Ministry of Rural Development
Government of India

Training Material
Certificate Course on Internal Audit

Volume-1

NIRDPR

National Institute of Rural Development and Panchayati Raj
Ministry of Rural Development, Government of India
Rajendranagar, Hyderabad - 500 030

Ministry of Rural Development

Government of India

Learning Material

CERTIFICATE COURSE

ON

INTERNAL AUDIT

Volume-I

NIRDPR

**NATIONAL INSTITUTE OF RURAL
DEVELOPMENT AND PANCHAYATI RAJ**

**The Institute of
Internal Auditors**

703796/2021/O/o CCA

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Message

The Ministry of Rural Development is the nodal Ministry for the development of rural area and plays a pivotal role in overall development strategy of the country with several flagship programmes. An outlay of more than Rs. 1,31,000/- crores has been provided to the Department of Rural Development during the year FY 2021-22 to carry out various programs of Rural Development like MGNREGS, DAY-NRLM, DDU-GKY, PMGSY, NSAP, PMAY-G, SPMRM and SAGY. The Ministry is responsible for ensuring proper management of public resources and operational efficiency and effectiveness of the schemes. These programmes encounter complexities and associated risks all the time and, therefore, these need to be addressed on continuous basis. Thus, there is a need to develop a very strong and robust accountability framework for all its programmes.

Internal Audit is an integral part of sound financial management systems worldwide. It also helps in improving economy, effectiveness and transparency of the public systems. The scope of Internal Audit has expanded from merely ascertaining compliance with rules and regulations to include appraisal and evaluation of individual schemes, assessment of risks and adequacy of internal controls and carry out a critical assessment of Economy, Efficiency and Effectiveness of service delivery mechanisms to ensure value for money.

The Internal Audit Wing through their reports provide an opportunity to the top management of the Ministry to initiate remedial measures and take steps for improvement in Programme delivery as well as to provide reasonable assurance and contribute to the improvement of risk management processes. An efficient and effective Internal Audit practice, therefore, warrants that the Internal Audit Wings have trained and competent staff and supervisory officers. Towards achievement of this objective, the Ministry of Rural Development has envisaged to provide sustainable capacity building of internal auditors through Training and Certification by conducting a certificate course on Internal Auditors through Center for Internal Audit in Rural Development (CIARD), NIRD & PR.

The learning material for the Certification Course (Volume-I on Audit Procedures and Volume-II on Rural Development Schemes) has been prepared in 2018 by NIRD&PR faculty along with The Institute of Internal Auditors-India (IIA-India). Since then a lot of changes have come in the Guidelines and Implementation processes of the Rural Development Schemes, it necessitated updation of the course material, which was carried out by CIARD with the assistance of other centers of NIRD & PR. I hope and believe that the updated material would be useful for the both the trainees and trainers as also laypersons interested in learning about the schemes and the system of controls and safeguards therein.

I congratulate Director General, NIRD & PR, Director, CIARD and his team, Internal Audit Wing and Programme Divisions for updating the learning material.

[Nagendra Nath Sinha]

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Dr. G. Narendra Kumar, IAS
Director General

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MESSAGE

The National Institute of Rural Development and Panchayati Raj (NIRDPR) is facilitating Rural Development efforts with particular emphasis on the rural poor by improving the knowledge, skills and attitude of Rural Development Officials and Non-officials through organizing trainings, workshops and seminars on various flagship programmes. Internal Audit is one of the tools to improve the accountability and transparency in the implementation of MoRD flagship programmes which was introduced in the year 2016 and a need is felt to create a well- equipped pool of internal auditors to conduct such Internal Audits. In this context Expert Advisory Group, which is constituted by MoRD to strengthen the internal audit process in RD programmes, has come up with some recommendations, and establishment of CIARD at NIRDPR is one of the recommendations which will take care of capacity building of internal auditors, liaising with State Governments/SIRDs, to conduct research/evaluation studies and to provide assistance to Internal Audit Wing (IAW).

O/o the Chief Controller of Accounts (CCA) had assigned the NIRDPR to design the training course for Internal Auditors and to develop the course material. NIRDPR has designed 21 days Certificate course for Internal Auditors and developed course material for the same in coordination with the Institute of Internal Auditors (IIA) and Resource Centres of NIRDPR.

The course material has been developed in two volumes in the year 2018. Volume-I explains about basics of Internal Audit whereas Volume –II enlightens the guidelines and implementing process of 9 flagship programmes of MoRD. After conducting 5 batches of Certificate courses and 3 batches of ToTs, it was felt that some changes are required as per feedback from participants and also there are considerable changes in the Scheme guidelines and implementation process of MoRD schemes. Thus the Centre for Internal Audit in Rural Development (CIARD) has updated the Volume-I on Internal Audit process by adding four new chapters and with the assistance of other NIRD&PR Resource Centers and Programme Divisions of MoRD. The Updated course material is very comprehensive which gives the exposure on theoretical knowledge in internal audit procedures as well as MoRD programmes.

