rejections/Scrap generation/rework
			3)	Direct material line rejection & Recovery
			4)	Quality Control
			5)	Plant Efficiencies / Capacity Utilisation/Resource Utilisation
			6)	Bill of Material Master data
			7)	Input-Output Analysis
			8)	Recording of Production & Consumption
			9)	Development projects
			10)	Manpower productivity indices
			11)	Product Design / Engineering Change Request
			12)	Capability Development Process
			13)	Cost variances
			14)	Manpower Planning
D.		**INVENTORY**		
		i) Raw Material	1)	Receipt & Storage of Material
		ii) Boughtout Components	2)	Issue of Material
		iii) Sub-contractor	3)	Age analysis
		iv) Consumables	4)	Physical verification of inventory
		v) Tools	5)	Inventory valuation

		vi) Spares	6)	Inventory adjustments
		vii) WIP	7)	Inventory Levels – Min/Max/Reorder etc
		viii) Finished goods		
		ix) Stock in warehouse		
		x) Goods-in-transit		
E.		**PROPERTY, PLANT & EQUIPMENT**		
			1)	Capital Expenditure Budgeting
			2)	Vendor Selection
			3)	Inspection, Commissioning & Acceptance
			4)	Cenvat Availment
			5)	Vendor invoice verification & payment
			6)	Liquidated damages
			7)	Capitalisation
			8)	Post Implementation review
			9)	Depreciation
			10)	Cost and time overruns
			11)	Fixed asset register
			12)	Physical verification
			13)	Assets given loan or given loan
F.		**PAYROLL**		
			1)	Recuritment process
			2)	Time keeping / Attendance records
			3)	Salary processing & payments
			4)	Overtime payments
			5)	Medical Benefits
			6)	Other benefits

			7)	Separation process & payments
			8)	Loans & Advances
			9)	Upaid salaries & wages
			10)	Maintenance of personal records
G.		**TREASURY**		
			1)	Investment of Surplus Funds
			2)	Cash Management
			3)	Funds Transfers to units /branches
			4)	Bank Reconciliation
			5)	Bank Charges & Interest
			6)	Borrowings
			7)	Cash Credit Utilisation
			8)	EEFC Account
			9)	Foreign Exchange risk management
H.		**STATUTORY COMPLIANCES**		
I.		**MANAGEMENT INFORMATION SYSTEMS**		
			1)	Review of MIS Reports
			2)	Budgeting
J.		**TRANSACTIONAL AUDIT**		

II. Internal Audit Functions/ Requirements under various Laws

- Risk Based Internal Audit (RBIA) in Banks under RBI Guidance.
- Compliance of Internal Audit requirements under Companies (Auditor's Report) Order, 2003.
- Internal audit of Operations of Depositary Participants.
- Internal Audit requirements mandated by SEBI on a half yearly basis for stock brokers/trading members/ clearing members.

- System Audit of Investment functions of Insurance Companies.
- Concurrent audit in Banks.
- Internal audit to be undertaken in respect of Credit Rating Companies Operations.
- Internal audit of Mutual Funds.
- Internal Audit of Custodians.
- Internal audit of Registrar & Share Transfer Agents.
- Internal audit mandatory for multiple banking or consortium RBI.
- Internal Audit requirement every quarterly required for insurers under IRDA (Investment) (Fourth Amendment) Regulations, 2008.

III. Enterprise Risk Management – The ERM Role

- Providing assurance on the design and effectiveness of risk management processes.
- Providing assurance that risks are correctly evaluated.
- Evaluating risk management processes.
- Evaluating the reporting on the status of key risks and controls.
- Reviewing the management of key risks, including the effectiveness of the controls and other responses to them.

Consulting Activities

- Championing the establishment of ERM within the organization.
- Developing risk management strategy for board approval.
- Facilitating the identification and evaluation of risks.
- Coaching management on responding to risks.
- Coordinating ERM activities.
- Consolidating the reporting on risks.
- Maintaining and developing the ERM framework.

Roles that internal auditors should NOT undertake are:

- Setting the risk appetite.
- Imposing risk management processes.
- Providing assurance to the board and management.

- Making decisions on risk responses. This is management's responsibility.
- Implementing risk responses on management s behalf.
- Accountability for risk management.

IV Audit of Compliance of Standards on Internal Audit

- Till date, there are 17 standards issued by IASB, ICAI.
- Standards on Internal Audit shall be recommendatory in nature in the initial period.
- The Standards shall become mandatory from such date as notified by the Council.

V Monitoring XBRL Implementation and Reporting Results

- Ensuring savings in cost/resources for redundant data related work - XBRL ensures data re-usability.
- Efficiency gains in external reporting processes.
- Enables more frequent review/updation of internal credit rating system.
- Integrating different systems and provide for easier generation of complete, consolidated and centralized information.
- Enhanced internal controls/audit processes if XBRL is extensively leveraged.
- Generation of standard and ad-hoc reports as required.
- Ease of incorporating data for various analytical studies and periodic reports.
- Use of business intelligence tool for advanced analytics and drill-down/roll up facility.
- Contextual and explanatory information available around every data.
- There is a common framework of definitions.
- Corporate information is available with transparency and accuracy.
- Comparison of financial data among multiple companies made easier.

VI. Audit of IFRS Convergence

Internal audit can and should play a key role in assessing organizational readiness by:

- Identifying project risks (e.g., operational, financial reporting, resources) in the planning stages.
- Focusing on control over the change management process and the impact on internal control over financial reporting and disclosure controls and procedures.
- Informing the company's board and senior management (and soliciting feedback from the same) on the status and progress of IFRS readiness and implementation.

VII. Forensic Audit

- Forensic auditing strengthens control mechanisms, with the objective of protecting the business against financial crimes.
- It plays an important role for companies under review by regulatory authorities.
- It helps protect organizations from the long-term damage to reputation caused by the publicity associated with insider crimes.
- It also provides a sound base of factual information that can be used to help resolve disputes.
- It can help with the detection and recording of potential conflicts of interest for executives by improving transparency.
- It can improve efficiency by identifying areas of waste.

VIII Fraud Detection

- Banking Frauds
- Insurance Frauds
- Stock market frauds
- Internet frauds
- Investment Frauds
- Cyber crimes

IX Internal Audit and Corporate Governance

1. The four characteristics of good governance are transparency, accountability, effectiveness/efficiency and responsiveness.
2. The role of internal control in a Corporate Governance framework:
   - Risk Assessment
   - Providing Assurance regarding controls
   - Compliance
   - Consulting and Operations.
3. Organizational Independence is vital for an effective internal audit function of the governance framework.
4. An Internal Audit Charter helps in administering the audit function.
5. Unrestricted access to all forms of evidence offers efficient audit results.

X Internal Audit of Management Functions

1. Business strategy process
2. Human resources functions
3. Marketing strategy
4. Production process

XI Stock Audit/ Credit Audit

1. Stock audit for bank borrowers
2. Stock audit other than bank borrowers

XII Internal Audit of Compliance with Commercial Laws (Illustrative List)

1. Anti Money Laundering Laws
2. Laws relating to Alternate Dispute Resolution
3. Laws relating to Real Estate
4. Family and Succession Laws
5. Legal Metrology laws
6. Laws relating to Charity
7. Labour Laws

8. Intellectual Property Right
9. Insolvency Laws/ Board for Industrial and Reconstruction (BIFR)
10. Securitization Laws
11. Laws relating to Non Banking Financial Institutions
12. Competition Laws
13. Consumer Laws
14. Laws relating to Cooperative Societies
15. Corporate Laws
16. Laws relating to Limited Liability Partnership (LLP)
17. Laws relating to Micro, Small And Medium Enterprises (MSMES)
18. Banking Laws
19. Insurance Laws
20. Securities Law
21. Laws relating to International Trade
22. Foreign Exchange Management Laws
23. Right to Information Law
24. Laws relating to Special Economic Zones (SEZ)
25. Energy Laws
26. Carriage Laws And Multi-Modal Transportation Of Goods
27. Laws relating to Aviation Sector
28. Laws relating to Telecom Industry
29. Laws relating to Pharmaceuticals
30. Information Technology and Cyber Laws
31. Environmental Laws
32. Carbon Credit

XIII Due Diligence

1. Commercial Due Diligence Process
2. Legal Due Diligence Process
3. Operational Due Diligence Process

4. Business Strategy/ Management Culture Due Diligence Process
5. Environmental Due Diligence Process
6. Human Resource Due Diligence Process
7. Marketing Due Diligence Process
8. Business Environmental Due Diligence Process
9. Preliminary Due Diligence Process
10. Full Due Diligence Process
11. Ongoing Due Diligence Process
12. Private Equity Due Diligence Process
13. Mergers and Acquisitions Due Diligence Process
14. Joint Venture Due Diligence Process
15. Venture Capital Due Diligence Process
16. Purchase of Business Due Diligence Process
17. Investment in Business Due Diligence Process
18. Loans for Business Due Diligence Process
19. Partnership in Business Due Diligence Process
20. Substantial Supply to Business Due Diligence Process
21. Financial and Accounting Due Diligence Process
22. Tax Due Diligence Process
23. Information Technology Due Diligence Process
24. Strategic and Commercial Due Diligence Process
25. Investor Due Diligence Process
26. Vendor Due Diligence Process

XIV Social Audit

1. Assessing the Social Performance of Corporate Enterprise
2. Assessing the Goal Oriented Performance of Government Utility Departments
3. Assessing the Social Performance of Government Sector Undertakings
4. Assessing the Social Performance of Government Departments
5. Assessing the Social Performance of Gram Panchayat Offices

6. Social Audit of Public Libraries
7. Social Audit of Employment Exchange Offices
8. Social Audit of Urban Local Bodies

XV Environmental Audit

1. Reviewing the effectiveness of Environmental Management.
2. Reviewing the compliance of an organization with all regulatory requirements and environmental performance.
3. Ensuring conformity with environmental assessment requirements.
4. Testing the accuracy of the assessment.

XVI Corporate Social Responsibility (CSR) Audit

1. Gain an understanding of Corporate Social Responsibility (CSR) issues that affect the organization and industry.
2. Understand CSR stakeholders and their needs.
3. Understand the economic value proposition and reputation drivers.
4. Examine how organizations approach: climate change challenges, health and safety issues, and supply chain imperatives.
5. Review of the CSR Programs – there consistency with the management philosophy and corporate goals.
6. Review emerging practices in social responsibility and sustainable development.
7. Examine CSR links to governance and risk management.
8. A CSR audit program can cover all or any of the following risks:
   - Effectiveness of the operating framework for CSR implementation.
   - Effectiveness of implementation of specific, large CSR projects.
   - Adequacy of internal control and review mechanisms.
   - Reliability of measures of performance.
   - Management of risks associated with external factors like regulatory compliance, management of potential adverse NGO attention, etc.
9. A guidance on social responsibility ISO 26000:2010 (Draft Stage) can be referred.

10. Network with your peers on this emerging area of internal audit focus.

XVII ISO 9000 Audit

1. The term *ISO 9000* has two different meanings:
   - It refers to a single standard (ISO 9000), and
   - It refers to a set of three standards (ISO 9000, ISO 9001, and ISO 9004).
2. All three are referred to as *quality management system standards*.
3. Two types of auditing are required to become registered to the standard: auditing by an external certification body (external audit) and audits by internal staff trained for this process (internal audits).
4. The internal audit programs comprises of five programs
5. The five programs comprise of
   - ISO 9001 *Compliance Audit Program*
   - ISO 9001 *Policy Audit Program*
   - ISO 9001 *Procedures Audit Program*
   - ISO 9001 *Process Audit Program*
   - ISO 9001 *Records Audit Program*

XVIII Cyber Audit

1. COBIT based Audits:
   - Reviews of Baselines and Standards for IT
   - Information System Implementations
   - Pre-Implementation Review
   - Implementation of Controls Certification Reviews
   - Post Implementation Review
   - Code Development / Source Code Management Reviews
   - General Controls Reviews
   - Data Center Reviews
   - Audits of the Business Continuity Program
   - Audits of Security Configuration

- Reviews of Security Administration
- Reviews of IT Purchasing and Procurement
- Application Review / Audits
- Audits of Business Processes

2. System Audit
3. Internal Audit of System Security Policy
4. Network Security Audit
5. Quality Management Systems Audit

XIX Industry Specific Internal Audit Programs (Illustrative List)

1. Educational Institutions
2. Information Technology Companies
3. Hotels
4. Hospitals
5. Stock Brokers
6. Portfolio Manager
7. Companies
8. Construction Company
9. Banks
10. Manufacturing Company
11. Insurance Company
12. Non Banking Finance Companies
13. Asset Management Company
14. Telecom Companies
15. Cooperative Societies

XX Assurance Services

1. Revenue Audit
2. Special Audit
3. Concurrent Audit

4. Income and Expenditure Audit
5. Grants Audit
6. Projects Audit
7. Investigative Audit
8. CAG Audit for PSUs
9. Diligence Report
10. Assurance On Sustainability Reporting

Understanding Various Opportunities in Internal Audit

I. Financial Audit

7.1 This type of audit involves a thorough review of a department's records and reports, in order to check that assets and liabilities are properly recorded on the balance sheet, and all profits and losses are properly assessed.

In financial audits, significance or materiality is usually defined as a monetary value. Consequently, planning decisions mainly involve the intended degree of audit assurance and the extent of audit work required to provide it. The requirements will vary from one organisation to another and applicable laws and regulations. Some activities common to most audits are as follows:

- Risk assessment
- Defining materiality
- Financial statement assertions
- Financial analysis of cash flow statement
- Compliance and substantiative procedures
- Analytical procedures

7.2 Meeting these objectives involves verification of:

- Revenue
- Sales
- Bank deposits
- Bank reconciliation
- Accounts payable
- Accounts receivable

- Disbursements
- Petty cash transactions
- Loans and Advances
- Assets

II. Operational Audit

7.3 This type of audit involves a thorough review of a department's operating procedures and internal controls. They deal with broad performance issues, focusing on whether funds and resources have been economically, efficiently and effectively managed to fulfill the mission and objectives. An operational audit includes elements of a compliance audit, a financial audit, and an information systems audit. In particular, management audits examine and report on matters related to any or all of the following:

- the adequacy of management systems, controls and practices, including those intended to control and safeguard assets, to ensure due regard to economy, efficiency and effectiveness;
- the extent to which resources have been managed with due regard to economy and efficiency; and,
- the extent to which programs, operations or activities of an entity have been effective.

Conducting Operational Audit

1. **Scope:** Unlike financial audit, the objectives and scope of operational audit are not so clear or well defined. The first step would be to brainstorm along with the client and define the scope and objectives of audit. It is also necessary to decide the exclusions to the scope.
2. **Set audit objectives:** The second step would be to set audit objectives. Appropriate audit evidence can be gathered only when objectives are clear. Three elements need to be identified-criteria, cause and effect. They will be concerned with whether the operating objectives will be met.

   Review and update the audit objectives after the preliminary survey.
3. **Set scope:** To manage expectations on what will be achieved by the audit by setting the boundaries of what will and will not be included.
4. **Gathering information:** The sources would be as follows:
   - Operating standards
   - Organisation chart

- Nature of operations
- Operating reports
- Senior management
- Prior audit papers, if available
- Internet
- Industry, trade journals and publications
- Files and papers

5. **Preliminary survey**: preliminary survey is essential to gain a working knowledge of the operation to be audited, to logically investigate and evaluate all information. It would be something like:
    - Information on overall business operations.
    - Develop a questionnaire for discussions with staff
    - Interview people within the operation
    - Learn the objectives, goals, and standards of the operation.
    - Ascertain any initial opportunities for improvement.
    - Understand the inherent risks and internal controls.
    - Learn about the people performing the operation –key personnel, job descriptions, evaluation methods
    - Physically inspect operations by touring the entity's facilities
    - Focus on possible cost savings from inefficiencies
    - Present the survey results

    Update (or create) audit objectives based on this larger information bases. Make the audit plan - time , resources and expertise required, audit programme, audit tests and identify audit risks

6. **Review of Internal Controls**: To determine what level of reliance can be placed on internal controls. This step takes place throughout the audit process. Methods to review would include
    - Responses of interviewing staff to control questions in the Internal Control Questionnaire would indicate areas of control weakness to concentrate on
    - Prepare flow charts or narrative descriptions
    - Walk-through and limited system testing
    - Evaluate policy and procedures manuals

    Results of Internal Control Review: This will provide information regarding the following:

- Identification of the controls that the auditor will rely on during detailed testing
- Analysis of the controls
- Evaluation of the appropriateness of the controls
- Risk Assessment

7. **Existence of controls:** It is important to consider whether there are any factors which might render controls ineffective.
   - Accidental or deliberate avoidance
   - Management override
   - Inadequate Backup and recovery
   - Environmental impact
   - Access control over computer systems

   A re-analysis of risk and budget time will need to be done at this stage..
8. **Detailed testing:** Carry out sufficient audit tests of compliance and substantiation to gain sufficient evidence on the objective of the audit. The testing is aimed at significant controls that have previously been assessed as adequate to evaluate their effectiveness, and those controls assessed as inadequate to verify that the required results are not being consistently achieved.
9. **Report:** the report should inform the recipients of the issues or opportunities for improvement and provide constructive means of achieving the goals.

III Grant Audit

7.4 Grant audits include financial and operational elements, but the focus is on compliance with the financial terms of grant agreements. Usually, when the grant is given, the receiver is obligated to review grants to determine whether funds are spent for the purpose for which the funds have been received.

Verification of Grants

1. Obtain copies of the Grant application and award documentation (grant file) which specify the purpose and scope of work to be done with the funds provided.

2. Review the reporting requirements, if any, included in the grant/sponsorship agreement. Determine whether the record keeping/ reporting process satisfies the requirements. Note discrepancies.
3. Determine whether there are limitations on the use of these funds and test to see if they were observed. Note any exceptions.
4. Verify that the amount of the grant noted in the above documentation was actually received and deposited in the bank account maintained for that purpose. Note any exceptions.
5. Ensure that any unused funds and/or interest earned are returned to the granting agency. Test to determine compliance with such requirements. Note discrepancies.

IV Project Audit

7.5 Project audits include review of project cost and performance terms. Usually, project is a large and complex activity and the entity may not have the appropriate internal expertise to negotiate and manage these contracts.

Whether it is a commercial business, government entity or a non-profit organisation, all of them face potential financial hazards of fiscal irresponsibility, theft, scams, substandard materials or labour. While the organisation finds it difficult to manage the project , it is the core competency of the contractors who have dedicated staff who help them secure best terms and maximise returns. As a result, many owners end up with ineffective expenditure controls for these projects and place too much reliance on their contractors.

Here the auditors come in. They work with project owners and advise the project owner through the lifecycle of the project as well as audit transaction documentation for compliance with the terms of the contract. They help in negotiating owner favourable contract , design and improve expenditure processes and controls; ensure the accuracy and proper documentation of for payment; ensure full value is received through monthly monitoring and on-site inspections; and reduce overall project costs.

Guidelines to Project Audit

7.6 Each organization is unique, and the audit would be based on assessment of internal controls and the limitations of the audit scope. However, certain issues such as economic justification, regulatory requirements, policies, and controls over contractor selection etc. should also be part of the audit package. Given below are few guidelines that can help auditors to reduce costs and minimize risks to their organizations.

1. Doing a cost benefit analysis: It is necessary that the auditor ask for documented evidence justifying the project to ensure that it is not the result of poor planning or wrong assumptions.
2. Regulatory requirements: It is essential to find out regulatory requirements affecting the project. The auditor should see that all clearances and certifications are obtained.
3. Administration of project: presence of internal control would go a long way in efficient management of construction activities.The auditor should see that following control issues are addressed :
    a. Review and approval process
    b. Project documentation and reporting
    c. Construction administration process, including a right-to-audit clause, change orders, substitutions, project overruns, and lien waivers.
    d. Bid and award process, including project size; contractor solicitation, reference, and selection; and controls over bid opening
    e. Management involvement and risk management.
4. Bid bonds: A bid bond guarantees that the contractor is insurable and can obtain a performance bond, which is procured after the bid is awarded. A contractor who does not have the financial strength to secure a bid bond will be unable to obtain a performance bond.
5. Adequate coverage by performance bond: In case the contractor fails to perform in accordance with a contract, the insurance company will reimburse the organization for the unfulfilled contract amount. If the contractor goes bankrupt, the proceeds of the bond are available to the owner to finish the project. Certain things need to be ensured in a performance bond:
    a. Whether there is a policy based on acceptable level of risk regarding performance bond based on acceptable level of risk (which is usually a monetary amount).
    b. Review whether bonds are for adequate amount and contract has not been broken into smaller parts to circumvent the requirement of bonds.
    c. Review whether senior management is consulted regarding performance bonding coverage limits.
6. Review liability coverage and other details: Ensure that the contractor has taken liability insurance. This provides the organisation protection if an accident or damage occurs as a result of action of any contractor's

employee.

a. Ensure that certificate of insurance is taken before the contractors commence work and retained till completion of project.

b. Ensure that Certificate is current and has not expired.

c. Review a sample COI for compliance with coverage in contract document.

d. Confirm that :

   i. General liability limits are adequate.

   ii. Workmen's compensation limits are appropriate.

   iii. Comments and exclusions section is appropriate.

   iv. the organization is named as the certificate holder.

   v. The certificate is signed by the insurance company.

   vi. The organization is listed as an additional insured under the "remarks section" of the COI. Being listed as an additional insured gives the organization added protection against an independent third party should someone be injured or property be damaged as a result of the contractor's operation on the organization's premises.

   vii. The insurance coverage minimums or limits stated in bid and contract documents are reasonable. Also determine when these documents were last updated. The risk management department, senior management, insurance agent, and legal counsel should periodically evaluate the insurance coverage requirements.

   viii. All organizational areas where contracted work can occur are identified.

7. Monitor or attend relevant meetings: Problems or significant issues can often be spotted in the minutes of the meetings.

8. Internal auditors should try to obtain invitations to as many relevant meetings as possible as direct observations can reveal much more than minutes, which may be filtered by the manager. Additionally, some safety issues may be prevalent, and the risk management or legal departments may have discouraged documentation of certain issues for legal purposes.

9. Look for accounting irregularities both intentional and unintentional: Find

out how projects are being coded in the general ledger account and determine whether the project should remain active. Coding to the wrong project, whether intentional or unintentional, can result in management decisions that are based on inaccurate data. Intentional coding to another construction project may be contrived to avoid scrutiny of a project-cost overrun and requisite approval and reporting.

Obtain construction project management reports and review contracted amounts, paid-to-date, and cost-to-complete to determine whether all liabilities have been properly recorded. A payment may have been made for materials that have not been received.

10. Guard against bid-related internal control breakdowns: Competitive bidding helps to ensure a wider choice of suppliers and products and higher quality goods and services at lower prices. A request for proposal, purchase order, or contract document provides adequate authorization for the purchase, clarifies the expectation of goods and services, and outlines the proper segregation of duties. This documentation also guarantees that a purchase decision analysis is made and documented for future reference.

Adherence to a sound system of internal control has never been more important, and the risks may never have been greater. Internal auditors should not be content to look only at contract payments. They should assess project-related exposures and implications from a broad perspective and act to protect and strengthen their organisations.

V Information Systems Audit

7.7 This audit consists of determining whether information systems adequately safeguard assets, maintain data and systems integrity, achieve organisational goals and internal controls are adequate to assure that business, operational and control objectives will be met and unwanted events will be prevented or detected and corrected in time.

Information System reviews include the following:

- Reviews of existing or new systems, before and after implementation, to ensure their security and that they meet the needs of users;
- Project management reviews to ensure controls are in place to mitigate project risks or to identify the strengths and improvements required for future projects;
- Organizational or operational reviews to ensure the organizations goals and objectives will be achieved; and,

- Specific technology reviews to ensure security and controls are in place.

VI Compliance Audit

7.8 Various programmes and contracts and grants have specific rules and regulations that must be followed in order to maintain funding. Audits in these areas are usually restricted to verification that recipients are in compliance with the established guidelines. Compliance audit would include compliances with:

- Laws and regulations
- Policies
- Standards
- Contracts

Compliance audit would entail:

- Gathering information about laws, regulations, and other compliance requirements.
- Understanding limitations of auditing in detecting illegal acts and abuse.
- Assessing the risk that significant illegal acts could occur.
- The auditor would design and perform procedures based on risk assessment that would provide reasonable assurance of detecting significant illegal acts.

Factors Affecting Risks

- complexity of laws and regulations
- newness of laws and regulations
- effectiveness of internal control in preventing and detecting illegal acts and acts of non-compliance.

Sources of Obtaining Information about Laws, Regulations, and Other Compliance Requirements

- Auditors' training and experience.
- Auditors understanding of the programme being audited may provide a basis for recognition that some acts coming to their attention may be illegal.

- Auditors' cannot determine whether an act, in fact, is illegal. However, auditors are responsible for being aware of vulnerabilities to fraud associated with the area being audited in order to be able to identify indications that fraud may have occurred.

Taking the Help of an Expert:

Auditors may seek help of legal counsel in

- designing tests of compliance with laws and regulations
- evaluating the results of those tests

Auditors also may find it necessary to rely on the work of legal counsel when audit objectives require testing compliance with provisions of contracts or grant agreements.

VII. Investigative Audit

7.9 Investigative assignments scrutinize allegations of wrongdoing or breaches of standards of conduct. Allegations may be internal or external to the organisation and may examine the records of individuals, organizations and firms with agreements between them and the organisation

Reasons for conducting Investigation:

- Internal theft,
- misappropriation of assets,
- conflicts of interest

Co-ordination for this audit is usually at the highest level in the organisation like with senior management or security department. Investigative audits differ from other audits because they are normally conducted without first notifying the personnel who may be affected by the findings.

VIII. Enterprise Risk Management

7.10 Risk is a concept used to express uncertainty about events and/or their outcomes that could have a material effect on the goals of the organisation. Every company that is in business has to take risks. In order to progress, a business entity has to identify risks, evaluate them, decide if they are at an acceptable level and, if they are not, design controls to respond to those risks. After controls have been identified to mitigate risks, the effectiveness of controls has to be evaluated on a regular basis. This is risk management.

Risk management has to be integrated into the organisation's culture and embedded in all its day-to-day and periodic activities. Enterprise–wide risk management is a structured, consistent and continuous process across the whole organisation. The overall responsibility for risk management lies with the Board.

Internal auditing activity's role with regard to Risk Management is to provide objective assurance to the board on the effectiveness of an organisation's ERM activities in managing key business risks and that the system of internal control is operating effectively. The Chief Audit Executive (CAE) has to ensure that the internal audit activity maintains its independence and objectivity when providing assurance and consulting services.

The Roles which Auditor Should NOT Undertake

- Setting the risk appetite.
- Imposing risk management processes.
- Management assurance on risks.
- Taking decisions on risk responses.
- Implementing risk responses on management's behalf.
- Accountability for risk management.

7.11 Internal auditors should provide advice, and challenge or support management's decisions on risk, as opposed to making risk management decisions. The nature of internal audit activity's responsibilities should be documented in the audit charter and approved by the audit committee.

Enterprise Risk Management (ERM) processes are essential to any organization for the purpose of management of risk and seizing those opportunities that enables the organization to achieve its goals and objectives. The process of ERM enables an organization to safeguard the assets and activities of the organization against possible dangers and risk factors in the process of doing its business. A preventive step is needed to protect the organization against the extremities that arise as a result of market movement

IX. Assurance on Sustainability Reporting

7.12 Sustainability means meeting the needs of present generation without affecting the ability of future generation to meet their own needs. Working for sustainability doesn't mean stop using of natural resources, which are essential to run a legitimate business. it only means to protect the wastage / misuse without forgetting that the long term survival of that business as well as many other businesses depends on those resources.

How an organization works towards protection of resources which are limited in supply so that the development may be sustained is important. One has also to establish equilibrium between the development and conservation of resources. The subject of Environmental accounting and reporting has emerged with this background only some times back and it has now become the most important part of sustainability accounting/ reporting.

Committed towards sustainable development, the management has to adopt a holistic approach to decision making in which all dimensions of sustainability i.e. Socio economic factors, eco-efficiency, environmental factors, etc., are given appropriate weight and consideration. It has to put in place such systems and procedures of reporting that reports, environmental and other impacts caused by company's products and services. This opens up varying degree of questions, *viz*.:

- What exactly we mean by Sustainability Accounting / reporting;
- What should be the format of reporting;
- Whether any assurance is require on such reporting and if so, what should be the principles applied while giving such assurance;
- How could sustainability reporting be correlated with the financial statements;
- Role of an accountant in sustainability accounting / reporting and providing assurance services.

Sustainability Accounting

7.13 Since early 90’s the world’s largest accounting bodies regional rganizations particularly in Europe have developed a serious thinking on these subjects and it has now been established that the accounting profession has been centrally involved in corporate sustainability. There is no clear cut definition of sustainability accounting developed so far, but one of the research report on the subject defines this as accounting for social economic and environmental aspects of decision making.

Effective Sustainability Reporting and Assurance

7.14 Sustainability assurance is an objective, systematic way for an organization to evaluate its environmental, social, and governance initiatives, including assessing how well its sustainability reporting processes are working and exploring how they can be improved.

Benefits of Improved Sustainability Assurance

- Greater understanding of current sustainability performance.
- Identification of areas for improvement arpund reporting processes and controls.

- Improved ability to meet investors and other stakeholder's expectations of accurate disclosure.
- Greater credibility among current and potential employees, business partners, and government regulators.
- Greater conformity to the standards of reporting under relevant frameworks.
- Enhanced corporate reputation with employees, investors, business relationships and government regulators due to an improved ability to provide more reliable informations and greater transperancy stemming from internal assurance.
- Improved monitoring of controls and processes related to environmental, social and governance metrics.
- Improved ability to maintain or achieve a sustainable business model.
- Increased awareness of and visibility into the contribution of sustainability activities to enterprise value.
- Improved decision making with integrated sustainability considerations.

X Revenue Audit

7.15 Revenue audit procedures allow an auditor to ensure that controls, policies and guidelines in a business entity's income-producing processes are adequate and effective. An auditor tests controls to detect significant weaknesses, and checks financial statements to ensure that such statements are in accordance with regulatory standards and generally accepted accountingprinciples.