I extend my appreciation and congratulations to the Director CIARD and his team for their efforts in updating the course material for Three-week Certificate Course on "Risk Based Internal Audit in RD Programmes". I strongly feel that this learning material will enhance the professional expertise of the Internal Auditors and thus improve the governance of rural development initiatives of the Ministry of Rural Development (MoRD).

(Dr. G. Narendra Kumar)
Director General

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Message

The Ministry of Rural Development is releasing huge amounts of funds to various schemes, and it is imperative to conduct audit of the implementing agencies and other stake holders. Internal Audit of the schemes is carried out by Chief Controller of Accounts, MoRD, which facilitates achievement of the Ministry's objectives by evaluating and improving the effectiveness of risk management, internal control and governance processes.

An efficient and effective Internal Audit practice, therefore, warrants that the Internal Audit Wings have trained and competent staff and supervisory officers with technical skills as well as knowledge of the schemes and IT skills. To achieve this, MoRD has envisaged to provide sustainable capacity building to Internal Auditors by conducting three week certification course on Internal Audit through National Institute of Rural Development and Panchayati Raj.

I am happy to state that MoRD has issued SoP for setting up Internal Audit Wing in the States and revised guidelines for Certificate Course and Training of Trainers. I hope and firmly believe that it will lay down a clear roadmap in strengthening the internal audit function in the states as envisaged by Expert Advisory Group.

The updated material Volume-I on Audit procedure and Volume-II on Rural Development Schemes is very comprehensive and it will be very useful for the trainees who are having previous experience in Accounting and Audit procedures as well as in implementation of Rural Development schemes. I congratulate the CIARD and NIRDPR team and IAW, O/o CCA, MoRD involved in updating the course material and also adding a few new chapters on Basic Concepts of Accountancy, GRIP, and PFMS.

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October 13ᵗʰ, 2021

Message

Internal Audit is an integral part of sound financial management systems worldwide. It should aim at looking both at the financial and non-financial aspects of the Government operations and ensuring full value for the Government money. The Internal Audit function would help in improving economy, efficiency, effectiveness and transparency in the Government administration in general and financial administration in particular. It would also help in maintaining a sound record keeping systems with adequate checks and balances to ensure timely/adequate identification of risks and its mitigation. It aims at providing timely and adequate information for better decision making by the executives.

The Controller General of Accounts (CGA), as the designated authority for the conduct of Internal Audit in the Government of India, laid down general guidelines for the conduct of Internal Audit in the ministries and departments of the Central Government. The Department of Rural Development, GOI has set up Internal Audit Wing in the office of Chief Controller of Accounts. The Expert Advisory Group on Internal Audit appointed by MoRD has suggested that the scope of internal audit should expand from merely ascertaining compliance with rules and regulations to evaluation of achieving the objectives of the schemes. It has also suggested for creating a pool of internal auditors with retired and serving accounts officers and to provide training under three week certificate course on internal audit.

With the above back ground, the course material was designed by NIRDPR with the assistance of Institute of Internal Auditors (IIA) in two volumes. The Volume-I on Audit procedure was updated by adding 3 new topics (Basic concepts of Accountancy and Book keeping, PFMS and GRIP) based on the suggestions of the trainees. Volume-II on Rural Development Schemes was updated incorporating the latest changes with the assistance of NIRDPR Centers and MoRD Programme Divisions.

It is a very comprehensive study material for the Certification Course and Training of Trainers (ToTs) covering all the topics required for Internal Auditors. I congratulate everyone who were involved in the updating of this course material.

[R.D. Chouhan]

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Message

The National Institute of Rural Development and Panchayat Raj (NIRDPR) an autonomous organization under the Ministry of Rural Development is a premier institute in capacity building, action research, skill development of all the functionaries that contribute for the welfare of the rural poor. With a view to strengthen the accountability in various rural development programmes and creating well equipped manpower for internal audit a" Three week certificate course on Rural Development programs" was designed. The certificate course of Internal Audit as envisaged by the Ministry of Rural Development was aimed at creating a pool of Trained Internal Auditors, who will be equipped with the process of Internal Audit, Role & responsibilities of Internal Audit, various tools and technique used in Internal Audit, understanding various rural development schemes and Risk areas.

The volume -1 of the learning material has been developed with the help of Institute of Internal Auditors of India and this is based on International standards and best practices for the Internal Audit functions. NIRD&PR with its expertise in the flagship programmes has developed the learning material on Rural Development schemes and Risk areas for Audit (Volume-II).

Due to changes in the implementation guidelines of the schemes the need has arisen to update the course material. CIARD with the assistance of other NIRD&PR centers along with the Programme Division of MoRD, the course material has been updated. In Volume-I three chapters (Basic concepts of Accountancy and Book keeping, PFMS and GRIP) are included on the request of the participants of Three week certificate course. The risk registers for each scheme has been prepared and it will be given as a hand out to each participant after the risks identification and presentation session to the participants.

I am thankful to all Center Heads of NIRD&PR andProgramme Divisions of MORD for giving latest changes in the scheme guidelines and in updating the course material Volume-II. My congratulations to the CIARD team for bringing the updated course material for three week certificate course on Internal Audit in Rural Development programme.
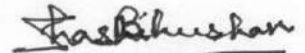
22/10/21

Shashi Bhushan

Table of Contents

Unit-I:

Ministry of Rural Development- Manual for Internal Audit

Learning outcomes:

To gain on insight into the organization structure of Internal Audit function including

♦ Internal Audit Wings

♦ Mandate of Internal Audit

♦ Internal Audit Charter

♦ Audit Committee

♦ Internal Audit Teams

♦ Roles and Responsibilities of IAWs

1.1   Introduction

- Departmentalization of Accounts was introduced by Government of India in 1976

- As per the provision of the scheme the Secretary, Ministry of RD is the Chief Accounting Authority of the Ministry

- This responsibility is discharged by Secretary through and with the assistance of Integrated Financial Advisor and Chief Controller of Accounts (CCA)

- The Internal Audit Wing (IAW) has been set up under the office of CCA

1.2   Responsibility of Chief Accounting Authority

- Under Rule 70 of GFR 2017 the Secretary of the Ministry or Department is the Chief Accounting Authority who is responsible and accountable for financial management of his/her Ministry or Department.

- Ensure that the public funds appropriated to the Ministry or Department are used for the purpose for which they were meant.

- Be responsible for the effective, efficient, economical and transparent use of resources of the Ministry or Department in achieving the stated project objectives of that Ministry or Department whilst complying with the performance standards.

- Review and monitor regularly the performance of the programmes and projects assigned to his Ministry to determine whether stated objectives are achieved.

- Be responsible for preparation of expenditure and other statements relating to his/her Ministry or Departments as required by regulations, guidelines or directives issued by Ministry of Finance.

- Shall ensure that his/her Ministry or Department maintains full and proper records of financial transactions and adopts systems and procedures that will at times afford internal controls.

- Shall ensure that his/her Ministry or Department follows the Government procurement procedure for execution of works, as well as for procurement of services and supplies and implements it in fair & equitable, competitive transparent and cost-effective manner.

- *Internal Audit, conducted by O/o CCA helps in all the above tasks.*

1.3   Role of CCA in Internal Audit

Internal Audit Wing working under the control and supervision of the CCAs/CAs would move beyond the existing system of compliance/regularity audit and would focus on:

- The appraisal, monitoring and effectiveness of individual schemes.

- Assessment of adequacy and effectiveness of Internal Controls in general, soundness of financial systems, reliability of financial and accounting reports in particular.

- Identification and monitoring of risk factors (including those contained in the outcome budget).

- Critical assessment of economy, efficiency and effectiveness of service delivery mechanism to ensure value for money; and

- Provide an effective monitoring system to facilitate mid-course corrections.

1.4 Role of Internal Audit

- Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operation.

- The internal audit activity evaluates risk exposures relating to the organization's governance, operations and information systems, in relation to:

  ◊ Effectiveness and efficiency of operations.

  ◊ Reliability and integrity of financial and operational information.

  ◊ Safeguarding of assets.

  ◊ Compliance with laws, regulations and contracts.

2. Internal Audit Manual of MoRD

- The purpose of this manual is to assist the Internal Auditing Wing of the Ministry of Rural Development in conducting audit.

- It is intended to provide Internal Audit Wing (IAW) with practical guidance, tools and information for assessing risk in processes and activities; developing an appropriate internal auditing work program; and planning, performing and reporting on audit engagements.

- It aims at creating awareness among the auditee units.

- It further provides all the other relevant information on:

  ◊ Audit Committee

  ◊ Scope of Internal Audit

  ◊ Objectives of Internal Audit

  ◊ Role of Internal Audit

  ◊ Checks to be exercised by Internal Audit

  ◊ Audit Methodology

  ◊ Preparation of Annual audit plan and further sub plans

  ◊ Internal Audit Standards

  ◊ Guidelines on Performance Audit

  ◊ Guidelines on Risk Based Internal Audit

  ◊ Process of drafting audit paras

  ◊ Audit guidelines for audit of PAOs, NPS scheme, etc.

  ◊ Audit guidelines for MoRD schemes.

2.1 Audit Committee

- To provide an effective oversight mechanism for functioning of Internal Audit Wing an Audit Committee should be constituted in each Ministry and the same have the following composition:

    ◊ Secretary to the Govt. of India, Chairman

    ◊ SS & FA to the Govt. of India, Vice Chairman

    ◊ CCA, Member Secretary

    ◊ Joint Secretary (Admn.) , Member

- The purpose of Audit Committee is:

    ◊ Reliability of the entity's financial statements and disclosures.

    ◊ Effectiveness of the entity's control and risk management systems.

    ◊ Compliance with the entity's code of business conduct, legal and regulatory requirements.

    ◊ Independence, qualification and performance of the external auditors and the performance of the internal audit activity.

- The Audit Committee would be responsible for finalizing and approving the Internal Audit Charter, establishing its role, responsibility and structure within the organization.