Revenue Process

An auditor gains knowledge about a business entity's revenue process by inquiring from the entity's management and segment heads. A revenue process describes controls, guidelines and procedures a corporate uses to earn income from its activities. Such a process includes check receipts, sales discounts, non collectable items and accounts receivable--amounts owedbycustomer.

XI Special Audit

7.16 The government may order a special audit conducted on a corporation if there is evidence that its financial affairs are not being run in accordance with proper accounting practice. Shareholders of a company may also pass a resolution to have a special audit done on their company if they feel recent management decisions have gone haywire.

The nature of audit opinion given in a special audit can be classified under four categories and they are as follows:

- Qualified Opinion - Situations that make an auditor give a qualified opinion report include when a company's financial statements have failed to include certain transactions over a certain period or to reflect depreciation in the value of asserts.
- Unqualified Opinion – A special audit report whose conclusion is that the financial records of the company are in order. This means that the company management has presented a true reflection of the real financial transactions without hiding some or exaggerating others. The company's financial reporting has complied with the Generally Accepted Accounting Principles (GAAP).
- Adverse Opinion – Where an auditor discovers outright distortions that make the financial statements of a company unreliable, he issues an adverse opinion
- Disclaimer of Opinion – Such an opinion is issued when an auditor is not in a position to offer an opinion.

XII Audit of Public Sector Undertaking

7.17 An effective public sector audit activity strengthens governance by materially increasing citizens' ability to hold their government accountable. Auditors perform an especially important function in those aspects of governance that are crucial in the public sector for promoting credibility, equity, and appropriate behavior of government officials, while reducing the risk of public corruption.

- Therefore, it is crucial that government audit activities are configured appropriately and have a broad mandate to achieve these objectives.
- The audit activity must be empowered to act with integrity and produce reliable services, although the specific means by which auditors achieve these goals vary.
- A PSE audit activity requires:
  - i. Organizational independence
  - ii. A formal mandate
  - iii. Unrestricted access

iv. Sufficient funding

v. Competent leadership

vi. Competent staff

vii. Professional audit standards

- Governments must establish protections to ensure that audit activities are empowered to report significant issues to appropriate oversight authorities. One means of accomplishing this protection is through creation of an independent audit committee.

Public sector governance encompasses the policies and procedures used to direct an organization's activities to provide reasonable assurance that objectives are met and that operations are carried out in an ethical and accountable manner. In the public sector, governance relates to the means by which goals are established and accomplished. It also includes activities that ensure a government's credibility, establish equitable provision of services, and assure appropriate behavior of government officials — reducing the risk of public corruption

XIII Audit of Stock Brokers

7.18 The Securities and Exchange Board of India (Sebi's) issued directives to the exchanges to carry out internal audits of their stockbrokers and clearing members, the National Stock Exchange (NSE) has asked its brokers and members to appoint an internal auditor for carrying out audits of their operations in all segments of the exchange.

The purpose of such audits is to ensure that books of account and other records and documents are being maintained in the manner required under stipulated SEBI Act. These audits are also required to ascertain if adequate internal control systems, procedures and safeguards have been established and followed by intermediaries to fulfil their regulatory obligations. Internal auditors are required to submit their reports within three months from the end of a half-year period.

While asking its brokers and members to follow the SEBI directive, NSE warned that non-submission of internal audit reports would be treated as non-compliance and appropriate action would be initiated against members concerned. In case the quality of an audit is found unsatisfactory, the exchange would advise the members concerned to change their auditors.

Stock Brokers

7.19 Stock Broker plays an important role in helping both the seller and the buyer of the securities to enter into a transaction. The buyer and seller may be either a broker or a client. The transaction so entered cannot be annulled except in the case of fraud, willful misrepresentation or upon prima-facie evidence of a material mistake in the transaction, in the judgment of the authorities.

The stock broker, while executing a order, may on behalf of his client buy or sell securities from his own account i.e. as a principal or an agent. For each transaction the stock broker has to issue necessary contract note indicating whether the transaction has been entered into by him as a principal or as an agent for another. While buying or selling securities as a principal, the stock broker has to obtain the consent of his client and the prices charged should be fair and justified by the conditions of the market.

A stock broker, thus, being a vital link between the regulators, issuers and investors, any aberrations in the capital markets has presumably direct bearing on the stock brokers, his governance processes and practices which in turn affect the confidence of the markets and investors. It is, therefore, convincingly argued that the persons who operate in the market are required to maintain high standards of integrity, promptitude and fairness in the conduct of their business dealings. It is, therefore, necessary that stock brokers put in place processes to ensure good governance practice and also to have constant monitoring and surveillance on the acts of intermediaries.

Objectives of Internal Audit

7.20 The objective of internal audit of stock brokers are as follows:

(i) to ensure that the books of account, records (including telephone records and electronic records) and documents are being maintained in the manner required under SEBI Act, 1992, SCR Act, 1956 and SEBI (Stock brokers and Sub-brokers) Regulations, 1992.

(ii) to ascertain to whether adequate internal control systems, procedures and safeguards have been established and are being followed by the intermediary to fulfill its obligations within the scope of the audit.

(iii) to ascertain to whether any circumstances exist which would render the intermediary unfit or ineligible.

(iv) to ascertain whether the provisions of the securities laws and the directions or circulars issued thereunder are being complied with.

(v) to ascertain whether the provision of stock exchange bye-laws, notices, circulars, instructions or orders issued by stock exchanges are being complied with.

(vi) to inquire into the complaints received from investors, clients, other market participants or any other person on any matter having a bearing on the activities of the stock broker.

PART VIII

PROFESSIONAL OPPORTUNITIES IN INTERNAL AUDIT - *IN DETAIL*

I. Audit of the Internal Control Framework

1. Cash and Bank Balance
2. Capital
3. Debenture and Long Term Loans
4. Creditors, Accruals, Provisions
5. Contingent Liabilities
6. Purchase and Other Expenditure
7. Sales and Other Income
8. Fixed Assets
9. Investments
10. Debtors, Prepayments, Accrued Income
11. Stock and WIP
12. Wages and Salaries
13. Bank Branches
14. Bank Head Office/ Central Office

1. Cash and Bank Balance

(a) Confirm selected bank accounts and special arrangements

Select bank accounts for confirmation in order to obtain a moderate to low level of assurance that the aforementioned audit objectives are achieved. Bank confirmations should be sent to all banking relationships to identify accounts not included in the general ledger.

Confirmation requests should be sent under our control and, second requests and, where warranted, third requests should be mailed when responses to confirmation requests have not been received within a reasonable time.

Consider sending a special inquiry letter to ascertain the existence of special arrangements or restrictions, for example, compensating balance arrangements, security arrangements, written guarantees.

(b) Review confirmation replies

For confirmations returned:

a) agree account information and account balance to comparative summary;

b) investigate all discrepancies reported or questions raised in review and determine whether any adjustments are necessary; and

c) assess impact of special arrangements or restrictions identified and determine whether disclosure is appropriate.

(c) Test accounts where there is no confirmation

In the unusual situation where we do not receive a bank confirmation and are willing to forego the receipt of the bank confirmation, consider performing the following procedures to obtain a high level of assurance that the aforementioned audit objectives are achieved:

a) obtain subsequent month bank statement, bank reconciliation and supporting documentation. Consider obtaining information directly from the bank;

b) test the mathematical accuracy of the bank reconciliation; (accuracy)

c) trace outstanding items listed on the bank reconciliation to the subsequent month's bank statement and for those not traced, trace to the cash disbursements records for the period prior to the balance sheet date; (accuracy and existence/occurrence)

d) trace deposits in transit listed on the bank reconciliation to the subsequent month's bank statement and for those not traced, trace to the cash receipts records for the period prior to the balance sheet date; (accuracy and existence/occurrence)

e) obtain explanation for large, unusual reconciling items and trace to supporting documentation and/or entries in the cash records, as appropriate; (accuracy and existence/occurrence)

f) review the date the above items cleared the bank or were recorded in the client's books to ensure appropriate recording period. Trace to supporting documentation as necessary; and (cut-off)

g) investigate items such as, long outstanding items, dishonoured checks and significant adjustments in the subsequent month, and record adjustments as necessary. (accuracy and existence/ occurrence)

(d) Test bank reconciliations

Test bank reconciliation in order to obtain a moderate to low level of assurance that the aforementioned audit objectives are achieved by performing the following:

a) test the mathematical accuracy of the reconciliation; (accuracy)

b) trace book balances on the client's bank reconciliation to the comparative summary; (accuracy)

c) trace bank balances on the client's bank reconciliation to the bank statement; (accuracy)

d) test reconciling items on the bank reconciliation by performing the following:

   i) obtain subsequent month bank statement and supporting documentation. Consider obtaining information directly from the bank;

   ii) trace outstanding items listed on the bank reconciliation to the subsequent month's bank statement and for those not traced, trace to the cash disbursements records for the period prior to the balance sheet date; (accuracy and existence/occurrence)

   iii) trace deposits in transit listed on the bank reconciliation to the subsequent month's bank statement and for those not traced, trace to the cash receipts records for the period prior to the balance sheet date; (accuracy and existence/occurrence)

   iv) obtain explanation for large, unusual reconciling items and trace to supporting documentation and/or entries in the cash records, as appropriate; (accuracy and existence/occurrence)

   v) review the date the above items cleared the bank or were recorded in the client's books to ensure appropriate recording period. Trace to supporting documentation as necessary; and (cut-off)

   vi) investigate items such as, long outstanding items, dishonored checks and significant adjustments in the subsequent month, and record adjustments as necessary (accuracy and existence/ occurrence).

   vii) review client's bank reconciliation for review and approval by appropriate management and timely completion of reconciliation.

2. Capital

Equity Share Capital

Share capital is that is not a preferential. In other words it is the basic kind of capital or an ordinary share capital.

Preferential Share Capital

This part of capital has the following characteristics:

It carries a preferential right as to the payment of dividend over other type of capital.

It carries the preferential right as to payment of capital in case of winding up or repayment of capital over the over the other type of capital.

Special Points in Audit of Share Capital

In case of share capital issued by the company, following points merit consideration of the auditor:

- Authorization of the issue – Auditor should check the minutes of the meeting of the board of directors to check the authorization of the terms of the terms of the issue of share capital.
- Vouching share applications – Auditor should test check the share application forms and vouches their respective entries in the cashbook.
- Legal requirement - "It should be checked that the legal requirements as laid down by the companies act, SEBI and other regulatory bodies are met.
- Compilation requirements - Auditor should check that various compilation requirement of various statements with the registrar of companies are met with. While doing the audit of share capital, auditor should vouch the following carefully:
    - Memorandum of association
    - Articles of association
    - Minutes of the directors meetings
    - Prospectus
    - Share application form
    - Letters of allotment
    - Letters of refund
    - Share registers
    - Cashbook
    - Ledger accounts.

Issue of Shares at A Premium

When a company issues its share at a premium, auditor should take care of the following points:

- He should check the prospectus.
- He should check the articles of association.
- He should check the minutes of the meetings of the board of directors.
- All the above should authorize the issue of shares at a premium.
- The receipt of premium should be vouched with the respective entries in the books of accounts.
- It should be vouched that the share premium account should be used for the authorized purposes only.

3. Debenture and Long Term Loans

Audit of Debenture and Long Term Loans involves determining:

a. All borrowings and other indebtedness have been properly recorded and represent valid liabilities of the entity at the balance sheet date.

b. Deferred debt discount or premium is properly recorded at the balance sheet date.

c. All executory or "off-balance sheet" obligations have been identified and considered (e.g., operating leases, product financing arrangements, take-or-pay contracts and throughput contracts).

d. Borrowings and other indebtedness are properly described and classified and adequate disclosures (including disclosures related to collateral, debt covenants and terms of repayment) with respect to these amounts and disclosures related to off-balance sheet financings have been made.

Substantive Procedure

- Compare the account balances with those of prior periods and investigate any unexpected changes.
- Review reasonableness of total interest expense for the period and amount accrued at year-end.
- Review minutes, agreements and bank and other confirmations replies for evidence of the existence of loans.
- Obtain list of lenders from client indicating the addresses of the lenders and circularize confirmations.

- Prepare confirmation control sheet and confirmation summary.
- Obtain reconciliation of any difference in the amounts, confirm and test its accuracy and propriety.
- Send reminders if necessary or cover in covering letter as a condition for signatures if the confirmations are not received.
- Ensure that confirmation received from lender:
    i. Is addressed to and received directly by FRSH through post;
    ii. Does not contain any unusual remarks by the lender;
    iii. Balance shown in their reply matches with the books of accounts and if not, the reconciliation is adequately provided;
    iv. Repayment period; and
- Clearly specify the interest / mark-up rates, security and any other details which should coincide the terms of loan agreement.
- Obtain a PBC roll forward of redeemable capital and loans payable, including description, stated or average interest rates, maturity dates, description of collateral, average and yearend balance, current and long-term portion, accrued interest and estimated interest expense. Foot and trace the total(s) to the lead schedule. Review for large/unusual items
- Test classification of debt by reference to debt instruments or confirmations. (Scope/Sample: __________.)
- Using a PBC, test the schedule of payments for each of the next five years and in total thereafter. (Scope/Sample: __________ .)
- Have the client prepare or update debt compliance carry forwards. Tie to support and discuss with management. Conclude as to company's compliance with debt covenants.
- Complete loan covenant checklist for each type of loan.
- Have client obtain written waivers of debt covenant defaults as necessary. Review for adequacy. Prepare support for financial statement disclosure.
- Inspect original or authenticated copies of loan agreements or other related documents to determine the terms, restrictions and other pertinent provisions of the loans.
- Ensure that the debt agreement made between the Company and the lender is adequate and that:

- It is made on the stamp paper;
- It is duly authorized by the notary public;
- It is signed by both the parties to the agreement and witnessed;
- Official stamp of both the parties to the agreement;
- Agreement is not expired during the period under review;
- The terms and conditions of such loans are compatible with normal business norms;
- Adequate security is provided by the Company to the lender;
- The terms and conditions are not vague;
- It is approved by persons authorized by the Company to do so; and
- The relevant clauses of the agreement are not questionable

- Review calculations and other evidence relating to compliance with the terms, restrictions or other provisions of loan agreements.

Securities and Pledges

- Identify liens, securities, charges, mortgages and pledges as loan collateral by confirmation with creditors and/or the appropriate public filing offices or by inspection of public records.
- Ensure that the security of loans i.e. mortgage of assets, stock etc. are not disposed off without prior approval of the lending Company.

Restructuring

- Review refinancing/restructuring agreements subsequent to the balance sheet date to determine their effects on balance sheet classifications or on disclosures.
- Ensure that the debt agreement is not rescheduled on frequent intervals and specially when Company is out of funds.

Interest and Financial Charges

- Perform a predictive testing on interest paid and accrued during the period.
- Cross-refer to relevant portion of working papers.

Related Parties

- Have the client prepare a detailed listing of any related-party borrowings as of the balance sheet date. Obtain an understanding of the nature of each transaction and its business purpose.
- Be alert for indications of related-party borrowings in review of minutes, debt agreements, attorney invoices, etc.
- In case of debts from Associated Companies, ensure that the Boards of Directors approves such loan in its meeting and the terms and condition are in accordance with the general business norms.
- Ensure that in case of balances and amounts outstanding towards related parties all the requirements of SRO 66 dated January 22, 2003 issued by SECP have been complied with.

Foreign Debts

- In case of foreign debts, ensure that these have been received through appropriate banking channels without violating Foreign Exchange Regulations Act
- Ensure that all liabilities in foreign currencies are re-translated at the exchange rate prevailing on the balance sheet date.
- Ensure that hedge accounting practices in accordance with IAS-39 have been performed with regard to any balances covered under foreign exchange contracts.
- Have the client prepare a schedule of re-translation, from rate at initial recognition and at balance sheet date/contract rate, of all liabilities. Cross-refer exchange differences with financial charges/other income.
- Where the company uses forward exchange contracts, such contracts should be accounted for as assets and liabilities. Gains and losses on such financial instruments used for hedging of foreign currency transactions should be recognized as income and expense on the same basis as the corresponding hedged item. Foreign exchange contracts are translated at exchange rates prevailing at the balance sheet date (representing their fair value).

Issue of Debentures

- Ensure that all the relevant legal requirements have been fulfilled at the time of issue of debentures/TFCs etc, particularly when these are listed.
- Ensure proper treatment of issue cost of such securities in light of IASs

4. Creditors, Accruals, Provisions

Audit of creditors, accruals and provisions involves the following steps

(a) Checking the internal control measures

(b) Identifying the objectives of audit

(c) Verifying creditors and accruals,

(d) Verifying purchase and leasing creditors

(e) Deferred Income analysis

(f) Verifying unpaid wages and salaries

(g) Verifying compliance of law

5. Contingent Liabilities

(a) Verifying disclosure requirements for contingent liabilities and other liabilities

(b) Verifying compliance with law

6. Purchase and other Expenditure

(a) Check the Internal Control Measures

(b) Determining the Objectives

(c) Verifying the recording of expenditure

(d) Verifying the genuineness of expenditure posting

(e) Verifying consistent accounting policies

(f) Verify proper disclosures

7. Sales and other income

(a) Checking of internal control measures

(b) Determining the audit objectives

(c) Verifying the recording of income

(d) Verifying the genuineness of income recording

(e) Verifying consistent accounting policies

(f) Verifying proper disclosure

8. Fixed Assets

(a) Check the internal control measures

(b) Determing audit requirements
(c) Verifying the existence and accounting of all assets
(d) Verifying land and building
(e) Verifying other assets
(f) Verifying intangible assets
(g) Verifying valuation and disclosure
(h) Depreciation

9. Investments

(a) Check the internal control measures
(b) Determing audit requirements
(c) Verfiying recording of investments
(d) Verifying accounting for investments
(e) Verifying valuation of investments
(f) Verifying proper disclosure

10. Debtors, Prepayments and Accrued Income

(a) Check for internal control measures
(b) Determining objectives of audit
(c) Verifying sales ledger debtors
(d) Verifying accounting of other debtors
(e) Verifying prepayment and accrued income
(f) Verifying provisions made
(g) Verifying disclosure requirements
(h) Audit of debtors balance

11. Stock and WIP

(a) Checking of internal control measures
(b) Objetives of the internal control measures
(c) Verifying that that recorded stock represented existing stock
(d) Verify the fair valuation of stock
(e) Provisions for foreseeable losses
(f) Verofy compliance under company law and accounting standards

12. Wages and Salaries

(a) Check the internal control framework

(b) Verifying the recording of wages/salaries

(c) Analytical review if wages and salaries

13. Bank Branch Audit

(a) Checking of cash and sage custody

(b) Checking of godowns

(c) Inspection of stocks hypothecated to the bank

(d) Checking of documents

(e) Checking of insurance

(f) Balancing of borrowers ledgers

(g) Checking of limits sanctioned

(h) Valuation of stocks pledged and hypothecated

(i) Drawing power of borrowers

(j) Clean advances or temporary advances

(k) Checking of bills purchased

(l) Advances under suits or decree

(m) Balances with other banks

(n) Gaurantees issued by the bank

(o) Payments made on account of branches

(p) Head Office account

(q) Purchase and sale of capital assets

(r) Checking of deposits

(s) Current account verification

(t) SB/ Term deposits/Recurring deposits

(u) Sundry Creditors

14. Bank Head Office/ Central Office Audit

Audit involves the following functions:

(a) Investments and returns thereon

(b) Reconciliation of inter-branch accounts

(c) Purchases, printing and despatch of stationary to the branches

(d) Purchase and supply fixed assets

(e) Borrowing from other banks

(f) Reserve

(g) Internal Audit Report

(h) Renewal of Limits

(i) Establisment of Head Office

II. Stock Audit/ Credit Audit

1. Meaning of Inventories

Inventories denotes 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 consumables stores and spare parts meant for replacement in the normal course.

Inventories thus normally comprises of :

a) stores,

b) spares parts,

c) loose tools,

d) maintenance supplies,

e) raw materials including components,

f) work in process,

g) finished goods including by-products,

h) waste or by-products, etc.

Meaning of Debtors

A debtor represent the amount due to an entity for goods sold or a service rendered or in respect of other similar contractual obligations but amount includes such amounts which are in the nature of loans and advances. Debtors are represented only by documentary evidence in the form of invoices and they don't have any physical existence.

Cash-Credit Facility

A major part of working capital requirement of any unit would consist of maintenance of Inventories of raw materials, semi-finished goods, finished goods, stores and spares etc. In trading concern the requirement of funds will be to maintain adequate inventories in trade. Finance against such inventories by banks is generally granted in the shape of cash credit facility where drawings will be permitted against Inventories of goods. It is a running account facility where deposits and withdrawals are permitted.

Cash credit facility is of two types (depending upon the type of charge on goods taken as security by bank.)

(i) **Cash credit - pledge**: When the possession of the goods is with the bank and drawings in the account are linked with actual movement of goods from/to the possession of the bank. The physical control of the goods is exercised by the bank.

(ii) **Cash credit- hypothecation**: when the possession of the goods remains with the borrower and a floating charge over the inventories is created in favour of the bank. The borrower has complete control over the goods and the drawings in the account are permitted on the basis of Inventories statements submitted by the borrower.

2. Inventories/ Receivables Audit

The term Inventories Audit in the context of banks refers to verification and valuation of the entire gamut of current assets, current liabilities, loans and advances, diversion of funds, application of funds, accuracy of Inventories statements, arriving at the revised drawing power and any other matter connected with the credit administration by the banks.

The main thrust in Inventories audit therefore, is towards authentication of the quantity, quality, composition and valuation of the Inventories and debtors.

Audit of inventory is undertaken for two major purposes:

- Audit of stocks of entity for financial reporting - verification as part of existence of assets and maintenance of records

- Stock audit from the view point of the lender/ banks

The difference in objective of the audit makes the process of audit different for both purposes hence they are discussed separately below.

Objectives and Scope of Stock Audit

The various purposes expected to be achieved through stock audit may be summarized as follows:

- To ensure proper preservation/ storage and handling of stock.
- To identify whether there exist any obsolete stock & if yes, whether it has been segregated & written off.
- To verify whether the stock is adequately insured against fire and other natural calamities (in appropriate cases against other risks like theft, burglary, marine, riots etc. as per sanction).
- To ascertain whether physical stock tally with the stock statement submitted to the banker.
- To ascertain whether hypothecated stock is realizable.
- To confirm that stock is owned by the borrower and finance is made against value of paid stock only.
- To examine the age wise debtors outstanding as per books and as per statement submitted by the bank, steps taken for recovery of long pending debtors and likely instances of debtors turning bad, if any.

Like any other audit, the rationale for conducting Inventories Audit also lies in prevention and early detection of frauds and errors. Inventories audit acts as a safeguard against occurrence of both Internal and External frauds.

Scope of Inventories audit

The scope of the audit covers all the aspects that have a direct impact on the working capital of the unit as well as the aspects relating to Inventories that have a bearing on the bank finance. In other words, it deals with the matters that have an effect on the security and liquidity in view of the banker.

It encompasses the following aspects:

a) Physical verification of inventories.

b) Verification of condition of storage.

c) Valuation of inventories and pointing out variances.

d) Valuation of obsolete / non-moving Inventories.

e) Age-wise categorization of inventories.

f) Evaluation of the Inventories management by the company.

g) Reconciliation of Inventories statements submitted with the accounting records maintained by borrowers particularly, relating to quantity, rate, value of inventories, age, marketability, etc.

h) Verification and evaluation of sundry creditors indicating separately those relating to Inventories and their relationship with bank finance.

i) commenting upon the sources of the raw materials, i.e., whether any credit is available for the material and which of the items are available against cash payments.

j) Review of the Inventories valuation system.

k) Age-wise and value-wise qualification of debtors.

l) Determination of the drawing power.

m) Determining adequacy of the insurance cover.

n) Verification of documents/ securities.

o) Commenting upon the comparative Profitability and Inventories ratio.

p) Ensuring that the compliance of the terms and conditions of limit sanctioned.

q) Verification of transactions with sister concerns, unsecured Loans to Directors and others.

r) Any other matters of interest to the bank.

Need for Audit

An Inventories audit is essential for the following purposes:

1) To give the bankers an assurance regarding the following:

    a) That a suitable environment for preservation of Inventories exists.

    b) That a responsible person for safeguarding the Inventories is always present.

    c) That degraded Inventories have been written off.

    d) That adequate safeguards exist against fire and natural calamities.

    e) That physical inventories tally with the Inventories statements submitted to bank.

    f) That the pledged/hypothecated Inventories is realizable.

   g) That Inventories is owned by the borrower.
   h) That all sanction terms have been adhered to.
   i) That inventories are not stagnating and becoming obsolete.

2) To investigate, wherever the party is not submitting periodic Inventories statements regularly.
3) To investigate, where the accounts have been marked as substandard.
4) To find out reasons when there are too many qualifying remarks about inventories and receivables in the Auditor's report on the Balance Sheet of the borrower.
5) To find out suspect dealing in lending procedure.
6) To make the banks aware of their right of enforcement of the security interest provided in the Securitization and Reconstruction of Financial Assets and enforcement of Security Interest Act, 2002.
7) To fulfill Head Office requirement

Classification of Stock Audit

1. Stock audit for bank borrowers
2. Stock audit other than bank borrowers

Applicability of Stock Audit

Under the following circumstances it is advisable for banks to get annual Inventories audit done by the independent Agencies-

a) Where there are over dues in term loans or other accounts, where the banks' stake is high.
b) Where there is evidence of pressure on the borrower from the creditors.
c) Where the inventories are stagnating.
d) Where party is not submitting period Inventories statements regularly.
e) Where there are grounds to suspect that the position of chargeable current assets indicated may not be correct.
f) Where there are too many qualifying remarks about inventories and receivables in the auditors report on the balance sheet of a borrower.
g) Where the accounts is marked as sub-standard.
h) Suspect dealings in lending procedure, jeopardizing advances given.

i) An errant borrower, where Inventories audit is needed to supplement actions of the branches for recovery.

j) Any other valid reason such as mismanagement, heavy losses, lockout, strikes etc.

k) Fulfilling the criteria fixed by the head office to get done Inventories audit.

Special considerations while conducting Stock Audits.

i. If the stock statement as shown in the hypothecation statement does not tally with the stocks as in the balance sheet , then appropriate action should be taken to find reasons for the differences

ii. It should be seen that the stocks have been properly valued.

iii. It should be seen that Current Assets are not over-stated.

iv. It should be seen that the Turnover is not over-stated.

v. It should be seen that the stocks that are genuinely owned by the borrower are shown in the accounts

Steps involved in Stock Audit

Stock audit is necessarily required to be conducted at the borrowers place for obvious reasons. But before visiting the borrower, understanding the entity, its banking operations and financial affairs is must.

Therefore, it is advisable to visit the respective branch where the borrower is having the account so as to gather the information relating to Sanction, account operations, nature of business, performance of the borrower and other fundamental information along with the comments / observations noted by other auditors (like Internal Inspectors, Concurrent Auditors etc) to have a brief understanding about the borrower and its financial affairs.

Visit to Borrower's Branch:

- Banks generally has the system of maintaining two folders (in few cases only one folder) for each borrower of which one is used for keeping original documents executed by the borrower (viz. Demand Promissory Note, Hypothecation Deed, Guarantee Bond etc.) while other folder contains Application form, project report, Sanction Letter, Audited Financial Statements, previous stock audit report etc. Stock statements submitted each month by the borrower are filed with the correspondence file or may be kept in a single file meant for keeping stock statements of all the borrowers. Scrutiny of both the files along with the account operations and DP Register with reference to terms of Sanction helps stock auditor to gain insight about the borrower' affairs and conduct of the account.

Visit to borrower and verification of stock:

- Once the basic information is collected from the bank branch, it is time to visit the borrower. It is advisable to carry audit questionnaire at the time of visit so that no important point / area is missed out. Visit to borrower involves verification of stock and debtors, inquiry about MIS and internal control, future projections and financial plans of the borrower and analysis of past results and bank operations.
- Although audit is related to stock and debtors only, understanding of overall financial scenario and inquiry as to sister concerns & their businesses may also help the stock auditor to finalize the report in a better manner.

Preparation of Audit Report and discussion about audit findings.

- After conclusion of visits, stock audit report in the prescribed format, if available is to be prepared. In the absence of format, questionnaire prepared can itself also act as a report format. However, at the end of the questionnaire or in the covering letter itself (where auditor has to report in bank specified format) summary of major adverse findings (or points for future action) must be submitted by the auditor. Before submission of audit report, discussion about audit findings with the monitoring branch as well as borrower may be a good practice which may bring further clarity in reporting. But, it should be done depending upon the circumstances of case in hand.

Format for Stock Audit

Format for stock audit report may vary from bank to bank. Some banks have customized stock audit report formats while others may hint only the important areas to be reported by stock auditors. Irrespective of the formats, it is good to have questionnaire to be prepared by stock auditor covering following important areas of stock audit :

- Compliance with terms and conditions of sanction.
- Timely and adequate submission of stock statements and other important financial information.
- Account operations – overdrawing, credit summation and cash withdrawals.
- Drawing power calculations by banks and by the auditors & discrepancies, if any along with the reasons.

- Physical maintenance and storage of stock and adequacy of facilities at the borrowers place.
- Systems/ procedures implemented by borrower to identify the slow and non-moving stock items.
- Borrower's Management information system, its adequacy & Internal controls to safeguard stock.
- Method of valuation of stock, time interval for valuation and adequacy & sufficiency of procedures thereof.
- Insurance of stock.
- Verification of Debtors.

The list of common irregularities / observations given below will give the better idea about preparation of stock audit questionnaire on above stated areas.

Common Irregularities/ Observations in Stock Audit

The common irregularities that may be observed by the CA firm during stock audit can be summarized as follows:

Observations about statement submission and Scrutiny	Observations about account operations	Observations about Insurance coverage
• Stock Book Debts statements not submitted/ not submitted in time. • Inadequate details *viz.* rate, quantity and amount of different type of stock items not stated in the statement. • Scrutiny of stock statements not done. • DP Register not written up to date. • Age wise analysis of Debtors not	• Operations in the accounts not scrutinized with reference to projections, QIS statements, audited accounts etc. • Defects pointed out by the Internal Auditors / Inspectors / Concurrent Auditors are not complied with. • No / belated review / renewal of A/c. • All sales as per financial statements not routed through account.	• Under insurance of stock. • Insurance expired and not renewed. • Premium for renewal policy paid but policy not on record. • Insurance Policy without Bank Clause. • No coverage of all risks as per sanction. • Wrong items/ description of goods on insurance policy.

<table>
<tr><td>given/ done. Debtors over 90 days (or as per sanction) considered for drawing power.
• Drawing power not correctly calculated.
• Latest visit report by branch official not on record.</td><td>• Account not operated actively.
• Cash withdrawal during current period is abnormal.
• Frequent overdrawing in the account.
• Balance over drawing power although within Sanctioned Limit.</td><td>• Location of goods wrongly stated.
• All locations of stock not covered.</td></tr>
<tr><th>Observations about verification of stock and creditors</th><th>Observations about verification of Sundry Debtors</th><th>General Observations</th></tr>
<tr><td>• Stock book not maintained/ not updated.
• Obsolete stock not excluded from stock figures submitted to bank.
• Deteriorating stock turnover ratio.
• Stock figures submitted at the year end and as per financial statement not matching.
• Stock debtors as per statements submitted and as per books not matching.
• Confirmation for inventory with third party not obtained or physical verification of Inventory not done.
• Material received</td><td>• Existence of long pending debtors.
• Long pending debtors shown as below 90 days debts to bank.
• Increase in the average collection period of debtors.
• Dispute with debtors and pending court cases.
• Amount receivable from Sister concern considered for calculation of drawing power.
• Advances received from debtors not reported resulting into lower DP than calculated by bank.</td><td>• Diversion of funds and inter account transfers are not properly monitored.
• Borrower having operations with other bank for which permission of lender not obtained.
• Bank name plate not displayed.</td></tr>
</table>

from third parties for job work not excluded while calculating drawing power.		

Above list is illustrative only and not the exhaustive one. In actual practice, there may be other observations / irregularities over and above stated in the list.

Appointment of Stock Auditors and Period of Audit

The appointment of stock auditors is generally made by the regional or zonal offices in case of nationalized banks, while in case of co-op banks sometimes concurrent auditors only are asked to conduct stock audit of select borrowers of the branch. Terms of appointment are prescribed by such offices which sometimes involves conducting of stock audit as one time exercise only while in others it may be a contract for two half yearly visits during a particular financial year, of which first visit to be conducted before September and second visit before March. The stock audit involves audit of latest stock and debtors information of the borrower and the report should give the position of stock and debtors ideally on the date of visit. Further it will also make examination of past data submitted by the borrower to the bank and appearing in the books of accounts of the borrower, to check reliability of information submitted by the borrower.

III. Concurrent Audit

The concept of concurrent audit has been introduced to reduce the time gap between occurrences of transaction and its overview or checking. The concurrent audit serves the purpose of effective control as it is normally conducted by external agencies like chartered accountants firms.

Concurrent audit is an examination, which is contemporaneous with the occurrence of transactions or is carried out as near thereto as possible. This concurrent audit is essentially a management process integral to the establishment of internal accounting functions and effective controls and setting the tone for a vigilance internal audit to preclude the incidence of serious errors and fraudulent manipulations. The main focus while conducting concurrent audit it to ensure that transactions are not dealt with in routine but in adherence with the systems and procedures laid down.

The main objectives of concurrent audit include that any violation of procedure is brought to light:

- Assessing overall performance of the branch while assessing productivity and profitability and to offer useful comments on the basis of audit conducted.
- Restriction of matter discussed on the spot with the help of concerned official.
- Reporting any inefficiency in any operational level.
- Reporting any irregularity in working which may result in financial or other loss to branch.

The auditor will necessarily have to see whether the transaction or decisions are within the policy parameters laid down by the Head Office, they do not violate the instructions or policy prescriptions of the RBI, and that they are with in the delegated authority and in compliance with the terms and conditions for exercise of the delegated authority. In every large branch, which has different divisions dealing with specific activities, concurrent audit is a means to help the in-charge of the branch to ensure on an ongoing basis that the different divisions function within laid-down parameters and procedures.

IV. Due Diligence

1. Introduction

Due Diligence is the process of evaluating a prospective business decision by getting information about the financial, legal, and other material (important) state of the other party.

Due diligence is a measure of prudence, activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent person under the particular circumstances; not measured by any absolute standard but depends on the relative facts of the special case.

Definition of Due Diligence

According to Merriam Webster dictionary the term 'due' means 'satisfying or capable of satisfying a need, obligation, or duty' and 'according to accepted notions or procedures'. The term 'diligence' the attention and care legally expected or required of a person (as a party to a contract).

Understanding Due Diligence

In simple terms due diligence means "making sure you get what you think you are paying for."A common example of due diligence in various industries is the process through which a potential acquirer evaluates a target company or its assets for acquisition

Due diligence refers to the care a reasonable person should take before entering into an agreement or a transaction with another party. Due diligence serves to confirm all material facts in regards to a sale. It is an investigation or an audit of a potential investment.

A reasonable investigation of a proposed investment deal and of the principals offering it before the transaction is finalized to check out an investment's worthiness; generally performed by the investor's attorney and accountant. Due Diligence' is universally applied to investigations of information provided by a potential seller to a potential buyer

A successful due diligence is the key to an eventual investment. This is a process much more serious and important than the preparation of the Business Plan.The due diligence process is applied in two basic business situations:

1) Transactions involving sale and purchase of products or services, and
2) Transactions involving mergers, acquisitions, and partnerships of corporate entities.

2. International History

The term "due diligence" first came into common use as a result of the United States' Securities Act of 1933.The US Securities Act included a defense referred to in the Act as the "Due Diligence" defense which could be used by broker-dealers when accused of inadequate disclosure to investors of material information with respect to the purchase of securities.

In Australia, a similar defence is available in relation to misleading or deceptive statements made in a prospectus under section 731 of the Corporations Act 2001, but, curiously, there is no such specific defence for misleading or deceptive conduct under section 52 of the Trade Practices Act 1974. The Corporations Act 2001 also provides officers with a quasi due diligence defence under section 180(2) (the business judgment rule) and section 189 (reliance on others). A general due diligence defence to criminal actions is also available under Part 2.5 Division 12 of the Criminal Code Act 1995.

3. Due Diligence

When is due diligence used?

- Where substantial financial obligations are involved.
- Where it is essential to determine the undisclosed risks which are attached to the transaction as this may result in the transaction being aborted or affect the purchase price or terms of the agreement.
- Due diligence is used most often when buying a business, as the buyer spends time going through the financial situation of the business, legal obligations, customer records, and other documents. The prospective buyer wants to validate his/her opinion of the business to see if it is truly a good decision.
- In business transactions, the due diligence process varies for different types of companies. The relevant areas of concern may include the financial, legal, labor, tax, IT, environment and market/commercial situation of the company. Other areas include intellectual property, real and personal property, insurance and liability coverage, debt instrument review, employee benefits and labor matters, immigration, and international transactions.
- Due diligence in civil procedure is the idea that reasonable investigation is necessary before certain kinds of relief are requested.
- Due diligence in supplier quality (also known as due care) is the effort made by an "SQE" (Safety, Quality and Environment) professional to validate conformance of product provided by the seller to the purchaser.
- In criminal law, due diligence is the only available defense to a crime that is one of strict liability (i.e., a crime that only requires an actus reus and no mens rea). Once the criminal offense is proven, the defendant must prove beyond a reasonable doubt that they did everything possible to prevent the act from happening. It is not enough that they took the normal standard of care in their industry - they must show that they took every reasonable precaution.
- Persons involved in buying, selling, lending, and managing of commercial real estate routinely need to perform a variety of types of commercial property due diligence.
- Information security due diligence is often undertaken during the information technology procurement process to ensure risks are known and managed.

- Due diligence reviews during mergers and acquisitions to identify and assess the business risks.
- Due diligence is also a concept found in the civil litigation concept of a Statute Of Limitations. In this context the term "due diligence" determines the scope of a party's constructive knowledge, upon receiving notice of facts sufficient to constitute "inquiry notice" that alerts a would-be plaintiff that further investigation might reveal a cause of action.

4. Due Diligence Cycle

Due diligence as a cycle consists of five stages namely:

(a) Pre - engagement

(b) Understanding

(c) Due Diligence Program

(d) Substantial Verification

(e) Reporting

Business Activities – Requiring Due Diligence Process

- Merger and acquisitions
- Joint ventures
- Privatization of state organizations
- Commercial undertakings for example, stock exchange listings, financing projects and performance based commercial agreements

Due Diligence an Arm of Governance

Within the world of corporate governance, there are at least three separate arms of governance – corporate governance, due diligence and compliance programs. One generally associates the expression 'due diligence' with the American securities law defence of due diligence provided by the American Securities Act 1933 to those charged with the task of investigating prospectuses issued during takeover machinations.

However, due diligence has evolved beyond its original role as a defense. Much of the confusion relating to due diligence results from its treatment under different statutes or in different contexts as if each use is completely unrelated. It is a set rule for the process of evaluating everything from a prospectus to the assets of a potential takeover target, and more recently a corporation's internal legal audit process. Thus, it is no longer merely a concept relevant to a corporation's external transactional activities (such as investigating the veracity of prospectus during fundraising) but also to its internal processes (for example, legal compliance).

5. Classification of Due Diligence

Due Diligence can be classified as follows:

a. Classification by Function
b. Classification by Process
c. Classification by Transaction
d. Classification by Scope
e. Classification by Perspective

a. Classification by Function

(i) *Commercial Due Diligence*

- Commercial due diligence is all about understanding customers, markets and competition all the things you need to get right for an acquisition to succeed.
- Financial due diligence cannot provide the same insights as commercial due diligence.
- Commercial due diligence should establish the target's strengths and weaknesses vis-à-vis customer-purchase criteria and the competition's performance.
- Commercial due diligence provides the most important insights on the future of the target and the merged entity.

(ii) *Legal Due Diligence*

- Legal due diligence covers the legal aspects of a business transaction, liabilities of the target company, veracity of representations, potential legal pitfalls and other issues.
- A legal due diligence consists of a scrutiny of all, or specific parts, of the legal affairs of the target company with a view of uncovering any legal risks and provide the buyer with an extensive insight into the company’s legal matters.
- Legal Due Diligence is one of the means to enable the parties to finalize commercial negotiations.
- Legal due diligence is relevant and an integral part of the following transitions:
    - Privatizations

  - Flotations
  - Share subscriptions
  - Acquisitions of businesses or assets
  - Mergers
- Participants in Legal Due Diligence:
  - Company
  - Company Counsel
  - Underwriters
  - Underwriters' Counsel
  - Other parties
- Examples of Legal Due Diligence are:
  - Fiscal
  - IPR
  - Corporate Law
  - FEMA
  - Foreign Trade Law – Foreign Trade Competition Act
  - Industry Specific Law
  - Capital Market Laws

(iii) *Operational Due Diligence*

Operational due diligence team conducts a comprehensive operational assessment on all potential investments, providing an analysis of the manager's operational risk independently of its investment merits:

- Preliminary review
- Onsite Visit
- Verification
- Background and Reference Checks
- Investment Committee Review
- Ongoing Monitoring

(iv) *Business Strategy/ Management Culture Due Diligence*

- Management Culture due diligence is an investigation of the quality and motivation of the management, the staff and the structural and procedural organization together with the process of investigating, assessing and defining the cultures of two or more distinct business units through a cultural assessment to discover areas of similarity and difference that will impact integration efforts and achievement of strategic objectives.

- In planning for external growth through mergers, alliances, and other relationships, the firm must recognize cultural factors in addition to products, plant and equipment, and financial factors

(v) *Environmental Due Diligence*

- Environmental Due Diligence (EDD) is the due diligence exercise carried out with primary focus on Environmental issues (health and safety can also be considered) that may have an implication on the transfer of liability that would take place as a result of the M&A.
- Environmental due diligence is an effective tool for companies who intend to participate in greenfield production, brownfield acquisition, merger or a sell off
- Stages in an EDD process:
  - Phase I Preliminary Site Assessment
  - Phase II Contamination Profiling
  - Phase III Site Remediation

(vi) *Human Resource Due Diligence*

- The Human Resources Due Diligence is a detailed examination of the employee component of the enterprise at all levels together with analysis of their terms of reference, deployment, qualifications, and other relevant details.
- Elements of HR due diligence tend to be determined by the level of HR functioning within the merging entities.
- Human resource due diligence aims to examine the corporate culture and HR strategy of the target organization for compatibilities and identification of risks

(vii) *Marketing Due Diligence*

- An unbiased marketing perspective during the due diligence effort will reveal potential hazards.
- A strong marketing component in the due diligence process, increases the chances of a transaction that builds value by uncovering revenue enhancing strategies and opportunities

- It analyses the magnitude of the opportunity a company has in store for the marketing-savvy buyer

(b) Classification by Process

(i) *Initial/Preliminary Due Diligence*

This step is necessary in evaluating what risk is involved in doing business with an entity prior to establishing a relationship and assesses risk at that point in time

(ii) *Full Due Diligence*

Full due diligence is a process that recognizes the critical issues which requires the most in-depth evaluation and that which can vary dramatically from one opportunity to the next.

(iii) *Ongoing Due Diligence*

It is the process of periodically evaluating each relationship to identify the links between current business relationships and its activities if any linked to corruption or illicit activities. This process will be performed indefinitely as long as a relationship exists, and usually involves comparing the companies and executives to a database.

(iv) *Cold Due Diligence*

It is a process of due diligence that deals with the ongoing business decision on those areas that does not have an immediate implication, but which is counted in the long run.

(v) *Hot Due Diligence*

As the name suggests it is a due diligence process undertaken on those critical issues that decide the fate of a business transaction and which have a long standing impact.

(vi) *Quick/Fast Due Diligence*

It is a fast tract process of due diligence considered when an immediate business decision is becomes a requirement.

(C) Classification by Transaction

(i) *Private Equity*

The goal of due diligence is to identify the risk/return profile of a fund offer. Before investing in a private equity fund, an investor should have sufficient comfort regarding:

- Strategy perspective: the investment strategy of the fund.
- Return perspective: evidence that the manager stands out compared to his/her peer group.
- Risk perspective: assurance that risk is mitigated to the level required by the investor. There are basically three steps in private equity due diligence process they are
  - Top- down review
  - Overview of the relevant fund manager
  - Ensure that risks related to the potential commitment are mitigated through an in-depth due diligence process

(ii) *Mergers and Acquisitions*

Due diligence process in mergers and acquisitions are performed in four steps:

Step 1 - Identification, in which information is gathered and risks are identified. The risk management team will review recent operations by the risk management department and assemble any and all lost data.

Step 2 - Concerns the law, as all pending and prior litigation the company may be undergoing is identified and assessed. Insurance policies are also reviewed in this step, as are the company's environmental issues. Lastly, all loss run prior to mergers and acquisitions are analyzed.

Step 3 - Involves the summarization of all the data that's been collected. The summarized data is then analyzed and the exposures compared to existing coverage by insurance. Recommendations will then be given to the due diligence team.

Step 4 - Occurs after mergers and acquisitions are finalized. This step involves visiting new business locations, consolidation of the companies' insurance programs, and fixing any administrative issues that may have arisen during the business acquisitions.

(iii) *Joint Ventures*

Joint ventures must be factored into future internal audit plans, not only because of their popularity and profitability, but also because of the business risk they carry. Due to the complexity and dual control of these organizations, joint ventures are among the most problematic of all business alliances in terms of risk and cost.

Due diligence is performed when the operating department responsible for the prospective investment combines its skills with those of various support organizations, such as, finance, legal, tax, and human resources to examine the operations of a proposed joint venture. The scope and depth of these reviews depends on the degree of financial risk involved and the percentage of ownership being considered. Responsibility for reviewing business controls and standards of conduct of the prospective joint venture participants devolves naturally to the internal audit function, according to traditional charter responsibilities. Survey checklists and questionnaires are standard techniques for gathering data. Common pitfalls often confront due diligence teams when the partners are from different countries.

(iv) *Venture Capital*

Before venture capitalists make an investment in your company, they will conduct business due diligence. It involves:

- A review of the market for the product of the company
- A background check on the founders and key management team
- The competition for the company
- Discussions with key customers of the company
- An analysis of financial projections for the business
- A review of any holes in the management team

Venture capitalists will also have their lawyers conduct a legal due diligence. You should expect to receive a due diligence checklist from the venture capitalists' attorneys, requesting information on the company

(v) *Purchase of Business*

The process of buying and selling a company requires a thorough due diligence of all key elements of the business. The following areas require review:

- Sustainability of business
- Competition

- Financials
- Organization Infrastructure
- Potential Abilities
- Technology
- Sales & Marketing
- Business to Business Fit

(vi) *Investment in Business*

Due diligence means a rigorous investigation and evaluation of an investment opportunity before committing funds. The process includes review of its management team, business conditions, projections, philosophy, and investment terms and conditions. Due diligence verifies any business opportunities that survive the initial screening stage. This verification process consists of checking the accuracy of business plans, audited accounts, and management accounts; getting replies to warranty and other standard questionnaires; patent searches; and technical studies.

(vii) *Loans for Business*

Loans for business are dispersed after considering various aspects of business and its operation. These loans offered towards running your business. Due diligence in applied in verifying:

- Determine the facility overhead cost required for minimum, standard, and maximum capacity.
- Ascertain the amount of capital replacements needed in the near future.
- Determine the periodic maintenance cost of existing equipment.
- Determine the maximum sustainable production capacity by production line.
- Estimate the cost of modifications needed to increase the capacity of each production line or facility.
- Verify bank reconciliations for all bank accounts harboring significant cash balances.
- Obtain current detail of accounts receivable.
- Determine the days of receivables outstanding and the probable amount of bad debt. Review the bad debt reserve calculation.
- Obtain a list of all accounts and notes receivable from employees.

- Obtain a list of all inventory items, and discuss the obsolescence reserve. Determine the valuation method used.
- Obtain the current fixed asset listing, as well as depreciation calculations. Audit the largest items to verify their existence.
- Appraise the value of the most expensive fixed assets.
- Obtain an itemized list of all assets that are not receivables or fixed assets.
- Ascertain the existence of any liens against company assets.
- Obtain any maintenance agreements on company equipment.
- Review the current accounts payable listing.
- Obtain a list of all accounts payable to employees.
- Review the terms of any lines of credit.
- Review the amount and terms of any other debt agreements. Review covenants in the debt agreements, and determine if the company has breached the covenants in the past, or is likely to do so in the near future.
- Look for unrecorded debt.
- Verify wage and tax remittances to all government entities, and that there are no unpaid amounts.
- Review the sufficiency of accruals for wages, vacation time, legal expenses, insurance, property taxes, and commissions.

(viii) ***Partnership in Business***

A healthy strategic alliance needs to be a partnership. Alliances may look good on paper, but most are difficult to manage. They work best when all parties agree on and work together to implement a common strategy to achieve business objectives. Choosing a partner based on who they are – their reputation, performance record, strengths and weaknesses – is a logical place to begin.

It is just as important to compare their goals for the partnership or alliance with your goals. In a strategic relationship, both companies make decisions and take actions. But often, the overall goals for each company are different enough to cause conflict. Trust also comes into the agreement you create to define the merger or alliance.

Experience shows that spending more upfront time to get the agreement right pays off for everyone. Over time, the performance of the alliance can decline, producing lower or fewer results for both parties. When that happens, it is time to restructure the alliance.

(ix) *Substantial Supply to Business*

Business Supply Management is a cross-function approach including managing the movement of raw materials into an organization, certain aspects of the internal processing of materials into finished goods, and the movement of finished goods out of the organization and toward the end-consumer. As organizations strive to focus on core competencies and becoming more flexible, they reduce their ownership of raw materials sources and distribution channels. These functions are increasingly being outsourced to other entities that can perform the activities better or more cost effectively. The effect is to increase the number of organizations involved in satisfying customer demand, while reducing management control of daily logistics operations. Less control and more supply chain partners lead to the creation of supply chain management concepts. The purpose of supply chain management is to improve trust and collaboration among supply chain partners, thus improving inventory visibility and the velocity of inventory movement.

(x) *Real Estate*

Due diligence is a must before investing in real estate. Due diligence should always include a look at the books. The process includes gathering necessary documents such as contracts, official plan designation, licenses and policies, financial statements and copies of other documents such as the engineering reports, environmental reports, survey and legal description, property tax details, physical inventory of furnitures and fixtures. While verification of the above list of documents provides a better picture of the real estate in question, a personal visit to the site and physical inspection completes the verification process or the due diligence process. It is important to buy the right property, at a right price and at the right time.

D. Classification by Scope

(i) *Financial and Accounting*

It is an investigation into the affairs of an entity prior to its acquisition, flotation, restructuring or other similar transaction. It is a process by which information is gathered about a target company and its business operations and the environment in which it operates. The objective is to ensure that prospective investors make an informed investment decision. It is a business oriented analysis. A reasonable level of enquiry into the affairs having a material impact on the prospects of the business, evaluating the business model and key business practices, examining the relevant aspects of the past, present and near future of the business and finally assessing the benefits and liabilities of the proposed transaction are some of the important aspects of Financial Due Diligence.

(ii) *Tax*

When companies acquire a business, dispose of a non-core business or go into a merger, they need to manage the tax risk by means of a tax due diligence. The structure of a transaction will have a bearing on the tax due diligence process. If the transaction is about acquisition of assets the relevant taxes are the stamp duty and VAT. Both being levied on the transaction it can be easily identified. The main activities involved in a tax due diligence are reviewing of corporate tax returns and computations, review of correspondence with tax authorities, understanding the details of tax investigations and audits by foreign tax authorities, understanding the analysis of corporate tax and deferred tax provisions in financial statements, review of tax payment procedure every quarter. At an early stage of tax diligence exercise an important analysis will be to build a profile of target's risk as far as tax is concerned namely low tax risk, medium tax risk and high tax risk operations.

(iii) *Information Technology*

Investors often find it difficult to perform due diligence in one key area—information technology (IT). They often lack the technical knowledge to assess current systems, recognize what it will take to fix those that are broken, or identify alternatives for

merging or upgrading IT operations. They often don't have the benchmarking data to determine whether IT spending is above or below industry norms. And they often don't have time to do an accurate analysis. Assessing the information technology function of a potential acquisition or investment is an important part of due diligence. The steps in due diligence process will be to understand the current state of IT Capabilities, Cost Savings, Performing Risk Assessment and Identifying the Corrective Actions and outlining the future scenarios for IT in an organization.

(iv) *Strategic and Commercial*

A commercial due diligence report usually involves a comprehensive review of the company's business plan in the context of projected market conditions and the industry/competition. A commercial due diligence process generally covers the following Sustainability of competitive advantage and revenues/ income:

- Achievability of business plan projections

- Target specific market/industry-related investment risks
- Strategic/market-related value-creating opportunities
- Implications for financial performance/valuation.

(v) *Legal*

A legal due diligence consists of a scrutiny of all, or specific parts, of the legal affairs of the target company with a view of uncovering any legal risks and provide the buyer with an extensive insight into the company's legal matters. Additionally, a legal due diligence often improves the buyer's bargaining position and ensures that necessary precautions in relation to the transaction be taken. The objectives of a legal due diligence exercise may vary from case to case. Some of the basic objectives may, however, be summarized as follows:

- Gathering of information from the target company,
- Uncovering of the target company's strong and weak sides, relevant risks and advantages in connection with the transaction,
- Minimizing the risk of unexpected situations,
- Improvement of the seller's bargaining position,
- Identification of areas where representations and warranties from the seller should be obtained in the acquisition agreement.

(vi) *Operational*

Operations are the engine of a business. Operational Due Diligence (ODD) can give you insights into and comfort over operations in transactions. Identifying the potential risk areas in which the client might not have the necessary industry experience. Increased attention on operational analysis leads to better clarity for the investment decision and the subsequent integration readiness and planning.

(E) Classification by Perspective

(i) *Investor Due Diligence*

Due diligence from a buyer's or investors perspective, appraising a potential acquisition involves more than the scrutiny of balance sheets. Due diligence can often make or break a deal--making the process of combing through projections, balance sheets and contracts all the more crucial and complex in today's highly competitive and consolidated media world. Buyer side considerations:

- Pay the right price

- Avoid unpleasant surprises and unforeseen risks
- Understand what you are buying
- Address deal objectives
- Give comfort to investors

(ii) *Target Side Due Diligence*

Target side due diligence is carried out at the expense of, and at the behest of, the seller, by independent third parties. This contrasts with due diligence carried out by the buyer. The biggest advantage of vendor due diligence is that is speeds up the sale process, and saves costs. It eliminates the duplication of due diligence work by multiple buyers, who want answers to many of the same questions. It also provides greater credibility to facts and numbers that the seller presents to potential buyers, because they have been verified by impartial accountants and lawyers.

The objective of the vendor should be to turn this process on its head and create a business which can be readily evaluated and quickly put into a state where the acquirer can exploit its potential. Both these objectives can be considerably advanced if the vendor undertakes a vendor due diligence with the aim of preparing the business for the buyer due diligence investigation. In essence, what the vendor is doing is undertaking a practice run at a buyer due diligence. The results of the vendor due diligence are then used to ensure that any problems are uncovered and fixed and the business made ready for the buyer due diligence.

6. Due Diligence Process

Due Diligence process consists of 3 important steps:

Step I: Requesting information.

Step II: Gathering information.

Step III: Reporting on information

Due Diligence Procedure consists of the following:

- Appointment of the team
- Skills/expertise
- Clear and definite mandate
- Costs
- Confidentiality agreements

- Data room and access to the room
- Due Diligence Questionnaire and Checklist
- One on one interviews with management from the target company
- Investigative mode of enquiry which will include searches of public registers

A business which wants to attract foreign investments must present a business plan. But a business plan is the equivalent of a visit card. The introduction is very important - but, once the foreign investor has expressed interest, a second, more serious, more onerous and more tedious process commences: Due Diligence.

- The firm must appoint ONE due diligence coordinator. This person interfaces with all outside due diligence teams. He collects all the materials requested and oversees all the activities which make up the due diligence process.
- The company must have ONE VOICE. Only one person represents the company, answers questions, makes presentations and serves as a coordinator when the DD teams wish to interview people connected to the firm
- Both employees and management must realize that this is a top priority
- They must be instructed not to lie.
- They must know the DD coordinator and the company's spokesman in the DD process.
- The DD is a process which is more structured than the preparation of a Business Plan.
- It is confined both in time and in subjects: Legal, Financial, Technical, Marketing, Controls

Various Areas of Investigation under Due Diligence Process

A. Finding a new investment manager for a specific asset class

- Initial Quantitative Screening
- Qualitative Evaluation
- Questionnaire Submission
- Conference Call Interview
- Manager Site Visit
- Contract Negotiation

B. Investment Process – Due Diligence

- Definition of Investment Process Objectives
- Initial Screening
- In-depth review qualitative and Quantitative
- Initial Due Diligence
- Investment Committee Approval

Phase I. Definition of Investment Process & Objectives

- Priority for actively discovered co-investment opportunities
- Due consideration for portfolio construction and risk mitigation
- Target transactions with the following minimum attributes:
- High-quality management team
- Sustainable competitive advantages
- Clear and growing market opportunity
- Clear path to value creation and realization
- Quality and experience of investment partners
- Capital-efficient business model
- Acceptable financial risk profile for achieving target return
- Attractive initial valuation

Phase II: Quantitative and Qualitative Deal Screening

- Pro-Active sourcing of investment leads
- Analysis of over 50 companies and/or investment structures
- Quantitative and preliminary qualitative analyses of opportunities

Phase III: Additional Qualitative Deal Screening

- Analysis of presentations, offering memorandum, discrete reference checks
- Industry and segment strategy review
- Thorough review of company's business model
- Analyses of risks and rewards
- Identify and confirm synergy and value creation
- Reviewing the background of the prospective partners and managers

- Quality of internal risk controls and procedures
- Assessment of resources available to manage current and future business

Phase IV: Additional Qualitative Deal Screening

- Assessment of quality of management
- Pricing and terms
- Performance financial and sensitivity analyses
- Performance or procure authoritative industry and segment analyses
- Checking and cross-checking of references, customers and suppliers
- Preliminary legal and accounting due diligence
- Preparation of potential investment decisions and structuring

Phase V: Preliminary Meeting with Co. Decision Makers and the Fund's Investment Committee for Preliminary Approval

- Verification and refinement of final financial and sensitivity analyses
- Verification and thorough reference checks with customers and suppliers
- Legal and accounting due diligence
- Negotiate pricing, terms and structuring
- Preparation of Potential Investment decisions and contingencies
- Preliminary Investment Committee Approval (short form memorandum

Phase VI: Final Investment Committee Approval prior to Completing the Proposed Transaction

- Preparation of documentation
- Final investment recommendation and approval (long form memorandum)
- Execution and disbursements (in phases in if possible)
- Enhance contingency and potential re-course based on additional information

Post-Investment I : Continual Monitoring Guaranteed

- Management participation
- Strict reporting from investee companies
- Quarterly site visits (at minimum)

- Recommendation of remedial actions
- Enhance options or alternative strategies for exit
- Consideration for further funding or early exit

Post-Investment II: Reporting and Performance Data

- Comparison of original financial projections with actual performances
- Deviation from milestone and time-table
- Early detection of risks and shift in project dynamics
- Quarterly asset valuation and estimates (NAV Reporting)
- Portfolio evaluation

Post-Investment III: Independent Internal & External Review and Audit

- Self-imposed internal audit and review by management and staff with high degree of independence
- Quarterly review and annual audit by an internationally recognized accounting firm

C. **Due diligence with regard to FCPA compliance** is required in two aspects:

- Initial due diligence - this step is necessary in evaluating what risk is involved in doing business with an entity prior to establishing a relationship and assesses risk at that point in time.
- Ongoing due diligence - this is the process of periodically evaluating each relationship overseas to find links between current business relationships overseas and ties to a foreign official or illicit activities linked to corruption. This process will be performed indefinitely as long as a relationship exists, and usually involves comparing the companies and executives to a database of foreign officials.