- Periodic review of the administration of Internal Audit functions.

- Taking stock of Internal Audits conducted and serious findings thereof.

2.2 Management Team

- Management Team of the Internal Audit function would be headed by the Chief Audit Executive who would supervise the Internal Audit function of the Ministry

- Management team would:

    ◊ Discuss key areas and plan audits

    ◊ Supervise all the phases of Internal Audit: Annual audit plan, planning the audit engagements, conducting the audits, preparation and issue of reports, monitoring and follow up with the auditees.

    ◊ Ensure availability of human resources and their utilization

- Management team would have following composition:

    ◊ Chief Controller of Accounts (Chairman)

    ◊ Director (Finance)/Deputy Secretary (Member)

    ◊ Controller/ Deputy Controller /Assistant Controller of Accounts, IA (Member Secretary)

- Chief Audit Executive is the head of Management Team

- CCA, MoRD is Chief Audit Executive.

2.3 Scope of Internal Audit

- Internal Audit Manual (IAM) defines the scope of Internal Audit (IA)

- No officer to undertake checks which are beyond the scope of IA

- Any special investigation, can only be taken up with the approval of competent authority only

- All the findings of audit should be brought to the attention of Head of office.

2.4 Objectives of Internal Audit

- Internal Audit Manual defines the objectives of Internal Audit

- Internal Audit has twin objectives:

  ◊ Pointing out any omissions and defects in established receipts and payments, transactions and their accounting

  ◊ Assisting the field offices in adopting corrective financial and accounting procedures

- Internal Audit party will provide technical guidance to the auditee to follow the corrective path

- The main objective of Internal Audit is to ensure that the objectives of Department /Schemes are strictly adhered to

2.5 Role of Internal Audit

- The main role of Internal Audit is to assist the Department to achieve its aims and objectives

- The role includes assessing:

  ◊ Proper implementation of rules and procedures

  ◊ Maintenance of proper records

  ◊ Accuracy in expenditure reporting

  ◊ Efficiency and Economy in Public Expenditure

  ◊ Effectiveness of Expenditure

  ◊ Quality of public expenditure

- The roles of Internal Audit can be divided into two segments:

  ◊ Compliance Audit

  ◊ Performance Audit

  ◊ The first two roles – proper implementation of rules and procedures and maintenance of proper records can be clubbed under Compliance Audit

- The remaining four roles are under Performance Audit.

3.1 Duties of Internal Audit

- The primary function of internal audit is to verify the accuracy and completeness of accounts by applying all the prescribed checks. The main duties of IA include:

    ◊ Study of accounting procedures to ensuring that they are correct, adequate and free from any defects or lacunae.

    ◊ Watch over the implementation of the prescribed procedures and the orders issued from time to time.

Scrutiny and check of payments, accounting work of the Accounting Units.

    ◊ Investigation of important areas in accounting and other records.

    ◊ Coordination with other Ministries and CGA regarding Internal Audit Procedures.

    ◊ Periodical review of all Account records.

    ◊ Pursuance/settlement of objections taken in test audit, notes issued by Statutory Audit officers and other matters relating to Statutory Audit.

    ◊ To examine and report on points or irregularities brought to its notice by the Principal Accounts Office/ PAOs.

    ◊ Scrutinize purchase procedures in the office inspected.

    ◊ Scrutinize purchase for disposal of Assets.

    ◊ Recoveries are being affected regularly from the Government Servant, Third Party concerned timely and correctly.

    ◊ To prepare an annual plan of internal audit each year.

    ◊ To keep the manual of internal audit up-to-date.

3.2 Checks to be exercised by Internal Audit

- The Internal Audit team needs to exercise the below checks:

    ◊ Scrutiny of accounts maintained by PAO and DDOs

    ◊ Verification of accounting and payments procedures

    ◊ Scrutiny of sanctions

    ◊ Scrutiny of NPS records

    ◊ Maintenance of cash book, measurement book, expenditure register, liability register, and advance registers, log books, etc.

    ◊ Pay fixations, service books

    ◊ Tender documents

    ◊ GPF advances and accounts

- The Internal Audit team needs to exercise the below checks on revenue receipts:

  ◊ Demands are raised properly as required by act or law

  ◊ Collection and refunds are proper and credited in proper accounting heads

  ◊ Ensuring that proper safeguard exists so that there cannot be any willful omission or negligence

  ◊ All revenue receipts are timely remitted to government exchequer

- The Internal Audit team needs to exercise the below checks on scheme audits:

  ◊ All scheme guidelines are followed

  ◊ Any omissions/deviations are recorded and brought to attention of Head of Office

  ◊ Procurements are as per the established procedures

  ◊ Selection of Blocks / GPs for physical verification must be objective

4. Audit Methodology

- The audit is conducted on the basis of objectives, provisions of the scheme, flow of funds, specific rules and laws governing the execution of programme etc. along with compendium of operational guidelines and circulars.

- Entry Conference is done with Head of Office / Head of Department on first day.