D. Due diligence investigation with regard to hedge fund refers to an in-detail review of a hedge fund's activity, conducted in order to ensure that the fund is in compliance with its prospectus. It is a roadmap for existing and potential investors in understanding whether a specific fund will meet his or her investment horizon, risk tolerance and investment strategy. This involves the following steps

- A fund snapshot
- Disclosed investment strategy
- Historical returns

- Assets under management (a copy of the fund's portfolio from the custodian is usually requested)
- Audited financial statements if the fund is regulated by the U.S. Securities and Exchange Commission (SEC)
- Fund's terms and details
- Regulatory registration if any
- Risk factors
- Valuation

E. Environmental due diligence

Environmental due diligence (EDD) is a relatively new discipline. Prior to the 1980s it was virtually unheard of; whereas today it is an integral part of the transaction process undertaken predominantly by purchasers, but increasingly by vendors.

The process has evolved over the past 20 years and can now include evaluation of health & safety (H&S), employees' exposure to toxic materials, product liability, the list goes on. This article explores the background to international EDD and examines the emerging future trends in process and practice.

The first appearance of EDD audits came in response to companies taking out Environmental Impairment Liability Insurance in 1980. The scope of EDD further increased with the realization in the 1990s that exposure of employees' in the 1950s, 1960s and 1970s to toxic materials such as asbestos could have huge cost implications for the 'descendents' of the original employers'.

Current Scope of EDD

EDD is conducted to identify and quantify 'material' (in the context of the individual transaction) liabilities or assets associated with the target. The materiality threshold, agreed prior to the start of EDD, will reflect not only the value of the target but also the risk averse nature of the client. It may be that prior investments by a client have had significant liabilities associated with a particular substance or activity e.g. polychlorinated biphenyls (PCBs) or brake lining servicing (asbestos exposure). As a result, the client may direct the scope to more closely evaluate their main aspects of concern.

Future Scope of EDD

Future trends in the scope of EDD are dependent upon future legislation and case law events. However, we are increasingly seeing the requirement for occupational health and safety (OHS) assessments. OHS assessments require specialist consultants for completion and are very often separate pieces of work to the common EDD audit.

Investors are also becoming increasingly aware of the merits of implementing a management plan based on the EDD for the duration of the investment. The plan may include the use of environmental insurance, company captives and other financial options to transfer or smooth the retained environmental risks or liabilities.

If the EDD is conducted properly and as part of an integrated DD process then not only will the reduction of technical, financial, legal and contractual risk be achieved at the time of acquisition, but throughout the period of ownership the environmental liabilities and balance sheet exposure may be controlled.

7. Due Diligence Process Checklist

I. Financial Information

A. Annual and quarterly financial information for the past three years

1. Income statements, balance sheets, cash flows, and footnotes
2. Planned versus actual results
3. Management financial reports
4. Breakdown of sales and gross profits by:
   a. Product Type
   b. Channel
   c. Geography
5. Current backlog by customer (if any)
6. Accounts receivable aging schedule

B. Financial Projections

1. Quarterly financial projections for the next three fiscal years
   a. Revenue by product type, customers, and channel
   b. Full income statements, balance sheets, cash
2. Major growth drivers and prospects
3. Predictability of business

4. Risks attendant to foreign operations (e.g., exchange rate fluctuation, government instability)
5. Industry and company pricing policies
6. Economic assumptions underlying projections (different scenarios based on price and market fluctuations)
7. Explanation of projected capital expenditures, depreciation, and working capital arrangements
8. External financing arrangement assumption

C. Capital Structure

1. Current shares outstanding
2. List of all stockholders with shareholdings, options, warrants, or notes
3. Schedule of all options, warrants, rights, and any other potentially dilutive securities with exercise prices and vesting provisions.
4. Summary of all debt instruments/bank lines with key terms and conditions
5. Off balance sheet liabilities

D. Other financial information

1. Summary of current federal, state and foreign tax positions, including net operating loss carryforwards
2. Discuss general accounting policies (revenue recognition, etc.)
3. Schedule of financing history for equity, warrants, and debt (date, investors, dollar investment, percentage ownership, implied valuation and current basis for each round)

II. Products

A. Description of each product

1. Major customers and applications
2. Historical and projected growth rates
3. Market share
4. Speed and nature of technological change
5. Timing of new products, product enhancements
6. Cost structure and profitability

III. Customer Information

A. List of top 15 customers for the past two fiscal years and current year-to-date by application

(name, contact name, address, phone number, product(s) owned, and timing of purchase(s))

B. List of strategic relationships

(name, contact name, phone number, revenue contribution, marketing agreements)

C. Revenue by customer

(name, contact name, phone number for any accounting for 5 percent or more of revenue)

D. Brief description of any significant relationships severed within the last two years.

(name, contact name, phone number)

E. List of top 10 suppliers for the past two fiscal years and current year-to-date with contact information

(name, contact name, phone number, purchase amounts, supplier agreements)

IV. Competition

A. Description of the competitive landscape within each market segment including:

1. Market position and related strengths and weaknesses as perceived in the market place
2. Basis of competition (e.g., price, service, technology, distribution)

V. Marketing, Sales, and Distribution

A. Strategy and implementation

1. Discussion of domestic and international distribution channels
2. Positioning of the Company and its products
3. Marketing opportunities/marketing risks
4. Description of marketing programs and examples of recent marketing/product/public relations/media information on the Company

B. Major Customers

1. Status and trends of relationships
2. Prospects for future growth and development
3. Pipeline analysis

C. Principal avenues for generating new business

D. Sales force productivity model

1. Compensation
2. Quota Average
3. Sales Cycle
4. Plan for New Hires

E. Ability to implement marketing plan with current and projected budgets

VI. Research and Development

A. Description of R&D organization

1. Strategy
2. Key Personnel
3. Major Activities

B. New Product Pipeline

1. Status and Timing
2. Cost of Development
3. Critical Technology Necessary for Implementation
4. Risks

VII. Management and Personnel

A. Organization Chart

B. Historical and projected headcount by function and location

C. Summary biographies of senior management, including employment history, age, service with the Company, years in current position

D. Compensation arrangements

1. Copies (or summaries) of key employment agreements
2. Benefit plans

E. Discussion of incentive stock plans

F. Significant employee relations problems, past or present

G. Personnel Turnover

1. Data for the last two years
2. Benefit plans

VIII. Legal and Related Matters

A. Pending lawsuits against the Company

(detail on claimant, claimed damages, brief history, status, anticipated outcome, and name of the Company's counsel)

B. Pending lawsuits initiated by Company

(detail on defendant, claimed damages, brief history, status, anticipated outcome, and name of Company's counsel)

C. Description of environmental and employee safety issues and liabilities

1. Safety precautions
2. New regulations and their consequences

D. List of material patents, copyrights, licenses, and trademarks

(issued and pending)

E. Summary of insurance coverage/any material exposures

F. Summary of material contacts

G. History of SEC or other regulatory agency problem, if any

8. Due Diligence Report

A due diligence report will consist of the following details pertaining to the due diligence procedure performed

- An outline of the scope of the review
- An analysis of the documentation and information revealed
- A list of all the information disclosed by investigations (public record searches)
- Limitations and disclaimers of liability

- An executive summary which outlines the legal issues identified and advises on the legal implications of proceeding with the transaction (Risks and Liabilities)
- The due diligence report starts with an executive summary that contains the name of the person who conducted the study and the name and position of the person who asked for the study.
- The executive summary will also list the documents and other items reviewed during the study. Finally, the executive summary will present an overview of the findings of the study.
- The report will outline the steps taken during the study, and the report will describe the specific areas of the business that were part of the study
- The report will discuss the company's history and the company's management.
- The report will state the mission statement and a description of the business model.

9. Tips for Effective Due Diligence

- Present an exhaustive list of requirements.
- Note contradictory information received.
- Clarify where the intentions / objectives are disguised so that the replier cannot manipulate the reply.
- Read through Internal Audit Reports.
- Identify the reasons for withholding the reply
- Note the time frame within which the replies are provided.
- Mark the tone of reply (defensive or attacking).
- Trace transaction which have been deferred or expedited
- Review transactions with related parties and
- Transfer Pricing Policy for inter company transactions to be scrutinized
- Scrutinize the legal and professional aspects of the transaction.

VI. Professional Opportunities for Chartered Accountants

Consultancy – Opportunities in the arena of Consultancy are as follows (Illustrative list):

- Growth in M&A and Private equity activity in India

- Quality due diligence specialists
- Other opportunities – bank funding, partnership, joint ventures
- IPO Candidates
- International Business Partners
- Strategic Alliance Partners
- Merger & Acquisition Targets Consultants and Representatives
- Franchisees
- Distributors, suppliers and vendors
- Patent Due Diligence in biotechnology transactions
- Licensing Due Diligence
- IT Due Diligence /Cyber Due Diligence Process
- Information Security Due Diligence Process
- Human Rights Due Diligence Process
- Customer Due Diligence Process
- International Trade Due Diligence
- Legal Due Diligence
- IPR Due Diligence
- Anti Money Laundering Due Diligence
- Tax Due Diligence

Compliance – Opportunities in the arena of Due Diligence Compliance are as follows:

- Cyber Laws - Information Technology Act 2000
- IFRS and Indian Accounting Standard Compliance Due Diligence Process
- Term Loan and Project Loan Due Diligence
- Setting Standards for Operational Due Diligence
- FCRA Due Diligence
- Financial Due Diligence
- Due Diligence Report under Consortium/Multiple Banking Arrangement under RBI Notification –

- The Reserve Bank of India (RBI) vide its notification no RBI/2008-2009/ 183 DBOD No.BP. BC.46/ 08.12.001/2008-09 dated 19/09/2008 has advised the Scheduled Commercial bank (excluding Regional Rural Banks and Local Area banks) to obtain regular certification (Diligence report) by qualified professional, preferably a Company Secretary, regarding compliance of various statutory prescriptions that are in vogue as per specimen given in the notification. Further in another notification RBI/2008-2009/379 DBOD. No. BP.BC.110/08.12.001/2008-09 RBI clarified that in addition to Company Secretaries, banks can also accept the certification by a Chartered Accountants & Cost Accountants.
- This report shall be prepared for half yearly basis. This notification shall be applicable to borrowers availing sanctioned credit limits of Rs.5.00 crore and above or wherever, it is in their knowledge that their borrowers are availing credit facilities from other banks.The banker will communicate to the company for their appointment with scope of certification. The remuneration shall be paid by the bankers to the professional as per slab.The report shall be submitted to the appointing bank (normally lead bank) and copy to member of the consortium arrangement.

Certification – Opportunities in the arena of Certification are as follows (Illustrative List):

- Capital Market Laws - SEBI prescribes the process of due diligence that a merchant banker has to complete before a prospectus is cleared. It also insists on submission of all the documents disclosing the details of account and the clearances obtained from the ROC and other government agencies for tapping peoples' savings. The responsibilities of lead manager, underwriting obligations, capital adequacy, due diligence certification, etc., are laid down in detail by SEBI.
- Banking Laws - RBI has issued the KYC guidelines under Section 35 (A) of the Banking Regulation Act, 1949 and any contravention of the same will attract penalty. Know your customer (KYC) is the due diligence and bank regulation that financial institutions and other regulated companies must perform to identify their clients and ascertain relevant information pertinent to doing financial business with them. In the USA, KYC is typically a policy implemented to conform to a customer identification program mandated under the Bank Secrecy Act and USA PATRIOT Act. The due diligence expected under KYC involves going into the purpose and reasons for opening an account, anticipated turnover in the account,

sources of wealth (net worth) of the person opening the account and sources of funds flowing into the account.

- Registered e-return intermediaries are required to submit a due diligence certificate from a certified ISA or CISA professional in the prescribed format that it has the necessary computing infrastructure.

V. Corporate Governance

Sound corporate governance is essential to the well being of an organization and its stakeholders. In the context of Indian Management, corporate governance can be drawn from a famous quotation of Arthashastra (in Sanskrit) "Praja sukhe sukham rajyaha prajanamcha hitehitam Natma priyam hitam rajnaha prajanam cha hitam piryam" which means that in the happiness of his subject lies the king's happiness, in their welfare his welfare. He shall not consider as good only that which pleases. Despite a strong history, the term 'Corporate Governance' was unknown until early nineties; Corporate Governance introduced itself with alarming series of business scams and fraudulent practices (which were common worldwide).

A statutory framework of Corporate Governance in India is primarily defined by Companies Act and SEBI regulations supplement the provisions stated in the Act. Mutual Fund Industry on the other hand is not regulated by the Companies Act and the SEBI (Mutual Fund) Regulations 1996, have not detailed upon the Corporate Governance procedure in the Mutual Fund Industry.

Most commonly accepted principles of corporate governance include:

- **Rights and equitable treatment of shareholders**: Organizations should respect the rights of shareholders and help shareholders to exercise those rights. They can help shareholders exercise their rights by effectively communicating information that is understandable and accessible and encouraging shareholders to participate in general meetings.
- **Interests of other stakeholders**: Organizations should recognize that they have legal and other obligations to all legitimate stakeholders.
- **Role and responsibilities of the board**: The board needs a range of skills and understanding to be able to deal with various business issues and have the ability to review and challenge management performance. It needs to be of sufficient size and have an appropriate level of commitment to fulfill its responsibilities and duties. There are issues about the appropriate mix of executive and non-executive trustees.

- **Integrity and ethical behaviour**: Ethical and responsible decision making is not only important for public relations, but it is also a necessary element in risk management and avoiding lawsuits. Organizations should develop a code of conduct for their trustees and executives that promotes ethical and responsible decision making. It is important to understand, though, that reliance by a company on the integrity and ethics of individuals is bound to eventual failure. Because of this, many organizations establish Compliance and Ethics Programs to minimize the risk that the firm steps outside of ethical and legal boundaries.
- **Disclosure and transparency**: Organizations should clarify and make publicly known the roles and responsibilities of board and management to provide shareholders with a level of accountability. They should also implement procedures to independently verify and safeguard the integrity of the company's financial reporting. Disclosure of material matters concerning the organization should be timely and balanced to ensure that all investors have access to clear, factual information.

Clause 49 of the Equity Listing Agreement to the Indian Stock Exchange came into effect from 31 December 2005. It has been formulated for the improvement of corporate governance in all listed companies. At the end of the first India Corporate Week in December 2009, the Ministry of Corporate Affairs issued new Corporate Governance Voluntary Guidelines and new Corporate Social Responsibility Voluntary Guidelines.

The main focus of Competition Commission of India is to take care of mergers, industries for a healthy competition among them incorporating the corporate governance principles in policy making.

There has been renewed interest in the corporate governance practices of modern corporations since 2001, particularly due to the high-profile collapses of a number of large U.S. firms such as Enron Corporation and MCI Inc. (formerly WorldCom). In 2002, the U.S. federal government passed the Sarbanes-Oxley Act, intending to restore public confidence in corporate governance.

In the first half of the 1990s, the issue of corporate governance in the U.S. received considerable press attention due to the wave of CEO dismissals (e.g.: IBM, Kodak, Honeywell) by their boards. The California Public Employees' Retirement System (CalPERS) led a wave of *institutional* shareholder activism (something only very rarely seen before), as a way of ensuring that corporate value would not be destroyed by the now traditionally cozy relationships between the CEO and the board of directors (e.g., by the unrestrained issuance of stock options, not infrequently back dated).

In 1997, the East Asian Financial Crisis saw the economies of Thailand, Indonesia, South Korea, Malaysia and The Philippines severely affected by the exit of foreign capital after property assets collapsed. The lack of corporate governance mechanisms in these countries highlighted the weaknesses of the institutions in their economies.

In the early 2000s, the massive bankruptcies (and criminal malfeasance) of Enron and WorldCom, as well as lesser corporate debacles, such as Adelphia Communications, AOL, Arthur Andersen, Global Crossing, Tyco, led to increased shareholder and governmental interest in corporate governance. This is reflected in the passage of the Sarbanes-Oxley Act of 2002.

With the goal of promoting better corporate governance practices in India, the Ministry of Corporate Affairs, Government of India, has set up National Foundation for Corporate Governance (NFCG) in partnership with Confederation of Indian Industry (CII), Institute of Company Secretaries of India (ICSI) and Institute of Chartered Accountants of India (ICAI). NFCG was set up with the following mission:

- To foster a culture for promoting good governance, voluntary compliance and facilitate effective participation of different stakeholders;
- To create a framework of best practices, structure, processes and ethics;
- To make significant difference to Indian Corporate Sector by raising the standard of corporate governance in India towards achieving stability and growth.

While corporate governance is about policies and practices that ensure fairness in the conduct of business, coupled with accountability and responsibility, conduct of internal audit is an important principle in the framework of corporate governance that checks the organization's adherence to internal control framework which is essential for the efficient performance of organizational duties and routine. Internal Audit offers valuable input to the management that enables them to understand the effectiveness of their organizations and the loopholes which other wise would not have been identified.

VI. Compliance with Commercial Laws

There is still a huge requirement for professionals who are well versed with the laws and accounting of not only our country but also of various other countries. The Chartered Accountants by continuously upgrading their skills and through their sound accounting knowledge can fill this gap. Monitoring the compliance of commercial laws emerges as a professional opportunity for chartered accountants.

1. Anti Money Laundering Laws

Money laundering involves disguising financial assets so that they can be used without detection of the illegal activity that produced them. Through money laundering, the launderer transforms the monetary proceeds derived from criminal activity into funds with an apparently legal source.The Prevention of Money Laundering Act, 2002 (PMLA 2002) is the primary anti money laundering legislation in India.

The Prevention of Money Laundering Act, 2002 (PMLA 2002) and the Rules notified there under came into force with effect from July 1, 2005. The PMLA 2002 consists of ten chapters containing 75 sections and one Schedule.

Financial Intelligence Unit - India (FIU-IND) is the central, national agency responsible for receiving, processing, analyzing and disseminating information relating to suspect financial transactions to enforcement agencies and foreign FIUs. The Director, FIU-IND and Director (Enforcement) have been conferred with exclusive and concurrent powers under relevant sections of the Act to implement the provisions of the Act.

Other Laws for Prevention of Money Laundering

- Smugglers and Foreign Exchange Manipulators Forfeiture of Property Act, 1976
- The Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974 (COFEPOSA)
- The Benami Transactions (Prohibition) Act, 1988
- The Prevention of Illicit Traffic in Narcotic Drugs and Psychotropic Substances Act, 1988

Other Related Acts

- Banking Regulation Act ,1949
- Chit Funds Act ,1982
- DICGC Act, 1961
- NABARD Act,1981
- National Housing Bank Act ,1987
- RBI Act, 1934

- SEBI Act ,1992
- Insurance Act ,1938
- IRDA Act 1999

2. Laws Relating to Alternate Dispute Resolution

Alternate or Alternative dispute resolution (ADR) includes dispute resolution processes and techniques that act as a means for disagreeing parties to come to an agreement short of litigation. ADR provides an alternative to going to court to settle disagreements. Methods include arbitration, where disagreeing parties agree to be bound by the decision of an independent third party, and mediation, where a third party attempts to arrange a settlement between the two sides.

Alternative dispute resolution in India is not new and it was in existence even under the previous Arbitration Act, 1940. The Arbitration and Conciliation Act, 1996 has been enacted to accommodate the harmonisation mandates of UNCITRAL Model. To streamline the Indian legal system the traditional civil law known as Code of Civil Procedure, (CPC) 1908 has also been amended and section 89 has been introduced. Section 89 (1) of CPC provides an option for the settlement of disputes outside the court.

3. Laws relating to Real Estate

The term 'real estate' refers to land as well as building. The word ‘land’ includes—the air above and the ground below and any buildings or structures on it. It covers residential houses, commercial offices, trading spaces such as theatres, hotels and restaurants, retail outlets, industrial buildings, factories and also government buildings.

Legislations Governing Real Estate Transactions

1. The Indian Contract Act, 1872
2. The Transfer of Property Act, 1882
3. The Registration Act, 1908
4. The Specific Relief Act, 1963
5. The Urban Land (Ceiling & regularization) Act, 1976
6. The Land Acquisition Act, 1894
7. The Indian Evidence Act, 1872
8. The Indian Stamp Act, 1899

9. The Rent Control Act
10. The State Laws governing the real estates
11. Law governing property tax
12. The Consumer Protection Act, 1986
13. The Arbitration & Conciliation Act, 1996
14. The Income Tax Act, 1961
15. The Wealth Tax Act, 1957
16. The Co-operative Societies Act, 1912
17. The Multi-State Co-operative Societies Act, 1912
18. Finance Act in relation to Service Tax
19. The Foreign Exchange Management Act, 1999
20. SEBI norms for Real Estate Mutual Funds
21. Foreign Direct Investment Guidelines (FDI)

4. Legal Metrology Laws

Legal Metrology" means that part of metrology which treats units of weighment and measurement, methods of weighment and measurement and weighing and measuring instruments, in relation to the mandatory technical and legal requirements which have the object of ensuring public guarantee from the point of view of security and accuracy of the weighments and measurements. (Sec.2(g) of Legal Metrology Act, 2009)

The Legal Metrology Act, 2009 has come into effect after its publication in the Official Gazette on the 14th January 2010. It replaces The Standards of Weights and Measures Act, 1976 and the Standards of Weights and Measures (Enforcement) Act, 1985. The new Act will become operative after the Rules there under are also notified.

5. Laws relating to Charity

The legal framework for charity in India is quite complex with a number of different acts of legislation governing it in their own way. There is no single piece of legislation, which comprehensively governs the sector and similarly no single regulator exists, in contrast to other countries where a Charity Commissioner regulates the individual organizations on nationwide basis.

Important Laws governing the charity sector in India

1. Public Trusts Acts of various States

A charitable trust is not required to obtain registration under the Indian Registration Act. However, in certain States there is a Public Trusts Act, which requires such institutions trusts to get registered as such under the said Act.

As regards the public trusts, there is no Central Act applicable in all the States. But some states - Maharashtra, Gujarat, Madhya Pradesh, Bihar, Orissa, and Tamil Nadu - have formed their own Public Trusts Acts, which primarily control the Public Trusts created in these states. These Acts are more or less similar in nature though there may be certain variations.

Some of these states have also created a Charity Commissioner, which operates at state level.

The states which do not have their own legislation mostly rely on The Indian Trusts Act, 1882, which is a national act and primarily deals with private trusts.

2. The Societies Registration Act, 1860

It is a central Act but modified versions operate at state level; 'Registrar of Societies' at state level deals with the registered organization.

3. The Companies Act, 1956

It is a central Act and section 25 deals with non-profit companies. 'Registrar of Companies' at state level deals with registered organizations under the Act.

4. The Income Tax Act, 1961

It is a central Act applicable uniformly to all states. It governs tax exempt status of charities as well as exemption available to donations to charities.

5. The Foreign Contribution (Regulation) Act, 1975

This Act regulates receipt and spending of foreign funds. Ministry of Home Affairs handles registration under the Act.

Any Charitable Trust, Society, Company, desirous of receiving any foreign contribution from a foreign source, is required to obtain registration under section 6(1) of FCRA Any such association which is not registered or which has been denied registration, can receive foreign contribution only after obtaining prior permission from the Home Ministry of the Central Government under section 6(1A) of the Act.

Apart from the above as per the form of organization of the charity and state where it is located, the following laws will apply:

A public charitable or religious institution can be formed either as a Trust or as a Society or as a Company registered u/s 25 of the Companies Act. It generally takes the form of a trust when it is formed primarily by one or more persons. To form a Society at least seven persons are required. Institutions engaged in promotion of art, culture, commerce etc. are often registered as non-profit companies.

Societies

Societies Registration Act, 1860

Religious Societies Act 1880

Religious Institutions (Prevention of Misuse) Act 1988

Trusts

Indian Trusts Act, 1882

Charitable and Religious Trusts Act, 1920

Religious Endowments Act, 1863

Charitable Endowments Act 1890

Hindu Religious and Charitable Endowments Act 1951

Official Trustees Act 1913

Mussalman Wakf Act 1923

Mussalman Wakf Validating Act 1913

Mussalman Wakf Validating Act 1930

Wakf Act 1995

State laws

Andhra Pradesh Charitable and Hindu Religious Institutions and Endowments Act, 1987

Bihar Hindu Religious Trusts Act, 1950

Bombay Public Trusts Act, 1950

Bombay Public Trusts Rules, 1951

Karnataka Hindu Religious Institutions and Charitable Endowments Act, 1997

Karnataka Hindu Religious Institutions and Charitable Endowments Rules, 2002

Kerala Travancore-Cochin Hindu Religious Institutions Act, 1950

Madhya Pradesh Public Trusts Act, 1951

Orissa Hindu Religious Endowments Act, 1951

Rajasthan Public Trust Act, 1959

Tamil Nadu Hindu Religious and Charitable Endowments Act, 1959

The Madras Hindu Religious And Charitable Endowments Act, 1951

Uttar Pradesh Charitable Endowments (Extension of Powers) Act, 1950

Charitable Endowments (U.P. Amendment) Act, 1952

United Provinces Charitable Endowments Rules, 1943 Religious Endowments (Uttar Pradesh Amendment) Act, 1951 Uttar Pradesh Hindu Religious Institutions (Prevention of Dissipation of Properties) (Repeal) Act, 2000

6. Labour Laws

Labour law is the body of laws, administrative rulings, and precedents which address the legal rights of, and restrictions on, working people and their organizations. The law relating to labour and employment in India is primarily known under the broad category of "Labour and Industrial Law"

Under the Constitution of India, Labour is a subject in the Concurrent List where both the Central & State Governments are competent to enact legislation subject to certain matters being reserved for the Centre.

Labour Laws enacted by the Central Government

There are over 43 legislations on labour from the Central Government and the number of legislations enacted by the State Governments is close to four times that of the Central Government. Besides, both Central and State Governments have formulated Rules to facilitate implementation of these laws.

Some of the Labour Laws enacted by the Central Government are:

1. The Employees' State Insurance Act, 1948
2. **The Employees'** Provident Fund and Miscellaneous Provisions Act,1952
3. The Mines Act, 1952
4. The Child Labour (Prohibition and Regulation) Act, 1986.
5. The Contract Labour (Regulation and Abolition) Act, 1970.
6. The Equal Remuneration Act, 1976.

7. The Industrial Disputes Act, 1947.
8. The Industrial Employment (Standing Orders) Act, 1946.
9. The Maternity Benefit Act, 1961
10. The Minimum Wages Act, 1948
11. The Payment of Bonus Act, 1965
12. The Payment of Gratuity Act, 1972
13. The Payment of Wages Act, 1936
14. The Apprentices Act, 1961
15. Unorganized Workers Social Security Act, 2008
16. The Employers' Liability Act, 1938
17. The Factories Act, 1948
18. The Plantation Labour Act, 1951
19. The Trade Unions Act, 1926
20. The Employees' Compensation Act, 1923

7. Intellectual Property Right (IPR)

Intellectual property Right (IPR) is an umbrella term for various legal entitlements which attach to certain types of information, ideas, or other intangibles in their expressed form. The holder of this legal entitlement is generally entitled to exercise various exclusive rights in relation to the subject matter of the Intellectual Property. The term intellectual property reflects the idea that this subject matter is the product of the mind or the intellect, and that Intellectual Property rights may be protected at law in the same way as any other form of property.

Overview of Laws Related To Intellectual Property Rights in India

The Rules and Laws governing Intellectual Property Rights in India are as follows:

a. **The Copyright Act, 1957 and The Copyright Rules, 1958**

   The umbrella legislation relating to copyright is the Copyright Act, 1957. According to the Act, the term 'copyright' means the exclusive right to do or authorize the doing of a 'work' or a substantial part of it. The term 'work' used here means a literary work, dramatic work, musical work, artistic work, cinematographic film and a sound recording.

b. The Patents Act, 1970 and The Patents Rules, 2003

The umbrella legislation relating to patents is the Patents Act, 1970. The term 'patent' is defined as a monopoly right which is granted to a person who has invented a new and useful article, or an improvement of existing article, or a new process of making an article. It consists of an exclusive right to manufacture the new invented article or manufacture an article according to the invented process for a limited period. Inventions that consist of products or new alloy is called product invention and the corresponding patent to this is referred to as 'product patent'. Whereas, inventions that consists of process or processes of making a known or new alloy is a process invention and patent for this is called a 'process patent'. This Act only provides for process patent and for product like food, pharmaceutical and chemicals, where the inventors are granted only EMR (exclusive marketing rights).

c. The Trade Marks Act, 1999, The Trade Marks Rules, 2002, The Trade Marks (Applications and Appeals to the Intellectual Property Appellate Board) Rules, 2003 and The Intellectual Property Appellate Board (Procedure) Rules, 2003

The Trade Marks Act, 1999 has been enacted to amend and consolidate the law relating to trade marks, to provide for registration and better protection of trade marks for goods and services and for the prevention of the use of fraudulent marks. It repealed the earlier Trade & Merchandise Marks Act, 1958. According to the Trade Marks Act, 1999, the term 'trade mark' means "a mark capable of being represented graphically and which is capable of distinguishing the goods or services of one person from those of others and may include shape of goods, their packaging and combination of colours".

d. The Geographical Indications of Goods (Registration and Protection) Act, 1999 and The Geographical Indications of Goods (Registration and Protection) Rules, 2002

The Geographical Indication of Goods (Registration and Protection) Act, 1999 has been enacted to provide for the registration and better protection of geographical indications relating to goods. According to the Act, the term 'geographical indication' (in relation to goods) means "an indication which identifies such goods as agricultural goods, natural goods or manufactured goods as originating, or manufactured in the territory of a country, or a region or locality in that territory, where a given quality, reputation or other characteristic of such goods is essentially attributable to its geographical origin and in case where such goods are manufactured goods, one of the activities of either the production or of processing or preparation of the goods concerned takes place in such territory, region or locality, as the case may be".

e. The Designs Act, 2000 and The Designs Rules, 2001

The Designs Act, 2000 has been enacted to consolidate and amend the law relating to registration and protection of new and original industrial designs. It repealed and replaced the Designs Act, 1911. According to the Designs Act, 2000, the term 'design' means "only the features of shape, configuration, pattern, ornament or composition of lines or colours applied to any article whether in two dimensional or three dimensional or in both forms, by any industrial process or means, whether manual, mechanical or chemical, separate or combined, which in the finished article appeal to and are judged solely by the eye; but does not include any mode or principle of construction or anything which is in substance a mere mechanical device, and does not include any trade mark as defined in the Trademark Act or property mark as defined in the Indian Penal Code or any artistic work as defined in the Copyright Act, 1957".

f. The Semiconductors Integrated Circuits Layout-Design Act, 2000 and The Semiconductors Integrated Circuits Layout-Design Rules, 2001

The Semi-Conductor Integrated Circuits Layout-Design Act, 2000 has been enacted to provide for the protection of semiconductor integrated circuits layout-designs and for matters connected therewith or incidental thereto. According to the Act, the term 'layout-design' means "a layout of transistors and other circuitry elements and includes lead wires connecting such elements and expressed in any manner in a semiconductor integrated circuit". Here, the term 'semiconductor integrated circuit' means "a product having transistors and other circuitry elements which are inseparably formed on a semiconductor material or an insulating material or inside the semiconductor material and designed to perform an electronic circuitry function".

g. The Protection of Plant varieties and Farmers' Rights Act, 2001 and The Protection of Plant varieties and Farmers Rights' Rules, 2003

The Plant Varieties and Farmers' Right Act,2001 has been enacted to provide for the establishment of an effective system for protection of plant varieties, the rights of farmers and plant breeders and to encourage the development of new varieties of plants. According to the Act, the term 'variety' means "a plant grouping except micro organism within a single botanical tax on of the lowest known rank, which can be:-

(i) defined by the expression of the characteristics resulting from a given genotype of that plant grouping; (ii) distinguished from any other plant grouping by expression of at least one of the said characteristics; and (iii) considered as a unit with regard to its suitability for being propagated, which remains unchanged after such propagation; and includes propagating material of such variety, extant variety, transgenic variety, farmers' variety and essentially derived variety".

h. **The Biological Diversity Act, 2002 and The Biological Diversity Rules, 2004**

   This biodiversity legislation is aimed at conservation of biological resources and associated knowledge as well as facilitating access to them in a sustainable manner and through a just process.

8. Insolvency Laws

Under the Constitution of India ' Bankruptcy & Insolvency ' is Entry 9 in the List III -Concurrent List, (Article 246 –Seventh Schedule to the Constitution) i.e. both Center and State Governments can make laws relating to this subject.

Although article 19 (1)(g) of the Constitution of India gives freedom to practice any profession or to carry on any occupation, trade or business to the citizens of India, there are restrictions on closure of any industrial undertaking.

The Present Nature of Insolvency Process in India can be described as follows:

1. Insolvency/ Liquidation process essentially encompasses aspects of recovery, revival, reconstruction and Winding up and therefore the process has to be seen in a holistic manner with all such aspects in sight; and
2. There is no separate unified Insolvency Code covering all the above aspects in one place at present. Therefore the process is complicated, time consuming and ineffective.

Laws governing Insolvency

The stream of insolvency laws in India can be segregated under three heads:

a. Pre-Insolvency Workouts

Pre-insolvency Work-out Schemes include:

- Companies Act, 1956 (Sections 391 to 396)

- The Sick Industrial Companies (Special Provisions) Act, 1985
- Corporate Debt Restructuring Scheme
- Asset Reconstruction under Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act,2002 (SARFAESI)
- RBI Guidelines on Special Mention Accounts.

b. Personal Insolvencies

This deals with individuals and partnership firms going Insolvent. The consequence of this personal insolvency is declaration of insolvency and incapacity to contract. It is governed by Provincial Insolvency Act,1920 and Presidency Towns Insolvency Act, 1909

c. Corporate Insolvencies

This deals with corporates going insolvent. The consequence is usually winding up of the company under the Companies Act, 1956.

The present Legal and procedural framework relating to Corporate Insolvency apart from several other special provisions like debt recovery laws, is laid out by 4 major legislations, namely:

- The Companies Act 1956
- The Companies (Second Amendment) Act, 2002
- Sick Industrial Companies (Special Provisions) Act, 1985 [SICA]
- Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI) Act, 2002 also known as the Securitization Act
- Recovery of Debts due to Banks and Financial Institutions Act, 1993 (RDB Act) [Debt Recovery Tribunals set up under this Act]

9. Securitization Laws

Securitisation is the process of pooling and repackaging of homogenous illiquid financial assets into marketable securities that can be sold to investors. Securitisation has emerged as an important means of financing in recent times. A typical securitisation transaction consists of the following steps:

- Creation of a special purpose vehicle to hold the financial assets underlying the securities;

- Sale of the financial assets by the originator or holder of the assets to the special purpose vehicle (SPV), which will hold the assets and realize the assets
- Issuance of securities by the SPV, to investors, against the financial assets held by it.

Securitisation Law

Securitization in India is regulated by the Securitization and Re-construction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI), RBI guidelines and The Credit Information Companies (Regulation) Act, 2005.

Securitisation and Reconstruction of financial assets and enforcement of security interest (SARFAESI) Act 2002 is a procedural law . The Act was enacted in 2002 to enable the banks and financial institutions to recover their non-performing assets. However, Supreme Court in the case of Mardia Chemicals Ltd. v/s Union of India had held section 17(2) as unconstitutional. Subsequently, the Act was amended by the enforcement of security Interest and Recovery of Debt Laws (Amendment) Act, 2004 to comply with the order of the Supreme Court. The Act has been under the scrutiny of various courts and a quite a many judgments have been passed over the last 3-4 years. The Act was envisaged to enable banks and Financial Institutions to realize long-term assets, manage problems of liquidity, asset-liability mismatches and improve recovery by taking possession of securities, sell them and reduce non performing assets (NPAs) by adopting measures for recovery or reconstruction. The SARFAESI Act has been largely perceived as facilitating asset recovery and reconstruction.

10. Laws relating to Non Banking Financial Institutions

A Non-Banking Financial Company (NBFC) is a company registered under the Companies Act, 1956 and is engaged in the business of loans and advances, acquisition of shares/stock/bonds/debentures/securities issued by Government or local authority or other securities of like marketable nature, leasing, hire-purchase, insurance business, chit business but does not include any institution whose principal business is that of agriculture activity, industrial activity, sale/purchase/construction of immovable property.

Statutory Provisions relating to Non Banking Financial Institutions

a. General

1. Chapters IIIB, IIIC and V of the Reserve Bank of India Act,1934
2. Certain sections of The Companies Act,1956

3. Companies (Acceptance of Deposit) Rules, 1975
4. Companies (Acceptance of Deposits Amendment) Rules, 1997
5. Companies (Application for Extension of time or Exemption under sub-section (8) of section 58A) Rules, 1979
6. Foreign Exchange Management (Deposit) Regulations, 2000
7. Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000
8. Securities Contracts (Regulation) Act 1956

b. Non Banking Financial Companies

1. Reserve Bank of India (Non Banking Financial Companies) Returns Specifications, 1997
2. Non Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998
3. Non Banking Financial Companies Auditor's Report (Reserve Bank) Directions, 1998
4. Non Banking Financial (Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007
5. Non Banking Financial (Non Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007
6. Non-Banking Financial Companies Auditor's Report (Reserve Bank) Directions, 2008
7. Minimum Net Owned Fund (NOF) for commencement of business of a Non-Banking Financial Institution (NBFI)- April 20, 1999
8. Guidelines for Asset Liability Management (ALM) System in Non-Banking Financial Companies (NBFCs)
9. ' Know Your Customer' Guidelines for NBFCs
10. Know Your Customer Guidelines – Anti Money Laundering Standards
11. Frauds – Future Approach towards monitoring of frauds in NBFCs
12. Guidelines on Corporate Governance
13. Guidelines on Fair Practices Code for Non-Banking Financial Companies
14. Guidelines for Issue of Commercial Paper

15. Guidelines for Issue of Certificates of Deposit
16. Master Circulars - Master Circulars are a one-point reference of instructions issued by the Reserve Bank of India on a particular subject between July-June. These are issued on July 1 every year and automatically expire on June 30 next year.

c. The Housing Finance Companies (NHB) Directions 2001

d. Mortgage Guarantee Companies

1. Mortgage Guarantee Companies Prudential Norms (Reserve Bank) Directions, 2008
2 Mortgage Guarantee Companies Investment (Reserve Bank) Directions, 2008
3. Regulatory Framework for Mortgage Guarantee Company (circular dated 15.1.2008)

e. The Securitisation Companies and Reconstruction Companies (Reserve Bank) Guidelines and Directions, 2003

f. Miscellaneous Non-Banking Companies

1. Miscellaneous Non Banking Companies (Reserve Bank) Directions, 1977
2. Non-banking Financial Companies and Miscellaneous Non-Banking Companies (Advertisement) Rules, 1977.
3. Chit Funds Act, 1982

g. Residuary Non Banking Companies (Reserve Bank) Directions, 1987

h. Infrastructure Finance Companies

1. Infrastructure Finance Companies - Notification No. DNBS. 213 / CGM(ASR)-2010 dated February 12, 2010

i. Others

1. Micro Financial Sector (Development and Regulation) Bill, 2007
2. Reports on Money Lending and Nidhis

   - Report of the Technical Group to Review Legislations on Money LendinG

   - Report Of The Expert Group On Nidhis
3. State laws on Money Lending

4. State Laws on protection of interests of depositors in financial establishments

11. Competition Laws

Competition law refers to laws enacted by governments to regulate competitive markets for goods and services, leading to the modern competition or antitrust laws around the world today.

India's competition law is contained in the Competition Act 2002. The Competition Act 2002 received assent of the President of India, on 13th January 2003 and was published in the gazette of India on 14th January 2003.

12. Consumer Laws

Consumer protection laws or Consumer Laws are designed to ensure fair competition and the free flow of truthful information in the marketplace. Consumer Protection laws are a form of government regulation which aim to protect the interests of consumers.

Legislations related to Consumer Protection in India

The Consumer Protection Act, 1986 is the main legislation pertaining to Consumer protection.

Other Legislations governing Consumer Protection include:

- The Consumer Protection Rules, 1987
- The Consumer Protection Regulations, 2005
- Consumer Welfare Fund Rules, 1992
- Bureau of Indian Standards (Recognition of Consumers' Associations) Rules, 1991
- The Essential Commodities Act, 1955
- Prevention of Black-marketing and Maintenance of Supplies of Essential Commodities Act, 1980
- The Emblems And Names (Prevention of Improper Use) Act, 1950
- The Indian Contract Act, 1872
- The Sales of Goods Act, 1930
- The Dangerous Drugs Act, 1930
- The Agricultural Produce (Grading and Marketing) Act, 1937
- The Indian Standards Institution (Certification Marks) Act, 1952

- The Prevention of Food Adulteration Act, 1954
- The Standards of Weights and Measures Act, 1976 (This Act will be enforced till the Legal Metrology Rules are notified.)
- Legal Metrology Act, 2009

13. Laws relating to Cooperative Societies

A Co-operative Society can be formed as per the provisions of the Co-operative Societies Act, 1912. At least ten persons having the capacity to enter into a contract with common economic objectives, like farming, weaving, consuming, etc. can form a Co-operative Society. A joint application along with the bye-laws of the society containing the details about the society and its members, has to be submitted to the Registrar of Co-operative Societies of the concerned state. After scrutiny of the application and the bye–laws, the registrar issues a Certificate of Registration.

Laws regulating Cooperative Societies in India are:

(a) State Cooperative Societies Acts of individual states; and

(b) Multi-State Cooperative Societies Act, 2002 for the multi-state Cooperative societies with Area of operation in more than one State.

(c) Companies Act, 1956 (for producer companies)

Some legislations governing Co-operative societies and Multi State Cooperative Societies include:

1. The Co-operative Societies Act, 1912
2. Delhi Cooperative Societies Act, 2003
3. The Sikkim Co-operative Societies Act, 1978
4. The Maharashtra Co-operative Societies Act, 1960
5. The Gujarat Co-Operative Societies Act, 1962
6. Kerala Co-operative Societies Act, 1969
7. Karnataka Co-operative Societies Act, 1959
8. The Meghalaya Co-operative Societies Act, 1976
9. Tamil Nadu cooperative Societies Act, 1983
10. Assam Cooperative Societies Act, 1949
11. The Multi-State Co-operative Societies Act, 2002
12. The Multi-State Co-operative Societies Rules, 2002

14. Corporate Laws

Companies incorporated in India and foreign corporations with a presence in India are regulated by the provisions of the Companies Act 1956. The Ministry of Corporate Affairs of the Government of India is responsible for the administration of the Act.

Legislations Pertaining To Companies

The main legislation pertaining to Companies is the Companies Act 1956. A number of Rules and Regulations have been framed under the Act.

Compliance Rules

(i) Companies (Accounting Standards) Rules, 2006

(ii) Companies (Issue of Share Certificate) Rules, 1960

(iii) Trustees (Declaration of Holdings of Shares and Debentures) Rules, 1964

(iv) The Companies (Public Trustee) Rules, 1973

(v) Companies (Particulars of Employees) Rules, 1975

(vi) Companies (Transfer of Profits to Reserves) Rules, 1975

(vii) The Companies (Declaration of Beneficial Interest in Shares) Rules, 1975

(viii) Public Companies (Terms of Issue of Debentures and Raising of Loans with Option to Convert such Debentures or Loans into Shares) Rules, 1977

(ix) Companies Unpaid Dividend (Transfer to General Revenue Account of the Central Government) Rules, 1978

(x) Companies (Appointment and Qualifications of Secretary) Rules, 1988

(xi) Companies (Disclosure of Particulars in the Report of Board of Directors) Rules, 1988

(xii) Private Limited Company and Unlisted Public Limited Company (Buy Back of Securities) Rules 1999

(xiii) The Companies ((Issue of Share Capital with Differential Voting Rights) Rules, 2001

(xiv) The Companies (Appointment of the Small Shareholders Director) Rules, 2001

(xv) The Companies (Passing of the Resolution by Postal Ballot) Rules, 2001

(xvi) Unlisted Public Companies (Preferential Allotment) Rules, 2003

Audit rules

(i) Companies (Branch Audit Exemption) Rules, 1961

(ii) Manufacturing and Other Companies (Auditor's Report) Order, 1988

(iii) Cost Audit (Report) Rules, 1996

(iv) Cost Accounting Record Rules of 44 products

(v) Cost Audit Report Rules 2001

(vi) Companies Auditors Report order 2003 (CARO)

Company Law Board

(i) The Offices Of The Company Law Board Benches (Destruction Of Records) Rules, 1980

(ii) Company Law Board (Fees on Applications and Petitions) Rules, 1991

(iii) Company Law Board Regulations, 1991

(iv) Company Law Board (Qualifications, Experience and Other Conditions Of Service of Members) Rules, 1993

Court liquidator rules

(i) Companies (Court) Rules, 1959

(ii) Companies (Official Liquidator's Accounts) Rules, 1965

(iii) Companies Liquidation Accounts Rules, 1965

Deposit rules

(i) Companies (Acceptance of Deposits) Rules, 1975

(ii) Companies (Acceptance of Deposits Amendment) Rules, 1997

Destruction of records rules

(i) Companies (Preservation and Disposal of Records) Rules, 1966

(ii) The Offices Of The Regional Directors (Destruction Of Records) Rules, 1976

(iii) The Office Of The Public Trustee (Destruction of Records) Rules, 1984

(iv) Disposal of Records (in the Offices of the Registrar of Companies) Rules, 2003

General rules and regulations

(i) Companies Regulations, 1956

(ii) Companies (Central Government's) General Rules and Forms, 1956

(iii) Application of section 159 to Foreign Companies Rules 1975

(iv) Companies (Appointment of Sole Agents) Rules, 1975

(v) Companies (Declaration of Dividend out of Reserves) Rules, 1975

(vi) Companies (Application for Extension of time or Exemption under sub-section (8) of section 58A) Rules, 1979

(vii) Companies (Fees on Applications) Rules, 1999

(viii) The Companies (Compliance Certificate) Rules, 2001

Investor rules

(i) The Investors Education and Protection Fund (Awareness and Protection of Investors) Rules 2001

15. Laws Relating To Limited Liability Partnership (LLP)

The Limited Liability Partnership (LLP) is viewed as an alternative corporate business vehicle that provides the benefits of limited liability but allows its members the flexibility of organizing their internal structure as a partnership based on a mutually arrived agreement.

Legislations Regulating Limited Liability Partnership

1. Limited Liability Partnership Act, 2008
2. Companies Act, 1956 (The LLP Act 2008 empowers the Central Government under section 67 to apply the provisions of the Companies Act 1956 or any other Act with appropriate exception, modifications and adaptation to LLP.)
3. Income Tax Act, 1961

16. Laws Relating To Micro, Small And Medium Enterprises (MSMES)

The MSME sector falls under the jurisdiction of the Ministry of Micro, Small and Medium Enterprises (Sukshma Laghu Aur Madhyam Udyam Mantralaya), of the Government of India.

In India, the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006 is the main legislation governing MSMEs. The Act came into force from 2nd Oct, 2006.

The Following categories of Laws amongst others are applicable to MSME sector

- Fiscal Laws
- Foreign Exchange Laws

- o Foreign Trade Laws
- o Labour & Industrial Laws
- o Environmental and Safety Laws
- o Laws applicable to various forms of Business organisation
- o Intellectual Property Laws
- o Competition Law
- o Banking & Financial Institutions Laws
- o Industry Specific Laws

17. Banking Laws

The banking system in India comprises commercial and cooperative banks, of which the former accounts for more than 90 per cent of banking system's assets.

Important legislations pertaining to Banking sector

Core Legislations

1. The Banking Regulation Act, 1949
2. The Reserve Bank of India Act, 1934

Acts governing specific functions

1. Public Debt Act, 1944
2. Government Securities Act, 2006
3. Securities Contract (Regulation) Act, 1956
4. Indian Coinage Act, 1906
5. Foreign Exchange Management Act, 1999
6. Payment and Settlement Systems Act, 2007

Acts governing Banking Operations

1. Companies Act, 1956
2. Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970
3. Bankers' Books Evidence Act, 1891
4. The Negotiable Instruments Act, 1881
5. The Prevention of Money Laundering Act, 2002
6. Securities and Exchange Board of India Act, 1992

7. Contract Act, 1872
8. Transfer of Property Act, 1882
9. Income Tax Act, 1961
10. Industrial Disputes (Banking and Insurance Companies) Act, 1949
11. The Recovery Of Debts Due To Banks And Financial Institutions Act, 1993
12. The Securitisation And Reconstruction Of Financial Assets And Enforcement Of Security Interest Act, 2002

Acts governing Individual Institutions

1. The State Bank of India Act, 1954
2. The State Bank of India (Subsidiary Banks) Act, 1959
3. The State Financial Corporations Act, 1951
4. Deposit Insurance and Credit Guarantee Corporation Act, 1961
5. Regional Rural Banks Act, 1976
6. National Bank for Agriculture and Rural Development Act, 1981
7. Export-Import Bank of India Act, 1981
8. National Housing Bank Act, 1987
9. The Small Industries Development Bank of India Act, 1989
10. The Industrial Finance Corporation (Transfer of Undertaking and Repeal) Act, 1993
11. Industrial Investment Bank of India Act, 1997

18. Insurance Laws

The insurance sector in India has taken a full circle from being an open competitive market to nationalization and back to a liberalized market again.

Laws governing Insurance Sector

The Insurance sector in India is regulated by the following Acts and Rules:

1) Insurance Act, 1938
    a. Insurance Rules, 1939
    b. Redressal of Public Grievance Rules, 1998
2) The Industrial Disputes (Banking and Insurance Companies) Act, 1949
3) Life Insurance Corporation Act, 1956

4) Deposit Insurance And Credit Guarantee Corporation Act, 1961
5) The Marine Insurance Act, 1963
6) The Personal Injuries (Compensation Insurance) Act, 1963
7) General Insurance Business (Nationalization) Act, 1972
8) The Public Liability Insurance Act, 1991
   a. The Public Liability Insurance Rules, 1991
9) Insurance Regulatory and Development Authority (IRDA) Act, 1999
10) Foreign Exchange Management (Insurance) Regulations, 2000
11) Actuaries Act, 2006
    a. Actuaries (Election to the Council) Rules, 2008
    b. Actuaries (Procedure for enquiry of Professional and other Misconduct) Rules, 2008

Rules and Regulations framed under the Insurance Regulatory and Development Authority (IRDA) Act, 1999:

1) IRDA (Actuarial Report and Abstract) Regulations, 2000
2) IRDA (Insurance Advertisements and Disclosure) Regulations, 2000
3) IRDA (Licensing of Insurance Agents) Regulations, 2000
4) IRDA (Life Insurance-Reinsurance) Regulations, 2000
5) IRDA (General Insurance-Reinsurance) Regulations, 2000
6) IRDA (Appointed Actuary) Regulations, 2000
7) IRDA (Assets, Liabilities and Solvency Margin of Insurers) Regulations, 2000
8) IRDA (Meetings) Regulations, 2000
9) IRDA (Registration of Indian Insurance Companies) Regulations, 2000
10) The Insurance Advisory Committee (Meeting) Regulations, 2000
11) IRDA (Investment) Regulations, 2000
12) IRDA (Salary and Allowances Payable To, and Other Terms and Conditions of service of, Chairperson and Other Members) Rules, 2000
13) IRDA (Insurance Surveyors and Loss Assessors (Licensing, Professional Requirements and Code of Conduct)) Regulations, 2000
14) IRDA (Conditions of Service of Officers and other Employees) Regulations, 2000

15) IRDA (Annual Report – Furnishing of Returns, Statements and Other Particulars) Rules, 2000
16) IRDA (Third Party Administrators - Health Services) Regulations, 2001
17) IRDA (Form of Annual Statement of Accounts and Records) Rules, 2001
18) IRDA (Re-Insurance Advisory Committee) Regulations, 2001
19) IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002
20) IRDA (Protection of Policyholders' Interests) Regulations, 2002
21) IRDA (Distribution of Surplus) Regulations, 2002
22) IRDA (Manner of Receipt of Premium) Regulations, 2002
23) IRDA (Obligations of Insurers to Rural and Social Sectors) Regulations, 2002
24) IRDA (Licensing of Corporate Agents) Regulations, 2002
25) IRDA (Insurance Brokers) Regulations, 2002
26) IRDA (Qualification of Actuary) Regulations, 2004
27) IRDA (Micro-Insurance) Regulations, 2005
28) IRDA (Sharing of Database for Distribution of Insurance Products) Regulations, 2010
29) IRDA (Treatment of Discontinued Linked Insurance Policies) Regulations, 2010

19. Securities Laws

As per section 2(h) of the Securities Contracts (Regulation) Act, 1956 - "securities" include—

(i) Shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

- (ia) derivative
- (ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes;
- (ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;

(id) units or any other such instrument issued to the investors under any mutual fund scheme;

(ii) Government securities;

(iia) such other instruments as may be declared by the Central Government to be securities; and

(iii) rights or interest in securities;

These securities are traded on a stock exchange. A Stock Exchange is a body of individuals, whether incorporated or not, constituted before corporatization and demutualization, or a body corporate incorporated under the Companies Act, 1956 whether under a scheme of corporatization and demutualization or otherwise - for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities.

Main Legislations governing securities:

1. The Securities Contracts (Regulation) Act, 1956
2. The Securities & Exchange Board of India Act, 1992
3. The Depositories Act, 1996

The other relevant laws which affect the capital market are:-

1. The Foreign Exchange Management Act, 1999
2. Arbitration and Conciliation Act, 1996;
3. The Companies Act, 1956;
4. Recovery of Debts due to Banks and Financial Institutions Act, 1993
5. Banking Regulation Act 1949
6. Benami Transactions (Prohibition) Act, 1988
7. Indian Penal Code, 1860
8. Indian Evidence Act, 1872

20. Laws relating to International Trade

The regulation of International Trade is done through the WTO at the global level and through several other regional arrangements like MERCOSUR (in South America), NAFTA (between US, Canada, and Mexico).

Laws governing International Trade

India's principal law governing foreign trade is the Foreign Trade (Development and Regulation) Act, 1992.

In accordance with the Act, the Government of India formulates and announces a foreign trade policy and amends it from time to time.

The latest Foreign Trade Policy (FTP) was announced in 2009. It shall come into force with effect from 27th August, 2009 and shall remain in force upto 31st March, 2014 unless otherwise specified. It provides a five year plan and comprehensive policy for the development of India's foreign trade.

The Department of Commerce under the Ministry of Commerce and Industry is the most important organ concerned with the regulation, development and promotion of foreign trade in India.

21. Foreign Exchange Management Laws

According to Section 2(n) of Foreign Exchange Management Act, 1999 (FEMA), Foreign Exchange means foreign currency and includes, (i) deposits, credits and balances payable in any foreign currency, (ii) drafts, travellers cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency (iii) drafts, travellers cheques, letters of credit or bills of exchange drawn by banks, institutions or person outside India, but payable in Indian currency. Foreign currency means any currency other than Indian currency. (Sec.2(m) of Foreign Exchange Management Act, 1999)

Section 47 of the Foreign Exchange Management Act, 1999 empowers the Reserve Bank of India to make regulations to carry out the provisions of the Act and Rules made thereunder. The regulations can be made for the following:

a) The permissible classes of capital account transactions, the limits of admissibility of foreign exchange for such transactions, and the prohibition, restriction or regulation of certain capital account transactions;

b) The manner and the form in which the declaration is to be furnished by exporters;

c) The period within which and the manner of repatriation of foreign exchange;

d) The limit up to which any person may possess foreign currency or foreign coins;

e) The class of persons and the limit up to which foreign currency account may be held or operated;

f) The limit up to which foreign exchange acquired may be exempted;

g) The limit up to which foreign exchange acquired may be retained;

h) Any other matter which is required to be, or may be, specified.

23 Regulations have been issued under the Foreign Exchange Management Act, 1999

22. Right to Information Law

Right to Information is a part of fundamental rights under Article 19(1) of the Constitution. Article 19 (1) says that every citizen has freedom of speech and expression. The right to information is implicitly guaranteed by the Constitution. However, with a view to set out a practical regime for securing information, the Indian Parliament enacted the Right to Information Act, 2005 and thus gave a powerful tool to the citizens to get information from the Government as a matter of right. This law is very comprehensive and covers almost all matters of governance and has the widest possible reach, being applicable to Government at all levels- Union, State and Local as well as recipients of government grants.

The Right to Information Act is a Central Act and came into force on the 12th October, 2005. Even before the Central Act, Right to Information laws had been enacted by thirteen states with Tamil Nadu being the first to introduce one. The other states to have laws were Andhra Pradesh, Assam, Delhi, Goa, Jammu & Kashmir, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Orissa, Rajasthan, and Uttar Pradesh.

Legislation Governing the Right to Information

The Right to Information Act 2005 is the legislation governing the right to Information in India.

The Rights to information Act came into force on the 12th October, 2005. This is a Central Act which extends to the whole of India except the state of Jammu & Kashmir. The Act contains 6 chapters and 31 sections with 2 schedules.

23. Laws relating to Special Economic Zones (SEZ)

Special Economic Zones (SEZs) are specifically delineated duty-free enclaves treated as a foreign territory for the purpose of industrial, service and trade operations, with exemption from customs duties and a more liberal regime in respect of other levies, foreign investment and other transactions.

Laws governing SEZ

With effect from 10th February, 2006 the activities relating to Special Economic Zones are guided by the provisions contained in the Special economic zones Act, 2005 and the Special economic zones Rules, 2006.

Previously Special Economic Zones in India were governed by Chapter X-A of the Customs Act, the Special Economic Zones Rules, 2003, and the Special Economic Zones (Customs Procedures) Regulations, 2003 and Chapter 7 and 7A of Foreign Trade Policy. After the enactment of the SEZ Act, 2005 Chapter X-A of the Customs Act, the Special Economic Zones Rules, 2003, and the Special Economic Zones (Customs Procedures) Regulations, 2003 are not in operation.

Apart from The Special Economic Zones Act 2005, various State also have there acts, rules and policies pertaining to SEZ like:

- Gujarat SEZ Act
- Haryana SEZ Act
- Madhya Pradesh SEZ Act
- West Bengal SEZ Act
- Tamil Nadu SEZ Act
- Punjab SEZ Act
- Gujarat SEZ Authority Rule
- Jaharkhand Special Economic Zone Policy
- Uttar Pradesh SEZ Revised Policy – 2007
- Karnataka State Policy for Special Economic Zones – 2009
- Punjab Special Economic Zone Policy - 2005
- Chandigarh Administration Special Economic Zone Policy - 2005
- Kerala Special Economic Zone Policy-2008
- West Bengal Special Economic Zone Policy
- Maharashtra Special Economic Zone Policy
- Madhya Pradesh Special Economic Zone Policy

24. Energy Laws

Under Section 2(h) of the Energy Conservation Act 2001, Energy means any form of energy derived from fossil fuels, nuclear substances or materials, Hydro-electricity and includes electrical energy or electricity generated from renewable sources of energy or biomass connected to the grid.

Legislations Pertaining To Energy

"Energy Law" is a comprehensive term and would include the following:

a. Laws governing Electricity

b. Laws governing Energy Conservation

c. Laws governing the Petroleum and Natural Gas sector including all fuels derived from petroleum sources

d. Laws governing the Coal sector including all forms of coal

e. Laws governing Nuclear Energy for electricity generation

A few of the legislations falling in different heads under energy laws are:

- The Atomic Energy Act, 1962
- The Electricity Act, 2003
- Electricity Regulatory Commissions Act, 1998
- Energy Conservation Act, 2001
- The Petroleum Act, 1934
- The Petroleum and Natural Gas Regulatory Board Act 2006
- Petroleum and Natural Gas (Safety in Offshore Operations) Rules, 2008
- The Oilfields (Regulation and Development) Act, 1948
- The Mines and Minerals (Regulation and Development) Act of 1957
- The Coal Mines Regulations, 1957
- The Gas Cylinder Rules, 1981
- The Petroleum Tax Guide, 1999

25. Carriage Laws and Multi-Modal Transportation of Goods

Laws Governing Carriage of Goods and Multi Modal Transportation

Accordingly, the law relating to carrying of goods in India is contained in the following enactments:

1. In case of carriage of goods by land:

(i) Carriage by Road Act, 2007 (Earlier enactment - The Carriers Act, 1865).

(ii) The Railways Act, 1989.

2. In case of carriage of goods by sea:

(i) The (Indian) Bills of Landing Act, 1856.

(ii) The Carriage of Goods by Sea Act, 1925.