- Audit team also visits line departments and securitizes their records.

- Internal Audit is conducted by scrutinizing the selected records of auditees, as complete scrutiny is not feasible, judgmental cases may be selected and checked.

- On the basis of the gravity of irregularities, Paras have been graded as high, moderate and low risk intensity by the Internal Audit.

- Site Inspection of project & works is also conducted by IA to validate the secondary data

- Internal Audit shall interact with beneficiaries to enquire about scheme implementation.

5. Preparation of Audit Plan

- Auditee units are selected by an objective criterion:

- An annual Audit Plan is prepared in the beginning of the year in such a way that the

  ◊ Units not audited in last 3-4 years

  ◊ Substantial expenditure / larger geographical area

  ◊ Any specific request from Program Division

- Audit plan is approved by the competent authority and is brought to the knowledge of the Secretary

- Quarterly sub plans are prepared out of the annual plan

- Any deviation from the plan needs to be approved on time by the competent authority

6. Internal Audit Standards

- These standards are prescribed by Institute of Charted Accountants of India

- Audit party must be aware of general principles prescribed by these Standards and should follow them while conducting the audit and preparing the reports and further action thereof

- 18 standards have been mentioned in the Internal Audit Manual

- The standards includes:

  ⇒ Planning an Internal Audit: SIA1: Ensures appropriate attention is devoted to significant areas of audit. Potential problems are identified.

  ⇒ Basic principles governing Internal Audit: SIA2: This standard explains the principles, namely, integrity, objectivity and independence, due professional care, skill, competence, work performed by others, documentation, planning, evidence and reporting which governs the internal auditor's professional responsibilities.

  ⇒ Documentation: SIA3: Establish standards and provide guidance on the documentation requirements in an internal audit. Adequate documents acts as basis for the planning and performing the internal audit. Documents provide the evidence of the work of the internal auditor.

  ⇒ Reporting: SIA4: Establish standards on the form and content of the internal auditor's report issued as a result of the internal audit performed by an internal auditor of the systems. SIA describes the basic elements of an internal audit report such as opening, objectives, scope paragraphs and executive summary.

  ⇒ Sampling: SIA5: It provides the guidance regarding the design and selection of an audit sample and also on the use of the audit sampling in the internal audit engagements. It provides guidance on the use of sampling in risk assessment procedures and test of controls performed by the internal auditor to obtain an understanding of the entity, business and its entity, business and its environment.

  ⇒ Analytical Procedure: SIA6: It deals with the aspects such as the nature and purpose of analytical procedures, analytical procedures as risk assessment, procedures and in planning the internal audit, analytical procedures as substantive procedures, analytical procedures in the overall review at the end of the internal audit.

  ⇒ Quality Assurance in Internal Audit: SIA7: Establishes standards and provides guidance regarding quality assurance in internal audit. A system for assuring the quality in internal audit should provide reasonable assurance that the internal auditors comply with professional standards, regulatory and legal requirements so that the reports issued by them are appropriate in all circumstances.

  ⇒ Terms on Internal Audit Engagement: SIA8: It defines the scope, authority, responsibilities, confidentiality, limitation and compensation of the internal auditors. Terms of Internal Audit Engagement lay down clarity

between the internal auditors and the users of their services for inculcating professionalism and avoiding misunderstanding as to any aspect of engagement.

⇒ Communication with Management: SIA9: It provides a framework for the internal auditor's communication with management. It identifies some specific matters to be communicated with the management as described in the terms of engagement like the internal auditor's responsibilities in relation to the terms of engagement, planned scope and timing of the internal audit, significant findings from the internal audit.

⇒ Internal Audit Evidence: SIA10: Establish standards on the basic principle that the internal auditor should obtain sufficient appropriate audit evidence through compliance and substantive procedures to substantiate his checking and findings and enable him to draw reasonable conclusion there from.

⇒ Consideration of Fraud in an Internal Audit: SIA11: The purpose of this standard is to establish standards on consideration of fraud in an internal audit. This Standard provides guidance on designing and implementation of the internal controls in an entity that would also help the internal audit to assess the risk of frauds. The Standard also establishes the responsibilities of the internal auditor relating to the fraud prevention and detection.

⇒ Internal Control Evaluation: SIA12: Establish standards and provide guidance on the procedures to be followed by the internal auditor in evaluating the system of internal control in an entity and for communicating weaknesses therein to those charged with governance.

⇒ Enterprise Risk Management: SIA13: Establish standards and provide guidance on review of an entity's risk management system during an internal audit or such other review exercise with the objective of providing an assurance thereon.

⇒ Internal Audit in an Information Technology Environment: SIA14: Establish standards on procedures to be followed when an internal audit is conducted in an Information Technology (IT) Environment. This Standard describes skill and competence needed by the internal auditor to conduct an internal audit in an information technology environment.

⇒ Knowledge of entity and its environment: SIA15: Establish standards and provide guidance on what constitutes the knowledge on an entity's business, its importance to the various phases of an internal audit engagement and the techniques to be adapted by the internal auditor in acquiring such knowledge about the client entity and its environment, prior to commencing an internal audit engagement.