(iii) The Merchant Shipping Act, 1958.

(iv) The Marine Insurance Act, 1963.

3. In the case of carriage of goods by air:

(i) The Carriage by Air Act, 1972.

Wherever there is no specific provision for a particular matter in these statutes, then the Indian Courts resort to English Common Law.

Laws governing multimodal transportation of goods

Multimodal transportation is the movement of cargo from the point of origin to the final destination, outside India, by using two or more modes of transport. Therefore the combination of all four modes of transportation i.e. (a) Air (b) Road (c) Rail (d) Sea is defined as `multimodal transport system'.

The Multimodal Transportation of Goods Act, 1993 governs multi modal transportation of goods.

26. Laws Relating to Civil Aviation

The Aviation industry in India is one of the fastest growing sectors globally.
The Ministry of Civil Aviation is responsible for formulation of national policies and programmes for the development and regulation of the Civil Aviation sector in the country. It is responsible for the administration of the Aircraft Act, 1934, Aircraft Rules, 1937 and various other legislations pertaining to the aviation sector in the country. This Ministry exercises administrative control over attached and autonomous organizations like the Directorate General of Civil Aviation, Bureau of Civil Aviation Security and Indira Gandhi Rashtriya Udan Academy and affiliated Public Sector Undertakings like National Aviation Company of India Limited, Airports Authority of India and Pawan Hans Helicopters Limited. The Commission of Railway Safety, which is responsible for safety in rail travel and operations in terms of the provisions of the Railways Act, 1989 also comes under the administrative control of this Ministry.

Laws Governing Civil Aviation

Acts

1. Aircraft Act, 1934(XXII of 1934)
2. Airport Authority of India Act, 1994
3. Air Corporations (Transfer of Undertakings and Repeal) Act. 1994.
4. The Airports Economic Regulatory Authority of India Act,2008

Rules

1. Aircraft Rules, 1937

2. Airports Authority of India (Annual Report and Annual Statement of Accounts)Rules, 2003
3. Airports Authority of India (Conditions of Service of the Chairman and Other Members) Rules,2003
4. Airports Authority of India (Manner of Investment of Funds) Rules, 2002

Policies

1. Domestic Air Transport
   - Categories of Air Transport Services
   - Public Private Partnership in Airport Infrastructure
   - Foreign Equity Participation in Air Transport Services
   - Requirements for Becoming Air Cargo Operator
   - Procedure for starting Scheduled/Non Scheduled Air
   - Transport Services
   - Route Dispersal Guidelines
2. Airport Infrastructure
3. Inclusive Tour Package Charter Flight
4. Greenfield Airport
5. Removal of Restriction on Photography

27. Laws Relating To Telecommunications

The telecom services have been recognized as an important tool for socio-economic development for a nation. It is one of the prime support services needed for rapid growth and modernization of various sectors of the economy. Indian telecommunication sector has undergone a major process of transformation through significant policy reforms, particularly beginning with the announcement of NTP 1994 and was subsequently re-emphasized and carried forward under NTP 1999.

Telecom Related Legislations, Acts & Regulations

1. Indian Telegraph Act, 1885
2. Indian Telegraph Rules, 1951
3. Indian Wireless Act, 1933
4. Information Technology Act, 2000
5. Telecom Regulatory Authority of India (TRAI) Act 1997

6. Cable Television Networks (Regulation) Act, 1995
7. Regulation on Guidelines for registration of Consumer Organisation / NGO and their interaction with TRAI, 2001
8. Regulation on Quality of Service Dial-Up and Leased Line Internet Access Service, 2001
9. The Telecommunication Interconnection (Charges and Revenue Sharing) Regulation, 2001
10. The Telecommunication Interconnection (Port Charges) Regulation 2001
11. The TRAI (Levy of fees and Other Charges for Tariff Plans) Regulation, 2002
12. Regulation on Quality of Service For VOIP Based International Long Distance Service, 2002
13. The Telecommunication INTERCONNECTION USAGE CHARGES (IUC) Regulation, 2003
14. Regulation on Reporting System on Accounting Separation
15. Regulation on Quality of Service of Basic and Cellular Mobile Telephone Services ,2005 (11 of 2005).
16. Regulation on Code of Practice for Metering and Billing Accuracy
17. Regulation on the Standards of Quality of Service (Broadcasting and Cable services) (Cable Television - CAS Areas) Regulation, 2006 (8 of 2006)
18. TRAI issues Regulations on Quality of Service Standards for Broadband Service

Government Policy and Guidelines

1. National Telecom Policy, 1994
2. New Telecom Policy, 1999
3. Broadband Policy, 2004
4. Uplinking Guidelines
5. Downlinking Guidelines
6. DTH Guidelines
7. National Frequency Allocation Plan (NFAP), 2002

28. Laws relating to Pharmaceuticals

The pharmaceutical industry is highly regulated in India.

The Drugs Controller General of India ("DCGI"), established under the Government of India's Ministry of Health and Family Welfare, is the nodal agency that regulates India's drug market including product safety and efficacy, clinical trials, market authorization, and post-market surveillance. The Drugs and Cosmetics Act, 1940 ("Drugs Act") and the Drugs Rules, 1945 ("Drugs Rules") regulate the import, manufacture, licensing, testing, distribution, and sale of drugs in India. The DCGI heads the Central Drugs Standard Control Organization and formulates policies in order to implement the Drugs Act. The DCGI also coordinates the activities of the different State Drug Control Organizations. Drug prices in India are regulated under the Drug Prices Control Order, 1995 ("DPCO").

The Government of India has also created a new department (2nd July, 2008) —Department of Pharmaceuticals—under the Ministry of Chemicals and Fertilizers to deal with issues relating to drugs and pharmaceuticals, excluding those specifically allotted to other departments. The objective of the creation of the Department is to give greater focus and thrust on the development of Pharmaceutical Sector in the country and to regulate various complex issues related to pricing and availability of medicines at affordable prices, research & development, protection of intellectual property rights and international commitments related to pharmaceutical sector which require integration of work with other ministries. All the drugs and pharmaceuticals, unless specifically allotted to any other department, would come under the purview of the Department of Pharmaceuticals.

Laws Governing Pharmaceutical Sector

(i) The Drugs and Cosmetics Act, 1940

(ii) Drug Policy 1986

(iii) The Drugs (Prices Control) Order 1995

(iv) The Pharmacy Act, 1948

(v) Pharmaceutical Policy 2002

(vi) The National Institute of Pharmaceutical Education and Research Act, 1998

(vii) The Drugs and Magic Remedies (Objectionable Advertisement) Act, 1954

(viii) The Narcotic Drugs and Psychotropic Substances Act, 1985

(ix) The Medicinal and Toilet Preparations (Excise Duties) Act, 1956

(x) Essential Commodities Act, 1955

(xi) Some Other Laws

There are some other laws which have a bearing on pharmaceutical manufacture, distribution and sale in India. The important ones being:

The Industries (Development and Regulation) Act, 1951

The Trade and Merchandise Marks Act, 1958

The Indian Patent and Design Act, 1970

Factories Act

29. Information Technology and Cyber Laws

The Information Technology (IT) Act 2000 is the main legislation pertaining to information technology and cyber laws in India and it aims to provide a legal and regulatory framework for promotion of e-Commerce and e-Governance.

The Department of Information Technology (DIT) under the Ministry of Communications and Information Technology, Government of India is responsible for all matters relating to Cyber Laws, administration of the Information Technology Act. 2000 (21 of 2000) and other IT related laws.

Legislations Governing the Information Technology Sector

i. The Information Technology Act, 2000
ii. The Information Technology (Certifying Authorities) Rules 2000
iii. The Cyber Regulations Appellate Tribunal (Procedure) Rules 2000
iv. The Information Technology (Certifying Authority) Regulations 2001
v. The Information Technology (Security Procedure) Rules 2004
vi. The Information Technology (Amendment) Act 2008
vii. Cyber Appellate Tribunal (Salary, Allowances and other terms and conditions of services of chairperson and members) rules, 2009
viii. Cyber Appellate Tribunal (Procedure for investigation of misbehavior or incapacity of chairperson and members) rules, 2009
ix. Information Technology (Procedure and safeguards for interception, monitoring and decryption of Information) Rules, 2009
x. Information Technology (Procedure and safeguards for blocking for access of information by public) Rules, 2009
xi. Information Technology (Procedure and safeguards for monitoring and collecting traffic data or Information) Rules, 2009
xii. Indian Penal Code 1860
xiii. Indian Evidence Act, 1872

30. Environmental Laws

The Indian constitution is amongst the few in the world that contains specific provisions on environment protection. In the Constitution of India it is clearly stated that it is the duty of the state to 'protect and improve the environment and to safeguard the forests and wildlife of the country'. It imposes a duty on every citizen 'to protect and improve the natural environment including forests, lakes, rivers, and wildlife'. Reference to the environment has also been made in the Directive Principles of State Policy as well as the Fundamental Rights.

The gamut of Environmental Laws in India falls under the following broad categories:

- Environment Protection
- Water Pollution
- Air Pollution
- Public Liability Insurance
- Animal Welfare
- Wildlife
- Forest Conservation
- Biodiversity

Important Environmental Legislations in India

Some Important Environment Legislations are:

- The Environment (Protection) Act, 1986
- The Environment (Protection) Rules, 1986
- Hazardous Waste (Management and Handling) Rules, 1989
- The Public Liability Insurance Act, 1991
- The Biomedical waste (Management and Handling) Rules, 1998
- The Municipal Solid Wastes (Management and Handling) Rules, 2000
- The Biological Diversity Act, 2002
- Water (Prevention and Control of Pollution) Act, 1974
- The Water (Prevention and Control of Pollution) Cess Act, 1977
- The Water (Prevention and Control of Pollution) Cess Rules, 1978
- Air (Prevention and Control of Pollution) Act, 1981

- The Air (Prevention and Control of Pollution) Rules,1982
- The Atomic Energy Act, 1982
- The Indian Forest Act, 1927
- Forest Conservation Act 1980
- The Wildlife Protection Act, 1972,

31. Carbon Credit

Carbon credits are a key component of national and international emissions trading schemes that have been implemented to mitigate global warming. They provide a way to reduce greenhouse effect emissions on an industrial scale by capping total annual emissions and letting the market assign a monetary value to any shortfall through trading.

The framework governing carbon credit is contained in the United Nations Framework Convention on Climate Change (UNFCCC) and the Kyoto Protocol.

Legislations Regulating Carbon Credits Mechanism

The United Nations Framework Convention on Climate Change (UNFCCC) is an international environmental treaty that sets general goals and rules for confronting climate change. It was entered into force on 21st March 1994.

The UNFCCC provides the basis for concerted international action to mitigate climate change and to adapt to its impacts. Its provisions are far-sighted, innovative and firmly embedded in the concept of sustainable development. States and regional economic integration organizations may become Parties to the Convention. Currently the Convention has been ratified by 194 parties (193 States and 1 regional economic integration organization).

The Kyoto Protocol is an international and legally binding agreement to reduce greenhouse gas emissions worldwide and is an addition to the UNFCCC treaty. The Kyoto Protocol was adopted in Kyoto, Japan, on 11 December 1997 and entered into force on 16 February 2005. Currently, 192 parties (191 States and 1 regional economic integration organization) of the UNFCCC have ratified the Protocol. The major feature of the Kyoto Protocol is that it assigns mandatory targets for 37 industrialized nations and the European Community to reduce their emission of the specified 6 greenhouse gases (GHGs). These amount to an average of five per cent against 1990 levels over the five-year period 2008-2012.

India signed UNFCCC on 10th June 1992 and ratified it on 1st November 1993. India acceded to the Kyoto Protocol on 26th August 2002. Under the UNFCCC, developing countries such as India do not have binding GHG mitigation commitments in recognition of their small contribution to the greenhouse problem as well as low financial and technical capacities.

The Ministry of Environment and Forests is the nodal agency for climate change issues in India.

VII. Social Audit

1. Social Audit

- Social Audit is a tool with which government departments can plan manage and measure non-financial activities and monitor both internal and external consequences of the department/ organization's social and commercial operations..
- It is an instrument of social accountability for an organisation. In other words, Social Audit may be defined as an in depth scrutiny and analysis of the working of any public utility in to its social relevance.
- It is a review of the public-interest, nonprofit, and social activities of a business. These audits usually are performed primarily for internal benefit and typically are not released to the public. The social audit may be performed routinely by internal or external consulting groups, as part of regular internal audits. These evaluations consider social and environmental impacts of business activities.
- Social auditing provides an assessment of the impact of an organisation's non-financial objectives through systematically and regularly monitoring its performance and the views of its stakeholders

2. Purpose of the Social Audit

- Answers to some basic questions about Social Audit and understanding the reasons for conducting Social Audit, certainly helps in identifying the purpose of social audit.
- The purpose of conducting Social Audit is not to find fault with the individual functionaries but to assess the performance in terms of social, environmental and community goals of the organisation.
- It is a way of measuring the extent to which an organisation lives up to the shared values and objectives it has committed itself to. It provides an assessment of the impact of organisation's non financial

objectives through systematic and regular monitoring, based on the views of its stakeholders.

3. Salient Features of Social Audit

The goal of Social Audit is to achieve continuously improved performances in relation to the chosen social objectives. Eight specific key principles have been identified from Social Auditing practices around the world. They are:

1. **Multi-Perspective/Polyvocal.** Aims to reflect the views (voices) of all those people (stakeholders) involved with or affected by the organisation/department/programme.
2. **Comprehensive.** Aims to (eventually) report on all aspects of the organisation's work and performance.
3. **Participatory.** Encourages participation of stakeholders and sharing of their values.
4. **Multidirectional.** Stakeholders share and give feedback on multiple aspects.
5. **Regular.** Aims to produce social accounts on a regular basis so that the concept and the practice become embedded in the culture of the organisation covering all the activities.
6. **Comparative.** Provides a means, whereby, the organisation can compare its own performance each year and against appropriate external norms or benchmarks; and provide for comparisons with organisations doing similar work and reporting in similar fashion.
7. **Verification.** Ensures that the social accounts are audited by a suitably experienced person or agency with no vested interest in the organisation.
8. **Disclosure.** Ensures that the audited accounts are disclosed to stakeholders and the wider community in the interests of accountability and transparency.

4. Social Audit as a Function

Social Audit as a function is used by government departments, private enterprises as well as the civil society. However, the scope in terms of audit boundaries would be specific to that of a government department, private organisation, an NGO or a community. In case of private organisations, the emphasis may be on balancing financial viability with its impact on the community and environment. In case of NGOs, in addition to using them to maximize the impact of their intervention programme, they could also be used as effective advocacy tools. Depending on the availability of resources

Social Audit can be comprehensive, state-wide, and can also be localized to the community level.

5. Performing Social Audit

The six steps followed in the performance of Social Audit are:

1. Preparatory activities
2. Defining audit boundaries and identifying stakeholders
3. Social accounting and book-keeping
4. Preparing and using social accounts
5. Social audit and dissemination
6. Feedback and institutionalization of social audit

The first two steps are critical when a department decides to incorporate social accounting, social book-keeping and social auditing. The department needs to look at its vision, goals, current practices and activities to identify those that are amenable to social auditing purposes. Small work groups (say, seven persons) are to be formed which would spend about two days each to list down the social vision, core values, social objectives and map stakeholders and their involvement. Ensure involvement of various functionaries with due representation to gender, while forming small groups. The small groups should have access to project documents, process documentation, department guidelines and policy notes.

The next activity would be to assign the task of matching the activities with the social objectives and identifying gaps. This again could be carried out by a small group drawn from the managerial cadre and execution/ implementation groups at the field level. All this information would be then looked into; to develop a plan for Social Auditing, including who would be responsible in the department, monitoring and identifying the resources required. This responsibility again could be given to a small group of three individuals.

Stakeholder consultation, involving department functionaries and civil society, would be the forum for sharing the Social Audit plan. This consultation would clarify the issues important for Social Auditing, role of stakeholders, as well as commitments from them. The outcome of the consultation would be fed into the process of detailing out: the indicators to be monitored; which existing records are to be used; and how additional information would be collected. The next key step is to fix responsibilities for various activities. The activities include preparing formats for social account-keeping, compilation of data and reporting the same on a monthly basis (internal use). Managers of the department/programmes can use this information for monitoring as well as providing feedback for improving performance and overcoming bottlenecks.

Ideally, Social Audit should be conducted regularly, and the method should be developed through a participatory relationship between the auditor and the organisations/departments..

The cycle starts with 'deciding to do a Social Audit' and at the end of each year planned targets and actual achievements are to be compared.

6. Success Factors in Social Auditing

- The success of Social Auditing is in knowing which techniques to use and in what sequence. The Social Auditor can choose different methods so as to capture both quantitative and qualitative information from the respondent.
- It is important to ensure the follow up action taken on the Social Audit report and the receptiveness of the departments/organisations to adopt the recommendations in the Social Audit report.
- The social auditors should suggest modalities for improving its performance based on the feedback received from different stakeholders.
- The detailed work plan needs to be identified by the social auditors and the same should be implemented at the earliest.

7. Social Audit Complements Annual Financial Audit

A social audit can complement an organisation's annual financial audit by providing clear and succinct information on performance against social objectives. The results can be fed into the organisation's strategic review and planning processes to improve overall performance and social impact. It has been shown to increase accountability of the organisation to its stakeholders and to enhance democratic practice. In addition to serving as a management tool, social audits can be used for marketing, promotion and advocacy purposes.

8. Issues relating to Social Audit

- To bring about a social change - The problems faced by the social auditor are partly of his own making and partly beyond his control. It should never be forgotten that social welfare programmes are intended to bring about social changes.
- Measurement of Quantities not enough - Mere measurement of inputs or outputs cannot meet the demands of effective social audit.

- A Positive Approach - A social auditor should have a very positive approach. For example, he cannot criticize a nutrition programme on the ground that it does not meet the nutritional standard set by the World Health Organization. Often he may even be unable to justify criticism of non-achievement of targets laid down in the programme.
- A Report all fair - He has to look at the positive social changes brought about and in some cases their costs. When scrutinizing short-falls and non-achievements, he has to take into account the efforts of events beyond the boundary of the programme all of which the designers of the programme may not have been in a position to envisage and allow for the implementers to deal with. This in a nut-shell is the reason why it is difficult to prepare a social audit report which will be fair to the society, the implementers of the programme and to its designers.
- Factors Beyond Control - The social auditor has to face several problems which are beyond his control. Not all social welfare programmes are well designed or based on valid assumptions. Some programmes do not attack the problems at the first level of symptom cause relationship, but at remoter levels and so are destined to achieve only moderate success. Others ignore the need for a package of programmes to simultaneously attack a variety of related unsatisfactory social situations. For instance, a programme for the improvement of rural health must be part of a well designed project containing several individual programmes dealing with the related issues of rural housing, rural water supply, education, nutrition, rural pollution, rural trade and industries for generation of income etc. And when a programme is well designed, it does not make the social auditor's task any easier because, in preparing the social audit report on a programme, he has also to consider how the related programmes are progressing.
- No well conceived Information System - Perhaps the most serious difficulty faced by the social auditor is the absence of a well conceived information system as part and parcel of a social welfare programme.
- Traditional Systems - Government agencies which design programmes often commit the error of relying on traditional government systems of information such as government accounts and government methods of reporting for conveying a picture of how a programme is progressing. This kind of hazy and incomplete system does not help them to take stock, speed up, slow down or apply corrective measures as and when required.

- No Provision for Measurement and Assessment of Social Changes - In any case, the system can give no information on the social changes achieved nor on how other related programmes have affected a programme. Thus a fundamental defect in the design of most social welfare programmes is the fact that they' do not provide for the measurement or assessment of the social changes, that is to say, they do not provide for an internal evaluation machinery, in terms of men and methodology, for evaluation of the impact produced by the programmes. Nowhere else as much as in social audit is the fundamental truth more obvious that where an implementing agency does not itself have the means and methodology to assess performance, no worthwhile audit can be done.
- Problems on a Case to Case basis - Apart from these problems of a general kind, individual programmes pose their own specific problems to the social auditor. To give an example, a programme for immunization of a section of the people against a disease by vaccination may show measurable effect only several years after it is implemented. Likewise, a programme of adult literacy in rural areas cannot be evaluated fairly unless information is available on the migration of educated villagers to urban areas. Almost every social welfare programme will present some such special feature whose import has to be fully grasped by the social auditor.
- No reliable information system - Social audit of public utilities and public undertakings faces its own problems the most important of which is again a reliable information system. Utilities maintain detailed records of what they do but hardly any of how their functioning influences society. They have records of services offered but hardly any of services refused. Even where such records are maintained they do not give a complete picture. For instance, a telephone company may maintain records of how many people applied for a telephone connection and how many applications could not be complied with. But they cannot and do not keep any record of how many people who wished to have a telephone did not even take the trouble of giving an application knowing that they were unlikely to get a quick response.
- Social Accounting - The concept of social accounting hardly exists- even in technologically advanced countries. In the absence of such an accounting system, social audit can become, unless the auditor plans his work with the greatest care a straight forward economy or efficiency audit.

9. Checklist before Designing a Social Audit

1. ***Survey Stakeholders for Feed Back:*** A survey of stakeholders should try to cover the attitudes and behaviour and make sure that adequate number of different stakeholder groups are covered to arrive at a reliable conclusion.

2. ***Check the Media for Information:*** Before setting out, the survey reports that have come out in the media during the recent past pertaining to the area under study, need to be looked into carefully.

3. ***Survey of the Attitudes and Behavior of the Stakeholders:*** A survey of attitudes and behavior of an adequate number of stakeholder groups will be useful in gathering significant and reliable results. Through this survey, different stakeholders are considered and the surveyor can get a perspective of how they perceive various issues.

10. Designing Social Audit

A social audit program is designed keeping in mind the following points

1. The need for social audit for this organization

2. Goal to be achieved from the Social Audit Program

3. For whom is the Social Audit Report being made?

11. Social Accountability Mechanisms and Tools

The key areas where social accountability methods in use are:

1. Preparation, implementation, monitoring & evaluation of programmes/ strategies;
2. Public sector reform and public expenditure management processes;
3. Community-driven development projects; and
4. Sectoral interventions in specific areas (e.g., health, infrastructure, education etc.)

The following is a brief description of few selected social accountability methods that have been used at different stages of public management across the world.

a. Participatory Planning, Policy Formulation & Budgetary Analysis

Participatory planning and policy formulation has become a common trend. Participatory planning is the process by which citizens come together to identify their needs and prioritize them within the resource envelope that can be mobilized through a socially and politically acceptable form of negotiation.

To ensure realism and specificity, planning has to be vis-à-vis an indicative budget. Participatory planning is an element of participatory budgeting.

In India, decentralized planning has been institutionalized in West Bengal and Kerala. Kerala has been way forward in institutionalizing participatory planning; known as people's planning in the local self government institutions. Participatory planning is only a beginning. If properly managed, it can lead to a demand-led improvement of service delivery and to responsive local government.

b. Citizens' Surveys/Citizen Report Cards

Citizens' survey methods are where feedback from individual citizens is aggregated to provide report cards and survey reports on a range of issues. These could pertain to service delivery assessments, opinion polls, awareness exercises etc. While surveys have been used extensively the world over, their use to generate Citizen Report Cards have been made in India, Ukraine, Philippines etc.

c. Participatory Budget Analysis

Participatory Budgeting can be broadly defined as a mechanism or process through which the citizens participate directly in the different phases of the budget formulation, decision making, and monitoring of budget execution. This may involve analyzing the impact and implications of budget allocations, demystifying the technical content of the budget, raising awareness about budget-related issues and undertaking public education campaigns to improve budget literacy.

Participatory budget formulation, though less common, has been used at the local level bodies in Brazil in over 100 municipalities. Due to the nature of citizen participation, this process is effective at the local government level and not at higher levels. When properly managed, participatory budgeting can improve the transparency, efficiency and effectiveness of public budgeting.

d. Citizen's Charters

A charter is an explicit statement of what a public agency is ready to offer as its services, the rights and entitlements of the people with reference to these services and the remedies available to them, should problems and disputes arise in these transactions. Citizen's Charters have been used in various government departments at the Centre and States in India for a longtime with varying degree of success.

e. Community Score Cards

These are used to assess service delivery in a participatory manner at the communitylevel. Typically, the process involves ratings of service delivery by users and self assessments by providers who then participate in an interface meeting to identify and sort issues and differences. Such experiments are been attempted in Malawi and in India (Andhra Pradesh and Maharashtra).

f. Social Audit/Participatory Expenditure Tracking

This involves citizen groups tracking how the government actually spends funds, with the aim of identifying leakages and/or bottlenecks in the flow of financial resources or inputs. Examples include participatory tracking of primary education expenditures in Uganda, Jan Sunwais or participatory audits in Rajasthan and Delhi, People's Estimate in Andhra Pradesh (for monitoring and execution of rural public works), etc. In addition to these methods and tools, many more exist such as people's campaign for electoral reforms, public interest litigations, etc. The Right to Information is a key weapon in the hands of citizens which not only facilitate the application of social accountability tools but also determine the successful institutionalization of accountability mechanisms.

12. ISO 26000:2010 – Guidance on Social Responsibility

ISO 26000:2010 provides guidance to all types of organizations, regardless of their size or location, on:

- concepts, terms and definitions related to social responsibility;
- the background, trends and characteristics of social responsibility;
- principles and practices relating to social responsibility;
- the core subjects and issues of social responsibility;
- integrating, implementing and promoting socially responsible behaviour throughout the organization and, through its policies and practices, within its sphere of influence;
- identifying and engaging with stakeholders; and
- communicating commitments, performance and other information related to social responsibility.

ISO 26000:2010 is intended to assist organizations in contributing to sustainable development. It is intended to encourage them to go beyond legal compliance, recognizing that compliance with law is a fundamental duty of any organization and an essential part of their social responsibility. It is intended to promote common understanding in the field of social responsibility, and to complement other instruments and initiatives for social responsibility, not to replace them.

In applying ISO 26000:2010, it is advisable that an organization take into consideration societal, environmental, legal, cultural, political and organizational diversity, as well as differences in economic conditions, while being consistent with international norms of behaviour.

ISO 26000:2010 is not a management system standard. It is not intended or appropriate for certification purposes or regulatory or contractual use. Any offer to certify, or claims to be certified, to ISO 26000 would be a misrepresentation of the intent and purpose and a misuse of ISO 26000:2010. As ISO 26000:2010 does not contain requirements, any such certification would not be a demonstration of conformity with ISO 26000:2010.

ISO 26000:2010 is intended to provide organizations with guidance concerning social responsibility and can be used as part of public policy activities. However, for the purposes of the Marrakech Agreement establishing the World Trade Organization (WTO), it is not intended to be interpreted as an “international standard”, “guideline” or “recommendation”, nor is it intended to provide a basis for any presumption or finding that a measure is consistent with WTO obligations. Further, it is not intended to provide a basis for legal actions, complaints, defences or other claims in any international, domestic or other proceeding, nor is it intended to be cited as evidence of the evolution of customary international law.

ISO 26000:2010 is not intended to prevent the development of national standards that are more specific, more demanding, or of a different type.

13. Corporate Social Responsibility

Corporate Social Responsibility is a form of corporate self-regulation integrated into a business model. CSR policy functions as a built-in, self-regulating mechanism whereby business monitors and ensures its active compliance with the spirit of the law, ethical standards, and international norms. The term "corporate social responsibility" came in to common use in the early 1970s, after many multinational corporations formed. The term stakeholder, meaning those on whom an organization's activities have an impact, was used to describe corporate owners beyond shareholders

CSR is titled to aid an organization's mission as well as a guide to what the company stands for and will uphold to its consumers. Development business ethics is one of the forms of applied ethics that examines ethical principles and moral or ethical problems that can arise in a business environment. ISO 26000 is the recognized international standard for CSR (currently a Draft International Standard). The UN has developed the Principles for Responsible Investment as guidelines for investing entities.

14. Social Audit in India

Social Audits are mandatory as per the 73rd Constitutional Amendment in 1993, through which the Village communities are empowered to conduct social audit of all development work in their respective villages and the concerned authorities are duty bound to facilitate them

- Social Audit is a process in which, details of the resource, both financial and non-financial, used by public agencies for development initiatives are shared with the people, often through a public platform. Social Audits allow people to enforce accountability and transparency, providing the ultimate users an opportunity to scrutinize development initiatives*
- Social audit as a term was used as far back as the 1950s. There has been a flurry of activity and interest in the last seven to eight years in India and neighboring countries. Voluntary development organizations are also actively concerned***
- The key difference between development and social audit is that a social audit focuses on the neglected issue of social impacts, while a development audit has a broader focus including environment and economic issues, such as the efficiency of a project or programme
- Social audit can also be used for auditing the performance of all three PRI tiers with a social audit committee at each level. These committees should not be permanent, but can be set up depending on the nature of programmes/schemes to be audited
- Article 17 (2) of the NREGA says "the gram sabha shall conduct regular social audits of all the projects under the Scheme taken up within the Gram Panchayat". Article 17 (3) says "the Gram Panchayat shall make available all relevant documents including the muster rolls, bills, vouchers, measurement books, copies of sanction orders and other connected books of account and papers to the gram sabha for the purpose of conducting the social audit."

Social audit rules under National Rural Employment Guaranty Scheme (NREGS):

- The rules lay out procedures under the three main stages of a social audit: preparatory phase, social audit forum, and post-social audit phase.
- The social audit forum (meeting of the gram sabha) must be conducted every six months, be presided over by a person selected by the forum, and must be widely publicised beforehand.

- The 'action taken report' relating to the previous social audit must be read out, attendance of all concerned officials is compulsory, and minutes of the meeting must be recorded by the secretary in the prescribed format. The audit is open to any outside individual, group, or NGO.
- The post-audit phase requires all complaints of non-performance to be looked into, and anyone involved in deviation of funds to be held accountable and the loss made good.
- The rules clearly state who is accountable for what at each stage of programme implementation. It also says that the central government will meet the costs of establishing and running a social audit cell at the state level.