⇒ Using the work of an Expert: SIA16: Establish standards and provide guidance where the internal auditor uses the work performed by an expert. The standard also explains situations in which the need for using the work of an expert might arise. Factors to consider when deciding whether to use the work of an expert or not.

7. Guidelines on Performance Audit

• Basic principles of Performance Audit

♦ Performance Audit is an assessment of efficiency and effectiveness of the programmes, with due regard to economy.

♦ Apart from the question whether the things are being done in the right way, it also addresses the question of whether the right things are being done

♦ Distinction between regularity and Performance Audit should always be kept in mind.

♦ Performance Audit is undertaken with the objective of improving performance of Public Sector/Govt. programmes.

- The subjects selected for Performance Audit could be a programme, segments of a programme including the processes, procedures and systems, and entity itself or parts of an entity, etc.

- The subjects of Performance Audit could be financial, non-financial or public interest and governance issues.

- The scope of audit should be limited to assessing and impact of the implementation of policy and the policy per se should not be questioned

- *Other guidelines and methodology for conducting Performance Audit is also mentioned in Internal Audit Manual*

8.1 Guidelines on Risk Based Internal Audit

Audit Process

RISK BASED INTERNAL AUDIT
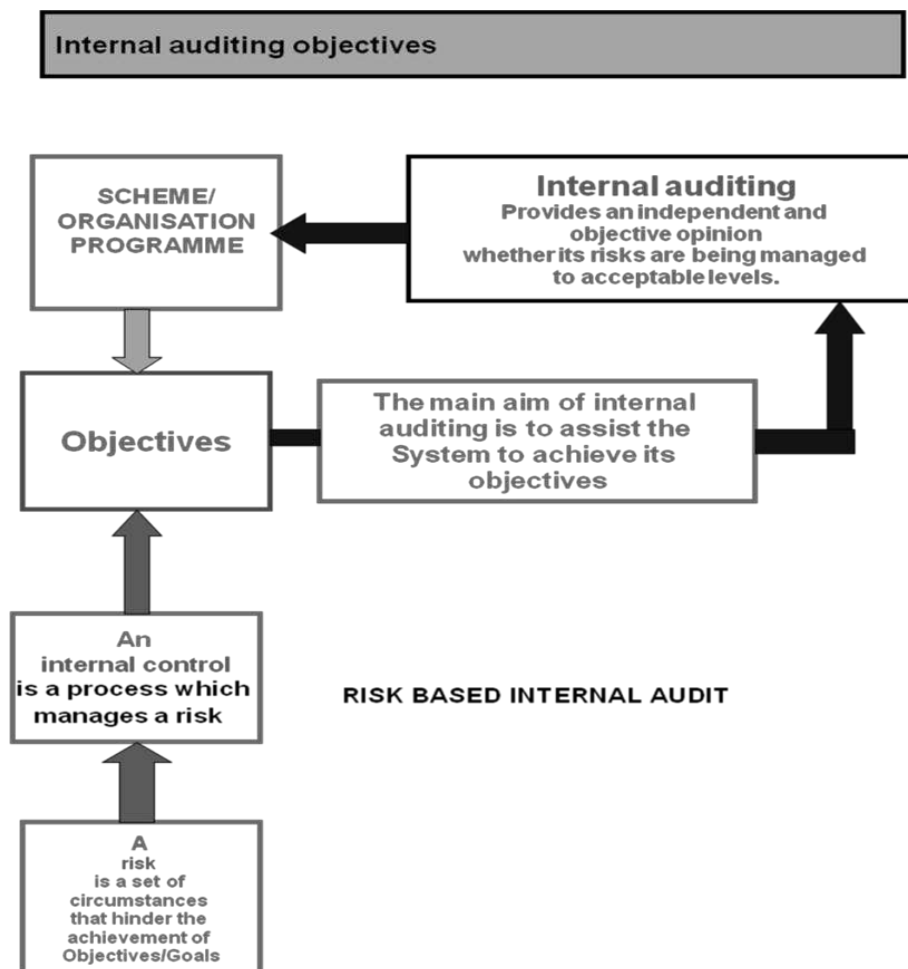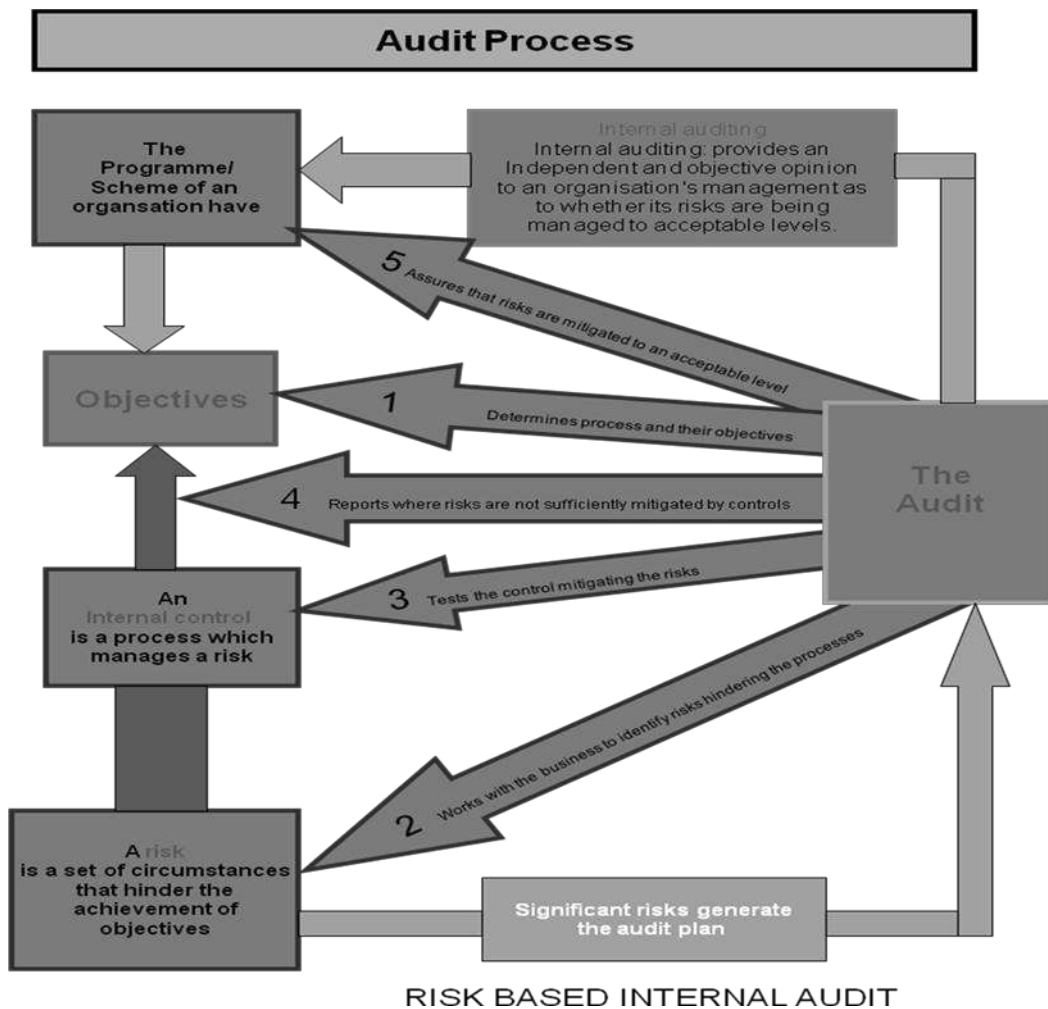
- There are three steps which are described below.