According to the Vision Foundation's (2005) Social Audit-Gram Sabha and Panchayati Raj-document, submitted to the Planning Commission, GoI, http://planningcommission.nic.in/reports/sereport/ser/stdy_sagspr.pdf:

- Social Audit is a process in which, details of the resource, both financial and non-financial, used by public agencies for development initiatives are shared with the people, often through a public platform. Social Audits allow people to enforce accountability and transparency, providing the ultimate users an opportunity to scrutinize development initiatives."
- In the Panchayati Raj set up, the Gram Sabha, the general assembly of villagers, has a key role for effective functioning of Panchayats. In the Gram Sabha meeting, the rural poor, the women and the marginalised people would now get an opportunity to join in decision making on matters affecting their lives.
- Active functioning of the Gram Sabha would ensure a participatory democracy with transparency, accountability and achievement. Gram Sabha has been given 'watchdog' powers and responsibilities by the Panchayati Raj Acts in most States to supervise and monitor the functioning of panchayat elected representatives and government functionaries, and examine the annual statement of accounts and audit reports.
- These are implied powers indirectly empowering Gram Sabhas to carry out social audits in addition to other functions. Members of the Gram Sabha and the village panchayat, intermediate panchayat and district panchayat through their representatives, can raise issues of social concern and public interest and demand an explanation.

- In order to supplement the Panchayati Raj Act, the Government of India, in 1996, passed another Act known as Panchayats (Extension to the Scheduled Areas) Act, which extended the provisions of the Constitution (73 Amendment) Act of 1992 to the tribal areas of Andhra Pradesh, Bihar, Gujarat, Himachal Pradesh, Maharashtra, Madhya Pradesh, Orissa and Rajasthan. This came into force on 24 December 1996.
- The social audits are expected to contribute to the process of empowerment of the beneficiaries and generate demand for the effective delivery of programmes. The instructions require that special Gram Sabhas be arranged to conduct Social Audits in every ward and that Social Audits of all ongoing development works be included as an item of discussion in every Gram Sabha meeting.
- The provisions of Panchayats (extension to scheduled areas) Act 1996 lays down that the completion certificate for all villages development works can only be accorded by the Gram Sabha.
- Rajasthan (India) Panchayati Raj (Amendment) Act 2000 vested on the Ward Sabha on "getting information on the detailed estimates of works prepared to be taken in the area of the Ward Sabha, exercising "Social Audit" in all works implemented in the area of Ward Sabha and awarding utilization and completion certificate for such work
- In the state of Madhya Pradesh (India) the process of Social Audit has been specified in the order No. 18069/22/JRY/vi - 7/96 dev. October 30th 1996.
- In the state of Orissa the Social Audit in rural development works has been mandatory with the issuance of Govt. order in the month of September 2002.

According to Social Audit and its Relevance to Audit of Public Utilities by M Parthasarathy,http://www.asosai.org/journal1988/social_audit_and_its_relevance.htm:

- Social audit of public utilities or public undertakings would be greatly facilitated if the undertaking prepared a social accounting document. Several models of social accounting and reporting have been tried out in a number of countries but efforts at standardising the models have not borne fruit. Even simple reporting systems devised will enable the social auditor of public utilities or undertakings to draw conclusions about the social benefits and social detriments arising from the operation of a public utility over and beyond the quality of service rendered by it for which it is set up. A reading of such reports over a time period of few years can provide the basis for judging whether the net social benefit is growing in acceptable proportion to the encroachments made by the utility on the resources of the society

- Perhaps the most serious difficulty faced by the social auditor is the absence of a well-conceived information system as part and parcel of a social welfare programme. Government agencies which design programmes often commit the error of relying on traditional government systems of information such as government accounts and government methods of reporting for conveying a picture of how a programme is progressing. This kind of hazy and incomplete system does not help them to take stock, speed up, slow down or apply corrective measures as and when required. In any case, the system can give no information on the social changes achieved nor on how other related programmes have affected a programme.

According to Social Audit by Amitabh Mukhopadhyay, http://www.india-seminar.com/2005/551/551%20amitabh%20mukhopadhyay.htm

- Constitutional amendments in 1992-93 for local self government which introduced provisions for accounts to be placed before the gram sabha and municipal wards are a revealing pointer to the need for accountability, not to a hierarchy of officialdom or representatives of the people but increasingly to people themselves, since they are the only stakeholders. That is the writing on the wall.
- Social audit assumes even greater importance in the context of democratic decentralization since 1992-93. Structures for accountability are the weakest in panchayats and municipal bodies who are implementing anti-poverty programmes and providing basic social services. Half-hearted devolution of powers by most state governments continues to stymie their effectiveness. Planning by district planning committees as envisaged in the constitutional amendments has hardly been operationalized. At the sub-district level of taluk and gram panchayats, poor book-keeping is coupled with audit certification by Examiners, Local Funds of the state governments, which is by and large no more than an exercise in stamping and signing inadequately authenticated accounts. Hearing the complaints of residents before certifying accounts, as is the audit convention for local authorities in Europe, is nowhere even on the agenda in India. The sheer spread and numbers of the local bodies, to be considered against the availability of ethical auditors, are daunting.

- At the behest of the Union Finance Commission, the CAG has recently undertaken an exercise in providing technical guidance and supervision to Examiners, Local Funds, which needs to be supported by a vigorous movement for social audit. It must be remembered that, as against the concerns of departmental auditors for classification of transactions under relevant schemes and programmes, citizens are interested in the veracity of the details in BPL surveys, vouchers and muster rolls. The actual construction of permanent assets along proper specifications also matters to them.

15. Public Accountability in Other Countries

In November 2006, the International Budget Project (IBP), the United Nations Department of Economic and Social Affairs (UN-DESA), and the Eastern Regional Organization for Public Administration co-hosted a two-day conference in Manila entitled "Dialogue on Civil Society Engagement in Public Accountability." During the conference, possibly the first of its kind, civil society organizations and public audit institutions from India, South Africa, the Philippines, Argentina, South Korea, and Mexico discussed opportunities for expanding collaboration.

The conference sought to familiarize representatives of civil society groups and audit officials with each other, enable participants to share experiences regarding the use of public audit processes, and foster dialogue between civil society groups and public auditors within the same country regarding ways in which they could strengthen oversight over public resources.

The IBP and UN-DESA, which organized the conference, selected these six countries because of their potential for collaboration between civil society and audit institutions. For example:

- In **India**, the Mazdoor Kisan Shakti Sangathan (MKSS), a peasants' and workers' union, uses public hearings to conduct social audits of local government expenditures in village communities. (In a social audit, program beneficiaries evaluate the performance of the agency and conduct oversight of agency expenditures.) During these social audits, communities check accounting records and other records on public-works programs in their area and identify instances of fraud, including falsified bills and labor rolls. MKSS' social audit methods are now being used all over India by citizen groups to monitor a new government program under which rural households are eligible to receive minimum-wage employment for 100 days in a year.

- In **South Africa**, the Public Service Accountability Monitor (PSAM), a research and advocacy organization, works closely with the legislature to track government responses to instances of financial misconduct and corruption identified in the auditor general's reports. PSAM has highlighted the large number of audit disclaimers issued by a provincial audit agency — which was unable to obtain financial information during the conduct of its audit — and organized a public campaign that led to stronger financial management practices in provincial government agencies.
- The **Philippines**, the Commission on Audit (the national supreme audit institution) and the NGO Concerned Citizens of Abra for Good Government (CCAGG) jointly conducted a participatory audit. CCAGG, which specializes in monitoring infrastructure projects, uses local volunteer monitors to verify that road construction projects are executed as per contract norms. (See CCAGG article below.)
- Also in the Philippines, the NGO Procurement Watch, Inc. specializes in building systems of transparency and accountability into government contracting and procurement practices. PWI's most recent initiative is to participate with the Commission on Audit in a pilot test of a new tool to measure corruption and inefficiency in public procurement. (See PWI article below.)
- In **Mexico**, Fundar, a research and advocacy organization, identified large-scale corruption in a government contract awarded to a private agency under an HIV/AIDS prevention program by obtaining hundreds of pages of government accounting records using the national freedom of information law. (An official investigation by the national supreme audit institution corroborated Fundar's findings.) Subsequently, pressure from the Fundar-led campaign led the government to recover the misappropriated funds and change its policies governing the management of discretionary funds, including funds for the HIV/AIDS prevention program.
- In **South Korea**, Concerned Citizens for Economic Justice (CCEJ), an NGO working on economic rights issues, routinely uses the country's national citizen audit request system to request government audits of public projects that waste resources or are plagued by corruption. CCEJ presented three cases of corruption in public projects that were corroborated by subsequent government audits. In one case, the government changed its procurement policies in part as a result of a

CCEJ campaign to limit the issuance of no-bid contracts. (See CCEJ article below.)

- In **Argentina**, La Asociación Civil por la Igualdad y la Justicia (ACIJ), a human rights organization, filed suit to obtain the minutes of meetings by the congressional commission responsible for reviewing public audits and then used these records to highlight the commission's failure to act in response to audit recommendations.

16. Writing a Social Audit Report

The social audit report is written for the board of directors, officers and staff, and indirectly for the members of the department. These individuals may not have much importance attached with specific methodological and statistical details, but are surely more concerned with learning quickly the major findings, conclusions and recommendations

The report, therefore, should be one that encourages rapid reading, quick comprehension of major findings and prompt understanding of the implications of these findings and recommendations. However, it should also take special care for the accuracy of the data.

The report should consists of the following characteristics

17. Characteristics of a Social Audit Report

1. **Readability -** Readability means the writing conformation is at the level that is appropriate to the recipients' reading abilities.
2. **Comprehensibility -** Comprehensibility means clearness, distinctness and explicitness
3. **Tone –** This refers to the way in which the prose sounds

18. Format of the Report (Eg.,Cooperatives)

The social audit report follows a well-delineated format, thus:

I. Social Audit

1. Why conduct a Social Audit?
2. What is a Social Audit?
3. Value of Social Audit
4. The Social Audit field

II. Executive summary

	Significant Findings	Key Recommendations
• Voluntary and Open Membership		
• Democratic Member Control		
• Member Economic Participation		
• Autonomy and Independence		
• Education, Training and Information		
• Cooperation among Cooperatives		
• Concern for Community		
• Co-op's Staff		

III. The Auditor's Prefatory Statements and Certification

1. The Report
2. Basis of the Report
3. Limitations
4. Comments on the Process
5. Auditor's Certification
6. Composition of the Social Audit team

IV. Summary of Findings

A. Voluntary and Open Membership

1. Database of members
   a. age
   b. civil status
   c. sex
   d. religion
   e. education
2. Percentage increase in regular membership

3. Market Penetration
   a. Members' Means of livelihood Profile
   b. Chapters (in relation to membership expansion)
   c. Branches (in relation to membership expansion)
4. Obstacles to membership
5. Convenience in refund of capital for withdrawing members

B. Democratic Member Control

1. Number of general assemblies
2. Average number of voting members in GA
3. Percentage of MIGS to total membership
4. Criteria in determining MIGS
5. Members' perception: Importance of General Assembly
6. Members' perception: Members' participation in the affairs of the co-op
7. Number of BOD meetings
8. Compliance to the provision on the terms of office of board of directors and committee members
9. Number of committee meetings
10. Integrity, character and credibility of officers
11. Members' perception: Performance, Participation and Conduct of Officers
12. Presence of core management team (manager, cashier, bookkeeper)
13. Members' perception: Deportment of staff
14. Members' perception: On staff's performance
15. Policies and procedures
16. Members' perception: Efficiency in service delivery
17. Development plans
18. Institutional mechanism through which the board and management of the co-op consult the members prior to any decision
19. Monitoring mechanisms to gather feedback
20. Members' perception on the receptiveness of the coop of their ideas, suggestions and complaints

21. Members' satisfaction that their ideas, opinions and grievance are heard
22. Members' perception: Branching
23. Members' perception: Chapter
24. Board members, male female ratio
25. Committees, male female ratio
26. Explicit provisions in its vision-mission-goals, in its by-laws and or other policies and procedures regarding gender-fair promotions

C. Member Economic Participation

1. Number of members contributing to share capital & savings deposits
2. Membership patronage to cooperative products and services
3. Paid-up capital and savings mobilization
4. The members borrowing pattern before becoming members
5. Members' perception: Cost of services
6. Members' perception: Interest rates on deposits
7. Members' perception: Availability of services
8. Allocation of patronage refund and interest on capital
9. Presence of institutional providential services to members
10. Presence of specific programs and services for senior members

D. Autonomy and Independence

1. Type of capital-up build-up mechanisms being implemented or adopted
2. Type of savings mobilization schemes being implemented
3. Number of income generating undertaking of the coop
4. Percentage increase (decrease) in working capital
5. Profitability ratio (net income over gross income)
6. Current ratio
7. Compliance with government rules and regulations

E. Education, Training and Information

1. Education services/Programs for the last 5 years
2. Members' perception: The educative purpose of ownership meetings
3. Economic capability building program
4. Culture building programs

5. Presence of gender related training for staff officers or general membership
6. Presence of education programs for the successor generation
7. Presence of a youth development program
8. Dissemination of important co-op information on operation
9. Dissemination of important cooperative information on the organization
10. Media of communication to disseminate information
11. Designation of point person in charge of information and communication
12. Capability enhancement program of board of directors, committees and management staff
13. Members' perception: Leadership development at the chapters

F. Cooperation among Cooperatives

1. Economic participation in other Co-ops
2. Active support to federation/apex organization
3. Partnership, cooperation, and/or alliances (business or otherwise) with other co-operatives and civil society formations
4. Participation in the cooperative federation/union activities/programs
5. Patronage of federation/apex organizations' services
6. Number of board members/officers in co-operative secondary organizations and time spent

G. Concern for Community

1. Environment protection programs and activities
2. Community infrastructure projects facilitation
3. Advocacy and education on social development
4. Co-op's marketing practices
5. Co-op practices in its dealings with its clients
6. Members' perception: Work ethics of staff
7. Cultural, sports and value enhancement program
8. Participation in local governance programs
9. Presence of institutional gender-specific programs that were implemented in the last two years

V. The Co-op's Staff

1. Staffs' profile
2. Commitment to VMG
3. Enjoyment and satisfaction
4. Staffs' feeling of being part of a team
5. Agreeableness of work environment to health
6. Fairness and objectivity of performance rating
7. Reasonability of remuneration and other benefits
8. Long-term future with the co-op
9. Others

VI. The Auditor's Analysis and Interpretations, and Conclusions

- **a. Identifying Weaknesses, Identifying Strengths**
- **b. Opportunities that are Open, Threats that are Confronting the Co-op**
- **c. Conclusions**

VII. Recommendations

VIII. Co-op's Response: Continuous Improvement of its Social Performance

19. Contents of the Report

- **The Need for Social Audit**
  - This section talks about the need for social audit for a particular organization and its benefits
- **Executive Summary**
  - This summary consists of two parts,
    - A miniature report
    - A paragraph on the significant findings and recommendations
- **The Auditor's Prefatory Statement**
  - This section narrates the process of the whole social audit engagement from the formulation of the various areas of decisions and actions, to the fieldwork and finally to the validation conference. This also contains comments on the side

issues and working relationships between the auditor and the client cooperative, and specifies the limitations of the study

- **The Auditors Certifications**
  - This section contains the certification of the auditor as to the reliability and accuracy of the social audit report, as well as to the involvement of the general membership in the process.
- **Summary of Findings**
  - The longest section in the Social Audit Report this section talks about the entire procedure of social audit. This section should be in plain prose presented in an organized manner
  - Graphs, tables, quantitative data should be presented wherever it is essential
- **Auditor's Analysis, Interpretation and Conclusions (SWOT Analysis)**
  - This section consists of three sections
    - Strengths and Weakness Analysis
    - Opportunities and Threats
    - Conclusions
- **Recommendations –** The auditors recommendation could range on a variety of issues
  - Maintenance of Strengths
  - Identification of Weakness
  - Future Growth
  - New Threats
  - Externally Generated Opportunities
- **Continuos Improvement –** This section elucidates the future direction in which the organization should proceed

20. Points to Note while writing a Social Audit Report

- Before writing a report on Social Audit the following points should be considered
  - The purpose of this report
  - The temperament of the board, officers and staff

    - Level of familiarity of the subject
    - Limitations based on which the report is prepared (time constraint and scope of study)
    - Utility value of the report
- Presentation of Statistics in a Social Audit Report **–** Statistics can be presented in four forms namely
    - Text form
    - Semi Tabular Form
    - Tabular Form
    - Graphical Form

A table is defined as a systematic arrangement of related data in which classes of numerical facts are given each a row and their subclasses are given each a column in order to present the relationships of the sets or numerical facts or data in a definite, compact, and understandable form or forms

Professional Opportunities in Social Audit

1. Assessing the Social Performance of Corporate Enterprise
2. Assessing the Goal Oriented Performance of Government Utility Departments
3. Assessing the Social Performance of Government Sector Undertakings
4. Assessing the Social Performance of Government Departments
5. Assessing the Social Performance of Gram Panchayat Offices
6. Social Audit of Public Libraries
7. Social Audit of Employment Exchange Offices
8. Social Audit of Urban Local Bodies

VIII. Environmental Audit

1. Environmental Audit

Environmental audits are intended to quantify environmental performance and environmental position. In this way they perform an analogous (similar) function to financial audits. An environmental audit report ideally contains a statement of environmental performance and environmental position, and may also aim to define what needs to be done to sustain or improve on indicators of such performance and position.

Environmental auditors can get certified through written exam and acceptance of the Environmental Auditor Association code of ethics. Depending on the nature of the audit, there are several different designations to choose from.

2. Enactments Pertaining to Environmental Protection in India

Environmental legislations in India are framed both at the Central and State level by two agencies namely the

- Ministry and
- The Regulatory Agencies

While the ministries are part of the central and state governments, the regulatory agencies are usually autonomous bodies established by the respective environmental legislations like the Central Pollution Control Board and the State Pollution Control Board at the national and state levels respectively

Important Enactments relating to Environmental Protection are as follows

1. Water (Prevention and Control of Pollution) Act 1974.
2. The Air (Prevention and Control of Pollution) Act 1981.
3. Environmental (Protection) Act 1986
4. Hazardous Wastes (Management & Handling) rules 1989.

3. Planning an Environmental Audit

Any organization/premises that wishes to conduct an environmental audit must have a clear idea of the objectives of the exercise and the steps required to achieve it. Before commencing an environmental audit, the following requirements must be fulfilled:

1. Commitment

- Obtain commitment at the Directorate level
- Communicate commitment to personnel at all levels

2. Define Audit Scope and Audit Site

To include:

- Audit site and boundary
- Audit objective(s)

- Areas of audit

Audit objectives typically entail:

- Verification of legislative and regulatory compliance
- Assessment of internal policy and procedural conformance
- Establishment of current practice status
- Identification of improvement opportunities

Areas of audit normally encompass:

- Material management, savings and alternatives
- Energy management and savings
- Water management and economy of use
- Waste generation, management and disposal
- Noise reduction, evaluation and control (internal and external)
- Air emissions and indoor air quality
- Environmental emergency prevention and preparedness
- Transportation and travelling practices
- Staff awareness, participation and training in environmental issues
- Environmental information publicity
- Public enquiry and complaints response
- Environmental management system set up, suitability and performance

4. Conducting Environmental Audit

An environmental audit is typically undertaken in three phases:

- Pre-audit
- On-site audit
- Post-audit

Each of these phases comprises a number of clearly defined Objectives, with each objective to be achieved through specific Actions, and these actions yielding results in the form of Outputs at the end of each phase.

Pre Audit Activities

Pre audit activities aim to develop an audit plan for the on-site activities and also to make necessary preparation and arrangements for the on-site audit.

1. Develop an Audit Plan

The Audit Plan should address the following questions

- Where is the audit site with boundary overview
- What is the scope & objectives
- How is the site personnel interview, site inspection, audit protocols; site logistics and administrative arrangement made?
- Who is the audit team
- Who does the site facilitation arrangement
- What is the audit schedule and milestones

The Audit Team should subsequently:

- Seek agreement from AMC on audit plan
- Establish the reporting structure

2. Prepare Pre-Audit Questionnaire

A questionnaire and document checklists is required to be prepared on the following:

- The "hard" issues:
  - Overall environmental management
  - Procurement policy
  - Energy management
  - Materials management
  - Water and wastewater management
  - Waste management
  - Noise monitoring and control
  - Air quality monitoring and control
  - Emergency response procedures
- The "soft" issues:
  - Transportation and travelling
  - Staff awareness and training
  - Publicity of environmental information
  - Response to public enquiries and complaints

- The questionnaire and checklists are to be forwarded to the relevant site personnel for completion.

3. Review Background Information

The Audit Team should gain familiarity with audit site through review of:

- Site layout plan(s)
- Site history, use and activities
- Blue prints/as built drawings
- Organisational structure at audit site(s)Internal environmental policies, procedures and guidelines

4. Review Operational Information

Understand and appreciate the site activities and operational practices on site through review of:

- Operational activities and process descriptions
- Management system policies, procedures and program documentation
- Relevant records (compliance, monitoring, training, maintenance, calibration etc.)
- Other relevant information pertaining to environmental management practices

5. Conduct Initial Site Visit

Make necessary arrangements with the site facilitator(s) for an initial visit during normal operation of audit site to:

- Meet with officer-in-charge to explain purpose of audit
- Assess whether background information gathered is up to date and accurate
- Follow-up on the list of preliminary audit impressions
- Identify and request additional site information as necessary
- Confirm thoroughness of audit scope
- Establish adequacy of resources for audit

6. Develop on-Site Questionnaire and Audit Protocols

Developing a series of step-by-step questions and evaluation criteria to assess:

- Compliance with pertinent legislative and regulatory requirements

- Conformance with internal environmental policies, procedures and guidelines
- Status of current environmental practices
- Staff awareness of internal environmental policies, procedures and guidelines

7. Review Audit Plan and Arrange Logistics

Review of documents and arrangements should be updated or revised to reflect current knowledge and conditions.

Key points to review include:

- Audit scope
- Audit schedule
- Audit protocols
- Allocated resources

The preparatory activities during this phase will yield the following outcome

- Audit Plan
- Package of background information
- Completed Operational Information Questionnaire and Audit Checklists
- On-site Questionnaire and Audit Protocols

On Site Audit Activities

The on-site audit objectives should reflect those of the environmental audit, which are:

- Verification of legislative and regulatory compliance
- Assessment of internal policy and procedural conformance
- Establishment of current practice status
- Identification of improvement opportunities

1. Open Meeting

Conduct on-site audit Opening Meeting with Office manager and site personnel to:

- Introduce audit team members
- Present audit scope and objectives
- Outline the audit approach and methodology

- Address questions or concerns of site personnel
- Rally staff support and assistance

2. Document Review

Audit Team member to undertake a review of relevant document such as:

- Management policy
- Management system documentation
- Operational procedures
- Records (utility, inventory, monitoring, calibration, transportation, training etc.)
- Previous audit reports
- Green management team meeting minutes
- Green suggestions

In particular, to evaluate whether the records are:

- Current
- Properly completed
- Signed and dated
- Consistent
- Meet relevant requirements

Post Audit Activities

Objectives

- To produce an Audit Report with audit findings and recommendations
- To contribute towards formulation of an Action Plan for continual performance improvement

Collate Information and Follow up on the Outstanding Issues

Information to be organised should include:

- Completed pre-audit questionnaire, operational document checklists
- Completed on-site survey questionnaires, on-site audit protocols
- All relevant correspondence, memoranda, reports, diagrams and drawings
- Copies of records, photographs, and other information collected during the site visit
- Detailed inspection and interview notes and summaries

5. Central Pollution Control Board

The Central Pollution Control Board (CPCB), statutory organisation, was constituted in September, 1974 under the Water (Prevention and Control of Pollution) Act, 1974. Further, CPCB was entrusted with the powers and functions under the Air (Prevention and Control of Pollution) Act, 1981.

It serves as a field formation and also provides technical services to the Ministry of Environment and Forests of the provisions of the Environment (Protection) Act, 1986. Principal functions of the CPCB, as spelt out in the Water (Prevention and Control of Pollution) Act, 1974, and the Air (Prevention and Control of Pollution) Act, 1981, (i) to promote cleanliness of streams and wells in different areas of the States by prevention, control and abatement of water pollution, and (ii) to improve the quality of air and to prevent, control or abate air pollution in the country.

Air Quality Monitoring is an important part of the air quality management. The National Air Monitoring Programme (NAMP) has been established with objectives to determine the present air quality status and trends and to control and regulate pollution from industries and other source to meet the air quality standards. It also provides background air quality data needed for industrial siting and towns planning.

Besides this, CPCB has an automatic monitoring station at ITO Intersection in New Delhi. At this station Resirable Suspended Particulate Matter (RSPM), Carbon Monoxide (CO), Ozone (O_3), Sulphur Dioxide (SO_2), Nitrogen Dioxide (NO_2) and Suspended Particulate Matter (SPM) are being monitored regularly. This information on Air Quality at ITO is updated every week.

Fresh water is a finite resource essential for use in agriculture, industry, propagation of wildlife & fisheries and for human existence. India is a riverine country. It has 14 major rivers, 44 medium rivers and 55 minor rivers besides numerous lakes, ponds and wells which are used as primary source of drinking water even without treatment. Most of the rivers being fed by monsoon rains, which is limited to only three months of the year, run dry throughout the rest of the year often carrying wastewater discharges from industries or cities/towns endangering the quality of our scarce water resources. The parliament of India in its wisdom enacted the Water (Prevention and Control of Pollution) Act, 1974 with a view to maintaining and restoring wholesomeness of our water bodies. One of the mandates of CPCB is to collect, collate and disseminate technical and statistical data relating to water pollution. Hence, Water Quality Monitoring (WQM) and Surveillance are of utmost importance

6. Guidelines for Environmental Audit

Environmental Audit is an exercise of self-assessment to minimise the generation of wastes and pollution potential.

A gazette notification on environmental audit has been issued by the Ministry of Environment and Forests on March 13, 1992 (amended vide notification GSR 386 (E) dated April 22, 1993). This notification applies to every person carrying on an industry, operation or process requiring consent to operate under Section 25 of the Water (Prevention and Control of Pollution) Act, 1974 (6 of 1974) or under section 21 of the Air (Prevention and Control of Pollution) Act, 1981 (14 of 1981), or both, or authorisation under the Hazardous Waste (Management and Handling) Rules, 1989, issued under the Environment (Protection) Act, 1986 (29 of 1986). The notification requires that an Environmental Statement for the financial year ending the 31st March be submitted to the concerned State Pollution Control Board, on or before the 30th September of the same year.

To assist the industry in carrying out environmental audit, the Central Pollution Control Board has conducted some case studies. The publication on the "Guidelines for Environmental Audit" deals with the pesticide industry.

7. Accountant's Role in Environmental Audit

Industry accountants must ensure that their firms are in compliance with accounting standards, including those pertaining to environmental issues. Several rules governing environmental disclosures have been developed in recent years.

8. Environmental Audit Report

The Environmental Audit Report or EA Report is a written record of the Environmental

Audit Process. It describes the project or process being audited, lists the environmental effects associated with that project or process, details the audit procedures that were followed and identifies the relevant environmental legislation and standards that apply.

The role of the Environmental Audit Report is:

- To provide an objective analysis of the environmental impacts arising from a project or process.

- To provide the information required to draw up a Comprehensive Mitigation Plan in the event of there being any significant negative impacts on the environment.
- Preparing an EA Report is a skilled task and it is unlikely that a project operator will be able to prepare such a report to the standards required by the Swaziland Environment Authority without professional consultancy advice.

Form and Content of Environmental Audit Report

Form of the EA Report

The EA Report needs to communicate the relevant information clearly and concisely and should therefore:

- Be presented to make information accessible to the non-specialist, avoiding technical terminology where possible.
- Have information presented in summary tables and use good quality maps, charts, diagrams and other visual aids wherever possible.
- Be clearly laid out with a clear table of contents, to allow the reader to find and assimilate information easily and quickly.
- Present information without bias and discuss issues with the emphasis appropriate to their importance as in the overall context of the Environmental Audit.

Content of the Environmental Audit Report

The **EA Report** should contain the following information:

1. Introduction

The objectives and scope of the **Environmental Audit**.

2. Description of the Development or Activity Under Audit

The size and nature of the development or activity, a description of the relevant management structures and workforce, a summary of all inputs and outputs, ancillary operations such as transport and services, storage and processing operations.

3. Description of the Environment

A brief description of the surrounding environment including the natural and built environment, local ecology and socio-economic or cultural factors that may have a bearing on the audit.

4. Description of Environmental Effects

The term *Effect* is usually substituted in this context for the term *Impact* to reflect the fact that an **Environmental Audit** is concerned with the effect of inefficient resource use and processing as well environmental impacts arising from wastes and emissions. Environmental effects related to the transport, handling, processing, storage and eventual disposal route to the environment of all relevant inputs and outputs should be presented systematically in a clear and appropriate manner.

They should include:

- The environmental effects observed during the course of the audit.
- The good and bad management practices that were observed during the course of the audit, including the effectiveness of existing environmental mitigation measures.

5. Conduct of the Audit

Those interviewed during the audit, the timing and audit methodologies used should be presented.

6. Evaluation of Environmental Effects

The relevant environmental legislation and standards that apply must be defined. These should be cross referenced to the environmental effects identified in **4. Description of Environmental Effects**. The environmental effects must be systematically evaluated and ranked in terms of their significance and the assessments of significance justified.

7. Recommendations

The EA Report must make recommendations to address any significant negative environmental effects and, importantly, allocate and justify priorities for action.

Recommendations should include the control and reduction of emissions by improved efficiency, management and technical control measures. The emphasis should be on incentive and removing the source of a problem rather than the use of command and control or "end of pipe" technology.

The **Comprehensive Mitigation Plan**, or **CMP**, is an integral part of EA report to which it refers. It is an important document as it is the CMP which presents how the recommendations made in the EA Report are going to be implemented.

IX. Management Audit

Management Audit is the systematic recognition, analysis and assessment of competencies and the actual behaviour of both individual executives as well as complete executive teams particularly with regard to the business' strategic requirements. The basis of Management Audit is structured interviews and reference checks conducted by external experts to be documented in expert opinions.vManagement Audits focus on personal attributes and business skills.

Personal attributes can be subdivided into:

- Ethical values and attitudes
- Intellectual Capability
- Charisma

Business skills can be subdivided into:

- Professional and methodical competencies
- Leadership behaviour
- Entrepreneurship

As psychological tests cannot adequately cope with above mentioned criteria (issues) the Management Audit should be conducted by experienced and well-trained interviewers. It is the objective of the process not to assess the individual manager in isolation but in context to their competitors and comparable roles outside the company. This benchmark information is most valuable and delivers conclusions as to the effectiveness of the management team.

Management Function

Management Function can be classified as follows:

- Business strategy process
- Human resources functions
- Marketing strategy
- Production process

Human Resource Functions

- The Human resource audit ensures that the organization is aware of the existing laws and rules and whether it is implementing them effectively.
- This creates an atmosphere of transparency and goes a long way in avoiding legal confrontation later.

- Human Resource Management (HRM) is the function within an organization that focuses on recruitment of, management of, and providing direction for the people who work in the organization. The Human resource audit ensures that the following:
  - organization is aware of the existing laws and rules and whether it is implementing them effectively so that legal confrontation is avoided later.
  - It helps build trust in the minds of the employees who are confident that things pertaining to their wellbeing are being taken care of
  - It also makes the HR employees familiar with the current laws.
  - It adds credibility to the company in the eyes of the investors, who may look favorably.
  - Laws such as those pertaining to discrimination, sexual harassment, overtime etc should be particularly looked into.
  - Even seemingly minor things such as the employment application should be studied if it solicits inappropriate information.

ANNEXURES

I. National Ambient Air Quality Standards

Pollutants	**Time-weighted average**	**Concentration in ambient air**			**Method of measurement**
		Industrial Areas	**Residential, Rural & other Areas**	**Sensitive Areas**	
Sulphur Dioxide (SO_2)	Annual Average*	80 µg/m^3	60 µg/m^{3p}	15 µg/m^3	- Improved West and Geake Method - Ultraviolet Fluorescence
	24 hours**	120 µg/m^3	80 µg/m^3	30 µg/m^3	
Oxides of Nitrogen as (NO_2)	Annual Average*	80 µg/m^3	60 µg/m^3	15 µg/m^3	- Jacob & Hochheiser Modified (Na-Arsenite) Method
	24 hours**	120 µg/m^3	80 µg/m^3	30 µg/m^3	- Gas Phase Chemiluminescence
Suspended Particulate Matter (SPM)	Annual Average*	360 µg/m^3	140 µg/m^3	70 µg/m^3	- High Volume Sampling, (Average flow rate not less than 1.1 m3/minute).
	24 hours**	500 µg/m^3	200 µg/m^3	100 µg/m^3	
Respirable Particulate Matter (RPM) (size less than 10	Annual Average*	120 µg/m^3	60 µg/m^3	50 µg/m^3	- Respirable particulate matter sampler
	24 hours**	150 µg/m^3	100 µg/m^3	75 µg/m^3	

microns)					
Lead (Pb)	Annual Average*	1.0 µg/m^3	0.75 µg/m^3	0.50 µg/m^3	- ASS Method after sampling using EPM 2000 or equivalent Filter paper
	24 hours**	1.5 µg/m^3	1.00 µg/m^3	0.75 µg/m^3	.
Ammonia1	Annual Average*	0.1 mg/ m^3	0.1 mg/ m^3	0.1 mg/m^3	.
	24 hours**	0.4 mg/ m^3	0.4 mg/m^3	0.4 mg/m^3	.
Carbon Monoxide (CO)	8 hours**	5.0 mg/m^3	2.0 mg/m^3	1.0 mg/ m^3	- Non Dispersive Infra Red (NDIR)
	1 hour	10.0 mg/m^3	4.0 mg/m^3	2.0 mg/m^3	Spectroscopy
*	Annual Arithmetic mean of minimum 104 measurements in a year taken twice a week 24 hourly at uniform interval.				
**	24 hourly/8 hourly values should be met 98% of the time in a year. However, 2% of the time, it may exceed but not on two consecutive days.				

II. Pre-Audit Questionnaire - *Sample*

PAQ-1

1. Introduction

The purpose of this questionnaire is gather the necessary information on the audit site prior to undertaking an on-site audit.

The questionnaire covers each area of environmental concern, and is supplemented by information checklists for each of these areas. This questionnaire is designed to familiarize the environmental audit team with the site operations prior to the audit visit, while information checklists highlight a list of the documents required prior to the audit.

Please complete the forms as thoroughly and accurately as possible. Where a question does not apply or cannot be answered, please respond with not applicable or unknown. Respondents are encouraged to provide responses which reflect the actual conditions as opposed to the 'ideal' situation. Provision of pertinent information prior to the audit visit will allow the audit team to be adequately prepared resulting in a more effective audit.

Note: Unless otherwise specified, references made to 'premises' or 'area' in this questionnaire generally refer to premises which the respondent represents.

PPAQ-2

2. General Departmental Information

(To be completed by the Designated Internal Auditor)

Building Information

A. Are the premises owned or leased?

i. When were the properties first acquired by this department?

ii. What are the areas of the premises (break down by floor/functional area)?

iii Are there any known cases of asbestos material use in the building construction? If so, are these uses indicated on the floor plans?

B. Indicate the dates, ownership, and use(s) of the properties prior to the date of acquisition or lease by this department.

C. Have there been any remedial investigations or corrective actions taken at these premises (e.g.indoor air quality monitoring, wastewater monitoring, etc.) ? Describe briefly:

D. Have there been any known discharges, investigations, or mitigation actions at neighbouringoffices/adjacent buildings? If so, describe briefly.

E. List the names of environmental or building services consultants retained (i.e. IAQ monitoring, energy audit etc.) and briefly describe the projects involved.

Provide name of staff responsible for Departmental building services issues.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-3

2.1 Overall Environmental Management

Departmental Level

(Questions A to K to be completed by Designated Internal Auditors)

A. List number of staff at the premises (by location):

   Professional

   Technical/Field

   Others (please specify)

B. Is there a Departmental Environmental Policy? If so, please provide a copy.

C. Describe the scope of existing Departmental Policy (i.e. application to resources used, pollution prevention, energy use and conservation, training, public relations etc.).

D. Is the Environmental Policy signed by the Director of the Department?

E. Has a Department Environmental Coordinator been formally appointed and given the responsibility of implementing the policy within the Department?

F. Has the Department Environmental Coordinator been given the responsibility for monitoring the effectiveness of policy implementation?

G. Is the Environmental Policy on prominent display at all Departmental premises?

H. Has every staff member been issued with a copy (or summary) of the Environmental Policy?

I. Is there a written procedure and schedule for reviewing the Environmental Policy?

PAQ-4

J. Are all revisions of the Environmental Policy communicated to all parties concerned? (i.e., office managers, staff members, concerned public members)?

K. Have staff, financial and other necessary resources been allocated to cover specific environmental issues (i.e., emergencies, waste management, monitoring, audit, etc.) at Departmental level? Please specify.

Provide name of staff responsible for Departmental Environmental Policy issues.

Name and Title:

Location:

Telephone:

Facsimile:

Premise Level

(Questions L to S to be completed by Site Facilitators or designated persons)

L. List number of staff at the premises (by floor):

Professional

Technical/Field

Others (please specify)

M Indicate elements of Departmental Policy pertinent to the responsibility of this premise.

N. Has an office environmental coordinator been formally appointed and given the responsibility of implementing the policy within the office?

PAQ-5

O. Has an office environmental coordinator been given the responsibility for monitoring the effectiveness of policy implementation?

P. Is the Environmental Policy on prominent display at this premise?

Q. Has every office member been issued with a copy (or summary) of the Environmental Policy?

R. Are all revisions of the Environmental Policy communicated to all members concerned?

S Have staff, financial and other necessary resources been allocated to cover specific environmental issues (emergencies, waste management, monitoring of discharges/ emissions, environmental performance audit) at office level? Please specify.

Provide name of staff responsible for Office Environmental Policy issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-6

2.2 Materials Procurement Policy

Departmental Level

(Questions A to E to be completed by the Designated Internal Auditors)

A. Is there an inventory of all incoming supplies and materials for:

   i. Office supplies (i.e., paper, stationery etc.)

   ii. Computer related supplies (i.e., printer toner cartridges, paper etc.)

   iii. Refreshment supplies (i.e., Styrofoam cups, packaged beverages etc.)

   iv. Others (specify)

B. Are there any defined procedures for inventory keeping, updating and checking?

C. Is there a mechanism for verifying new supplies/materials for:

   i. Nature, quality, quantity, and specification

   ii. Compliance with environmental regulations and/or Departmental guidelines

   iii. Potential environmental impacts

   iv. Compliance with health and safety regulations and/or Departmental guidelines

   v. Packaging materials (i.e., quantity, biodegradability, recyclability etc.)

D. Provide details on any policy/guidance for reviewing existing supplies and materials in relation to possible 'environmentally friendly' alternatives:

E. Is there a similar system of controls on the materials introduced to the premises (i.e., contractors, laboratory samples etc.)?

Provide the name of staff responsible for Departmental procurement issues.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

(Questions F to J refer to areas over and above procurement undertaken at the premise level, and are to be completed by Site Facilitators or Designated persons)

F. Is there an inventory of all incoming supplies and materials?

G. Are there any defined procedures for inventory keeping, updating and checking?

H Is there a mechanism for checking of new supplies and materials for:

   i. Nature, quality, quantity, and specification

   ii. Compliance with environmental regulations and/or Departmental guidelines

   iii. Possible environmental impacts

   iv. Compliance with health and safety regulations and/or Departmental guidelines

   v. Packaging materials (i.e., quantity, biodegradability, recyclability etc.)

I. Provide details on any policy/guidance for reviewing existing supplies and materials in relation to possible 'environmentally friendly' alternatives:

J. Is there a similar system of controls on the materials introduced to the Departmental premises (i.e., contractors, laboratory samples etc.)?

Provide the name of staff responsible for procurement issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-9

2.3 Energy Management

(To be completed by the Designated Internal Auditor)

A. Are there records of energy use for the Department's premises (e.g. break down by floor)?

B Have there been audits undertaken to identify energy use and minimisation opportunities? If so, where are the reports kept?

C Are there defined maintenance programmes to ensure all equipment is operating at optimum efficiency?

D. Are there formal arrangements to replace energy inefficient equipment/ fixtures?

E. Are there formal procedures to consider energy efficiency when purchasing new equipment?

F. Is there a written commitment to reduce energy use? If so, attach a copy.

G. Has the responsibility to reduce energy use been formally allocated in writing?

H. Programmes to monitor energy use and to quantify reduction? Where are the records kept?

Provide name of staff responsible for energy management issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-10

2.4 Material Management

(To be completed by the Site Facilitators or other appropriate persons)

Office Operation

A. Is there an inventory for all supplies and materials?

B. Is there a mechanism for managing existing supplies and materials for:

i. Nature, quality,quantity and specification

ii. Compliance with environmental regulations and/or Departmental guidelines

iii. Possible environmental impacts

iv. Compliance with health and safety regulations and/or Departmental guidelines

v. Packaging materials (i.e. quantity, biodegradability, recyclability etc.)

C. Describe any guidance or procedures to review current supplies and materials in relation to:

i. Eliminate/minimise use of 'environmentally unfriendly' materials

ii. Eliminate/minimise storage of 'environmentally unfriendly' materials

iii. Eliminate/minimise waste generation

iv Recycling and reuse (i.e. printer toner cartridges, used paper etc.)

D. Describe any guidance or practice on material management leading to overall environmental performance improvement (i.e., double sided printed, single line spacing, use of non glossy report covers, use of recycled paper stock etc.).

PAQ-11

Laboratory Operation

E. Indicate activities where hazardous materials are used. Describe the nature and quantity of hazardous materials involved, including the following materials - acids, irritants, bases, sensitizers, asphyxiants, heavy metals, cryogens, flammables, carcinogens, poisons, biological/infectious materials, radioactive, explosive materials.

F. Is there an inventory of all incoming supplies and materials for:

i. Standard laboratory supplies

ii. Dangerous materials

iii Chemicals

iv. Biological/infectious materials

v. Radioactive materials

G. Does the facility maintain a current file of material safety data sheets (MSDS) for all hazardous materials stored at the facility?

H. Provide details of any licences, permits or applications on file pertinent to hazardous materials storage and handling (i.e. title, number, materials covered, etc).

I. If applicable, describe investigations or corrective actions taken in the past (i.e. regarding fugitive emissions to atmosphere, major chemical spillages, etc.).

J. Provide details on any policy or practices relating to the prevention or reduction in overall environmental impact concerning:

   i. Elimination of use of environmental or health and safety adverse substances (i.e., ozone depleting substances, asbestos etc.)

   ii. Proper storage and leakage containment of dangerous materials and chemicals (i.e., corrosive substances, explosives, poisons etc.)

   iii. Appropriate storage and labelling of materials

   iv. Scheduled inspection of storage and handling facilities

Provide name of staff responsible for hazardous materials handling at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

Pesticides

K. Are pesticides used in the premises? If yes, indicate general types and indicate if the use of these pesticides are restricted by any sort of control:

Algicides Herbicides

Insecticides Rodenticides

Fungicides Other

L. Are pesticides applied by Departmental personnel? If so, indicate whether any certification is required by pesticide handlers. Provide details of this certification (i.e., certification title and number, type of pesticide covered etc.).

PAQ-13

M If pesticides are stored at these facilities, briefly describe the following:

i. Locations and storage practices

ii. Measures in pesticide storage, application and disposal

iii. Segregation practices

N If outside contractors are utilized for pesticide application, indicate below:

Contractor

Service

Provided

Initial Date of

Application &

Frequency

Certification

Number

Indicate the name of staff responsible for pesticides issues at this premise.

Staff name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-14

Asbestos

O. Describe any formal asbestos management programme in place

P. Describe any formal procedures to audit compliance in the asbestos management programme.

Q. Have formal surveys and inspections been conducted at the site to identify areas if and where asbestos-containing materials are located?

R. If known, list the premises that have been identified as having asbestos-containing materials and indicate whether the buildings are leased or owned, whether abatement is occurring or is planned, and the type of asbestos-containing material(s) present.

Premises Leased/Owned Abatement Action

Asbestos-Containing

Material Type*

* Use following codes: A = sprayed on insulation; B = pipe insulation; C = vessel/ tank

insulation; D = equipment (describe, i.e. ovens etc.); E = other (describe, i.e. floor tiles, bench tops etc.)

Provide name of staff responsible for asbestos management issues.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-15

2.5 Water Supply Management

(To be completed by Site Facilitators or other appropriate persons)

A. Indicate the source of water supply at the premises.

B. What are the uses of water supplied?

C. Describe any on-site potable/process water treatment systems.

D. Indicate frequency of system maintenance/resin regeneration.

Provide name of staff responsible for water supply and quality issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-16

2.6 Wastewater Management

(To be completed by Site Facilitators or other appropriate persons)

A. List the sources of wastewater, type of discharge and daily volumes for the following types of wastewater.

   Source

   Discharge

   Frequency

Volume

(indicate units)

i. Laboratory Wastewater

ii. Sanitary Wastewater

iii. Cooling Water

Contact

Noncontact

iv. Others (describe)

B. Provide details of any licences or applications on file pertaining to water pollution control regulations (i.e. licence title and number, issuing agency, sources of wastewater covered, locations of discharge points, specific discharge standards etc.).

C. Describe type(s) of wastewater pre-treatment prior to discharge (i.e. oil separation, neutralization, filtration, ion exchange, carbon treatment etc.).

D. Indicate locations of all discharge points.

E. Describe operational specifications and maintenance schedules of the pre-treatment system. Have records been kept?

PAQ-17

1.6 Wastewater Management (Cont'd)

F. Is any wastewater recycled? If so, describe briefly (i.e. treatment and use).

G. Describe any formal criteria for reviewing the premises discharge strategies (i.e., reduce or eliminatedischarges).

H. Describe any written procedures to be followed in the event of exceedence of discharge standards.

I. Are all relevant staff fully trained in the above procedures?

J. Describe any wastewater compliance monitoring programmes in place. Where are records of all monitoring results kept?

K. Were there ever any internal investigation and/or mitigation actions taken for wastewater related issues? If so, specify.

Provide name of staff responsible for premises related wastewater regulatory issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-18

2.7 Waste Management

(To be completed by Site Facilitators or other appropriate persons)

A. Provide details of internal classification, source, nature, quantity and frequency of waste generated (including waste samples brought in for analysis and used pesticides) for:

   i. Dangerous waste

   ii. Chemical waste

   iii. Biological/infectious waste

   iv. Solid waste (including obsolete equipment)

   v. Radioactive waste

   vi. Other wastes (specify)

B. Provide details of any licences, permits or applications on file (i.e. licence/permit and title, number, issuing agency, sources covered, special conditions etc.) in relation to generation, storage, handling, disposal or transportation of these wastes.

C. Provide details of any on-site waste or disposal systems (i.e. type of waste disposal system and capacity, type and quantity of waste disposed of etc.) for these wastes.

D. Describe operational specifications and maintenance schedules of the pre-treatment system. If records have been kept, indicate location.

E. Briefly describe any waste recycled (i.e. type, source, characteristics, treatment and use).

F. Briefly describe any current waste minimisation programmes (i.e., reduction, reuse and recycling) and indicate responsible staff.

PAQ-19

G. Provide the following information for any off-site facilities used for waste treatment, storage or disposal in the past three (3) years.

   Company

   Name

Premises

Name

Type of

Waste

Volume

(Per Month)

Treatment/

Disposal Method

H. Existing programme to audit regulatory compliance in place at the premises? Describe briefly.

I. Has there been any internal investigation in relation to waste generation, storage, handling or disposal? If so, describe briefly.

Provide name of staff responsible for waste management issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-20

2.8 Air Quality Monitoring and Control

(To be completed by Site Facilitators or other appropriate persons)

General

A. Describe any formal policy or written guidance in relation to air quality (e.g. smoking policy, use of non-formaldehyde containing carpet underlay/furniture, substitute ozone depleting substances in solvents, refrigerants and fire extinguishers etc.).

Office Operation

B. Indicate the number of each type of the following equipment at this premise:

Laser printer

Xerox/Photocopier

Facsimile machine

Computer

Others(e.g. ozone

generator, specify)

C. Indicate all other significant sources of indoor air emissions/pollutants not covered above.

D. Has indoor air pollution at this premise been monitored in the past? If so, are records of findings kept and where?

F. Is there a programme to monitor the indoor air quality at this premise? If so, describe briefly.

G. Describe any mitigation actions taken in the area with respect to indoor air quality improvement.

PAQ-21

H. If applicable, indicate any known respiratory symptoms or irritations experienced by your premise members (i.e. frequent flu symptoms, sore throat, eye irritation etc.).

I. Describe known time pattern of symptoms occurrence and relief (i.e. morning, afternoon, weekend etc.).

Provide the name of staff responsible for indoor air quality issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

Laboratory Operation

J. Identify operations conducted at the premises that involve air emissions (i.e. handling of chemicals and solvents, biological sample preservation etc.).

K. Is there an inventory of all emissions (including fugitive emissions) released from the area?

L. Describe any programme of updating emissions inventory.

M. Describe the air pollution control equipment installed and operating at the premises (i.e. particulate filters, scrubbers etc.).

PAQ-22

N. Indicate the number and location of stacks, vents or other outside emission points originating from the area.

O. Provide details of any licences or applications on file pertinent to ambient air quality regulations (i.e. licence title and number, issuing agency, sources of air emissions etc.).

P. Describe any formal criteria for reviewing the premises emission strategy (i.e., eliminate or reduce emissions).

Q. Has this area ever been under any internal investigation and/or taken mitigation action related to ambient air emissions? If so, specify.

R. Describe any ambient air compliance monitoring programmes in place at the premises. Are records kept of all monitoring results?

S. Describe any written procedures to be followed in the event of standard exceedance.

T. Are all relevant staff fully trained in the above procedures?

Provide name of staff responsible for outdoor air quality issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

2.9 Noise Monitoring and Control

(To be completed by Site Facilitators or other appropriate persons)

A. Identify all operations or activities that may substantially elevate noise beyond normal premise background levels.

B. If applicable, describe any current practices to reduce noise levels at the premise.

C. Have there been any noise monitoring programmes undertaken at the premises? If so, describe briefly.

D. Have there been any formal complaints received on noise generated within the area? If so, provide details.

Provide name of staff responsible for noise monitoring and control issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-24

2.10 Transportation and Travel

(To be completed by Site Facilitators or other appropriate persons)

A. Describe any formal car fleet procurement policies or selection criteria related to overall environmental performance (i.e. fuel type and economy, refrigerant use, emissions standard, noise level, recyclability of materials, paint use etc.).

B. Is there an inventory of transportation devices operated by the Department? Describe scope of the inventory (i.e. fuel type and economy, emission level, maintenance requirements etc.).

C. Describe scope of maintenance programme in place for all transportation devices.

D. Is there any formal policy or guidance on spillage prevention and disposal of fleet maintenance wastes (i.e., engine oil, refrigerant, tyre etc.)?

E. Is there a programme in place to monitor air and noise emissions and to effect appropriate arrangement for corrective maintenance as required?

F. Describe training/instruction provided to drivers/operators on increasing the fleet's environmental performance (i.e. turn off idle engines, minimise number of trips etc.)?

G. Is there any written policy or guidance on use of Department vs. private vehicles?

H. Existing guidance on staff transport arrangements to encourage use of public transportation?

Provide name of staff responsible for transportation and travel related issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-25

2.11 Emergency Response Procedures

(To be completed by Site Facilitators or other appropriate persons)

A. Attach copy of any formal emergency response procedures and/or contingency plans on:

   i. Disruption of water supply

   ii. Supplied water treatment system failure

   iii. Wastewater treatment system failure

   iv. Chemical/chemical waste spillage

   v. Dangerous materials/waste spillage

   vi. Biological/infectious materials/waste release

   vii. Radioactive materials/waste release

B. Provide details of any equipment located in areas where emergencies have the potential to occur.

C. Are the staff in these areas appropriately trained in emergency response procedures?

Provide name of staff responsible for emergency response procedures issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-26

2.12 Staff Awareness and Training

(To be completed by Site Facilitators or other appropriate persons)

Staff Awareness

A. Are there any regular general meetings on the improvement of the working environment?

B. Has there been wide participation in specific environmental management issues in the office (e.g. campaigns on reduction of paper and energy usage)? If so, are staff members adequately informed of the specifics (i.e. objectives, approach etc.)?

Training

C. Describe briefly the nature and topics of premises environmental training (workshops, seminars, campaigns/ activities etc.) offered in the past year.

D. Is the training programme offered to all relevant personnel?

E. Have there been regular reviews to ensure the effectiveness of the training programme?

F. Have the participants been involved in the training review process?

Provide name of staff responsible for staff awareness and training related issues at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

PAQ-27

2.13 Publicity of Environmental Information

(To be completed by Site Facilitators or other appropriate persons)

A. Describe any formal programme to ensure staff members responsible for publicity of environmental information have the relevant experience and adequate training.

B. Are there any formal procedures to review adequacy of publicity materials?

C. Describe any programme to ensure that information contained in the publicity materials are correct and up to date.

Provide name of staff responsible for publicity of environmental information at this premise.

Name and Title:

Location:

Telephone no.:

Facsimile no.:

QUESTIONNAIRE COMPLETED BY:

Name and Title:

Premise:

Location:

Telephone no.:

Facsimile no.:

Date:

2.14 Response to Public Enquiries and Complaints

(To be completed by Site Facilitators or other appropriate persons)

A. Describe any formal procedures or guidelines in enquiry referral (i.e. both internal and external).

B. Does the Department have any procedures in place to handle enquiries on environmental information that is publicly available? If so, describe the procedures.

C. Are there any procedures or guidelines available to handle complaints received from the public?

If so, describe briefly.

Provide name of staff responsible for public enquiries and complaints at this premise.

Name and Title:

Location:

Telephone no.:

Fascsimile no.:

For Further Understanding

1. INTOSAI Working Group on Environmental Auditing

The International Organization of Supreme Audit Institutions (INTOSAI) is the professional organization of supreme audit institutions (SAI) in countries that belong to the United Nations or its specialized agencies. INTOSAI was founded in 1953 and has grown from the original 34 countries to a membership of over 180 SAIs.

WEGA – Working Group on Environmental Auditing

Mission

The Working Group on Environmental Auditing (WGEA), under the International Organization of Supreme Audit Institutions (INTOSAI), aims to improve the use of audit mandate and audit instruments in the field of environmental protection policies, by both members of the Working Group and non-member Supreme Audit Institutions (SAIs). Joint auditing by SAIs of cross border environmental issues and policies, and the audit of international environmental accords, has the Working Group's special attention.

Mandate/Objectives

In order to carry out our mission, the WGEA:

- Assists supreme audit institutions (SAIs) in acquiring a better understanding of the specific issues involved in environmental auditing;
- Facilitates exchange of information and experience among SAIs; and
- Publishes guidelines and other informative material for their use.

Different working bodies of the INTOSAI WGEA

The INTOSAI WGEA is a large, volunteer organization with a number of distinct bodies and players, each with associated responsibilities. These include the Chair and Secretariat, the full WGEA (the Assembly), the Steering Committee, Project Leaders and project subcommittees, and the Regional Working Groups on environmental auditing. With a view to strengthening the overall functioning of the WGEA and to clarify the key roles and responsibilities for each of bodies, a Roles and Responsibilities document was approved by the Assembly

2. Environmental Cost and International Accounting Standards

At the highest level of generally accepted accounting principles (GAAP) are the Statements of Financial Accounting Standards (SFAS) which are issued by the Financial Accounting Standards Board (FASB).

The FASB Emerging Issues Task Force (EITF) was formed in July 1984 to assist the FASB identify emerging issues affecting financial reporting and resolve problems in implementing authoritative pronouncements. A consensus position reached by the EITF is GAAP that must be followed unless it conflicts with a FASB Statement, Interpretation or Technical Bulletin, APB Opinion, Accounting Research Bulletin, SOP, or AICPA Industry Audit and Accounting Guide.

EITF consensus positions generally are effective upon issuance. Statements of Position (SOP) are issued by the Accounting Standards Executive Committee of the American Institute of CPAs (AICPA). Some of the key accounting pronouncements that regard environmental reporting are the following:

(1) SFAS No. 5 states under "Accounting for Contingencies" that a liability should be recognized in the financial statements if a loss is probable and the amount is estimable. If the loss amount is not estimable which is often the case, the contingency must be described in the footnotes to the financial statements.

(2) ETIF Issue No. 90-8 required that all environmental contamination costs be expensed as incurred unless costs extend the life or increase capacity of the property, costs mitigate or prevent future environmental contamination (that would otherwise occur), or costs are incurred to prepare a property for sale.

(3) ETIF Issue No. 93-5 concluded that an environmental liability must be evaluated independently from any potential claim for recovery. This recovery claim can reduce the liability only if it is probable. Securities Exchange Commission (SEC) standards state that it is appropriate to net the asset and liability if the asset's recovery is recognized as probable. The asset and liability should be disclosed in the notes to the financial statements. The SEC approves discounting of liabilities to their present value. The Management Discussion and Analysis section of the annual report requires "forward looking" disclosures.

The SEC in Interpretation No.14 states that registrants must take reasonable steps to identify the minimum end of the loss range with a higher priority on studying sites where a known problem exists. Registrants should assess the probability of an environmental obligation and any insurance recovery independently. Post-remediation monitoring approaches have been developed.

(4) AICPA Statement of Position (SOP) 96-1, "Environmental Remediation Liabilities," covers auditing and accounting topics dealing with environmental

issues. It details the responsibilities of corporations involved in environmental cleanup, and responsibilities of corporations to avoid environmental destruction. SOP 96 is a comprehensive environmental issues guide.

U.S. publicly traded companies are required to be audited by an independent auditor (CPA firm) each year. The audited financial statements and audit report are filed with the Securities Exchange Commission. With regard to environmental issues, the auditor must first identify environmental risks and second, must check for compliance with related accounting standards.

Addressing Environmental Issues

The Financial Accounting Statements Board (FASB), the American Institute of Certified Public Accountants (AICPA), and the Securities and Exchange Commission (SEC) are addressing financial reporting questions associated with environmental costs and obligations. Their deliberations will have an impact on environmental reporting, accounting, and auditing. During the past two decades, corporations have significantly increased their voluntary disclosures of information about environmental matters and performance. A large number of companies have adopted environmental guidelines expecting to gain valuable public relations dividends and to attract more investment opportunities.

Protecting the environment is widely regarded as a God-given responsibility of mankind. People must have clean air, water, and soil to survive.

3. Certification Bodies

a. CECAB

The Canadian Environmental Certification Approvals Board (CECAB) is responsible for the overseeing the administration, evaluation and ratification of ECO Canada's certification of Environmental Professionals (EP) in Canada.

In 1997, the Canadian Environmental Certification Approvals Board (CECAB) was established by ECO Canada to oversee the development and administration of a voluntary certification program for environmental professionals in Canada

EP certification establishes credibility for professionals on the basis of demonstrated competence. Recipients of the EP designation have demonstrated that their skills and knowledge meet or exceed the National Occupational Standards (NOS) in the areas of environmental protection, resource management, environmental sustainability, environmental management, environmental auditing and/or greenhouse gas reporting.

As a stepping-stone toward the EP designation, the Environmental Professional in Training (EPt) option is a developmental certification designed for emerging environmental professionals. It helps recipients identify professional development needs and provides centralized access to career resources.

National Occupational Standards for all Environmental Professionals

Developed and maintained by ECO Canada (Environmental Careers Organization), the NOS were created to provide a definitive guide to the skills and knowledge required for professionals to do their jobs within each specific field of environmental specialization. ECO Canada updates the standards in consultation with industry on a five-year minimum basis in order to reflect the rapidly evolving requirements of environmental practice.

b. IEMA

The Institute of Environmental Management & Assessment (IEMA) is **the largest professional membership body for the environment** with over 15,000 members working across all industry sectors. Join our growing community and help us influence government and decision-makers in organisations, which will place you, as an environmental professional, at the heart of change.

IEMA is the Competent Body in the United Kingdom for EMAS the European Union's Eco Management and Audit Scheme and also offers the Acorn Scheme, an officially recognised EMS standard recommended by the government. Acorn offers accredited recognition for organisations evaluating and improving their environmental performance through the phased implementation of an environmental management system (EMS).