  ◊ Planning

  ◊ Performing

  ◊ Reporting

8.2 Planning

  ◊ Prepare the risk matrix

  ◊ Give weightage to different risks

  ◊ Prepare the audit memos

  ◊ Audit team must familiarize with objectives, processes and associated risks

  ◊ Performing

- Environment

- Internal Objectives Setting

- Event Identification

- Risk Assessment

- Risk Response

- Control Activities

- Information and Communication; and

- Monitoring

8.3   Performing: It has 8 interrelated components:

◊   Internal Environment

◊   Objectives setting

◊   Event Identification

◊   Risk Assessment

◊   Risk Response

◊   Control Activities

◊   Information and Communication; and

◊   Monitoring

8.4   Reporting: Audit reports should be based on below structure:

◊   Audit Objectives – To which audit engagement objective does this observation relate?

◊   Criteria – What should exist? (what ought to be)

◊   Condition – What exist?

◊   Impact – What effect did it have? (cumulative, direct and systematic)

◊   Cause – Why did it happen? (proximate, intermediate, Root-cause)

◊   Recommendation – What should be done? (cause focused condition focused or recovery focused)

◊   Propose ratings for different risks: High, Moderate and Low risks.

8.5   Drafting of IA reports

- The report should include the following elements:

◊   Brief description of activity under review

◊   Scope and purpose of engagement

◊   Time frame covered

◊   Observations. The methodology to draft it is:

*   Criteria

*   Condition or fact: as exists

*   Cause : why the conditions exists

*   Effect

*   Recommendations

*   Conclusion

◊   Draft reports are approved by the competent authority

◊   GRIP software is also being used by MoRD for this purpose

◊   Approved reports are dispatched to auditee

◊   Pursuance of audit reports with the auditees

◊   Processing the ATRs and settlement of audit paras, with the approval of competent authority

◊   Further follow ups

◊   Submission of monthly, quarterly and annual Audit reports

9.1   Audit guidelines for PAOs, NPS

• Internal Audit Manual provide guidelines to be followed for auditing PAOs, NPS

• These are based on guidelines issued by O/o CGA, time to time

• Detailed guidelines are available for inspection of different records, registers, assests, receivables, inventories, receipts and expenditure

• Proper procedures and guidelines are also mentioned for audit of financial statements, balance sheet.

10.1 Audit guidelines for MoRD Schemes:

• Scheme audits are the most important audits conducted by Internal Audit Wing of MoRD

• It includes schemes of MoRD, DWS, LR and MoPR

• Checklists have been mentioned for different schemes

• Risk matrices are included for different schemes

• Audits are conducted to assess the compliance with the scheme objectives

- Checklists are followed while conducting the audits

- Risks are identified and categorized based on the risk matrix

- Reports are prepared as per procedure mentioned earlier in Internal Audit Manual

- It is the guiding document based on which all the Internal Audits will be conducted

- Reports are also prepared as per Internal Audit Manual guidelines

- It is not a static document and needs to be updated timely to make it up to date with changes in schemes guidelines, upcoming risks, etc.

WORKBOOK

1.   What is the primary function of internal audit?

_____

_____

_____

2.   How does the IIA define internal audit?

_____

_____

_____

3.   What are the different types of internal audit?

_____

_____

_____

4.   What are the typical components of a code of ethical conduct?

_____

_____

_____

5.   How many core principles are there for the professional practice of internal auditing?

_____

_____

_____

6.   Name any 5 core principles for the practice of internal auditing?

_____

_____

_____

7.   Internal audit provides reasonable assurance that:

    1.   _____ is accurate, reliable and timely

    2.   _____ are acquired economically

    3.   _____ are safeguarded

    4.   Compliance with _____ and _____

    5.   _____ will be achieved

8. Name the 3 E's of performance audit

_____

_____

_____

9. Financial audit provides reasonable assurance that financial statements of the ministry present a _____

and _____ view.

10. In risk based auditing, the role of internal auditor shifts from examination of _____

to review of the risk management process.

_____

_____

_____

11. The primary purpose of a code of ethical conduct is to

_____

_____

_____

Unit-2

GRameen Internal audit Portal (GRIP)

GRameen Internal audit Portal (GRIP)

Learning Outcomes:

♦ Introduction and objectives

♦ GRIP features

♦ Audit process flow and support tasks

♦ Communication support and reports

♦ Advantages of GRIP

1. INTRODUCTION AND OBJECTIVES

1.1 INTRODUCTION

GRIP stands for GRAMEEN INTERNAL AUDIT PORTAL, and it is an initiative taken by Office of Chief Controller of Accounts (CCA), Ministry of Rural Development, (MoRD), Government of India (GoI) in order to give impetus to Digital India, with deriving advantage of digital technology, to expedite the Risk Based Internal Audit process through automation. It is web based software application with the support of audit process to strengthen the accountability framework of MoRD schemes through facilitating risk based internal auditing. It is first of its kind project of Government of India (GoI) in the field of internal control and Internal Audit on internet enabled platform.

1.2 OBJECTIVES

• Digitalization and Automation of the Internal Audit process

• Facilitating the Risk Based Internal Audit process

• Ensuring Efficiency and Effectiveness of internal controls

• Improved Transparency and Data Security

• Creating impact on decision making by Data Integration and Analytical Insights

• Speed-up auditing process by providing User Friendly Interface

• Promoting Eco-friendly process by digital transactions

• Evolving Information and Communication Technology (ICT) usage, across India by Capacity Building in Risk Based Internal Audit for all the schemes

• Facilitating to share expertise, knowledge and best practices

2. FEATURES OF GRIP

2.1 GOVERNMENT PROCESS RE-ENGINEERING

Automation with GRIP brings easy way of audit process, with eliminating redundant processes, with accuracy, easy follow up of Action Taken Report (ATR), improved work flow with fastness and transparency.

2.2. USER CONVENIENCE

The software is user-friendly, with 24x7 accessibility, flexible, serviceable delivery channels with SMS and email facilities, and support of transaction status tracking.

2.3 WEB BASED TECHNOLOGY

GRIP software is built on open source technology, with full security frame work, and working with English/Hindi language option mode. The software supports with encrypted user password. For change of password for application user, it is facilitated with One Time Password (OTP) sending to registered mail-id. Application is interoperable and data exchangeable.

3.   AUDIT PROCESS FLOW AND SUPPORT TASKS

3.1   AUDIT PROCESS FLOW

Software supports the sequence activities of audit life cycle. Using the software, the following activities can be taken up

- Formation of Audit Team/Party

- Creation of users of Auditors, Reviewer and Auditee

- Scheduling of Field Audit with respective audit teams

- Capturing of Entry & Exit Conference /Meeting

- Recording of Audit Findings/Observation with online uploaded document(s)

- Approval of Audit Para as per workflow at different stages

- Generation of Audit Report and sending it online to Auditee Facilitate CCA office to use CMS to upload contents on portal.

- Online Submission of Reply/Response by Auditee and follow up on individual pending audit observation.

- Captures complete process of the audit by seamless mapping the processes of Auditor/Auditee and ensures reply and follow up instantaneously and amenable for analysis and monitoring.

PROCESS FLOW USING GRIP
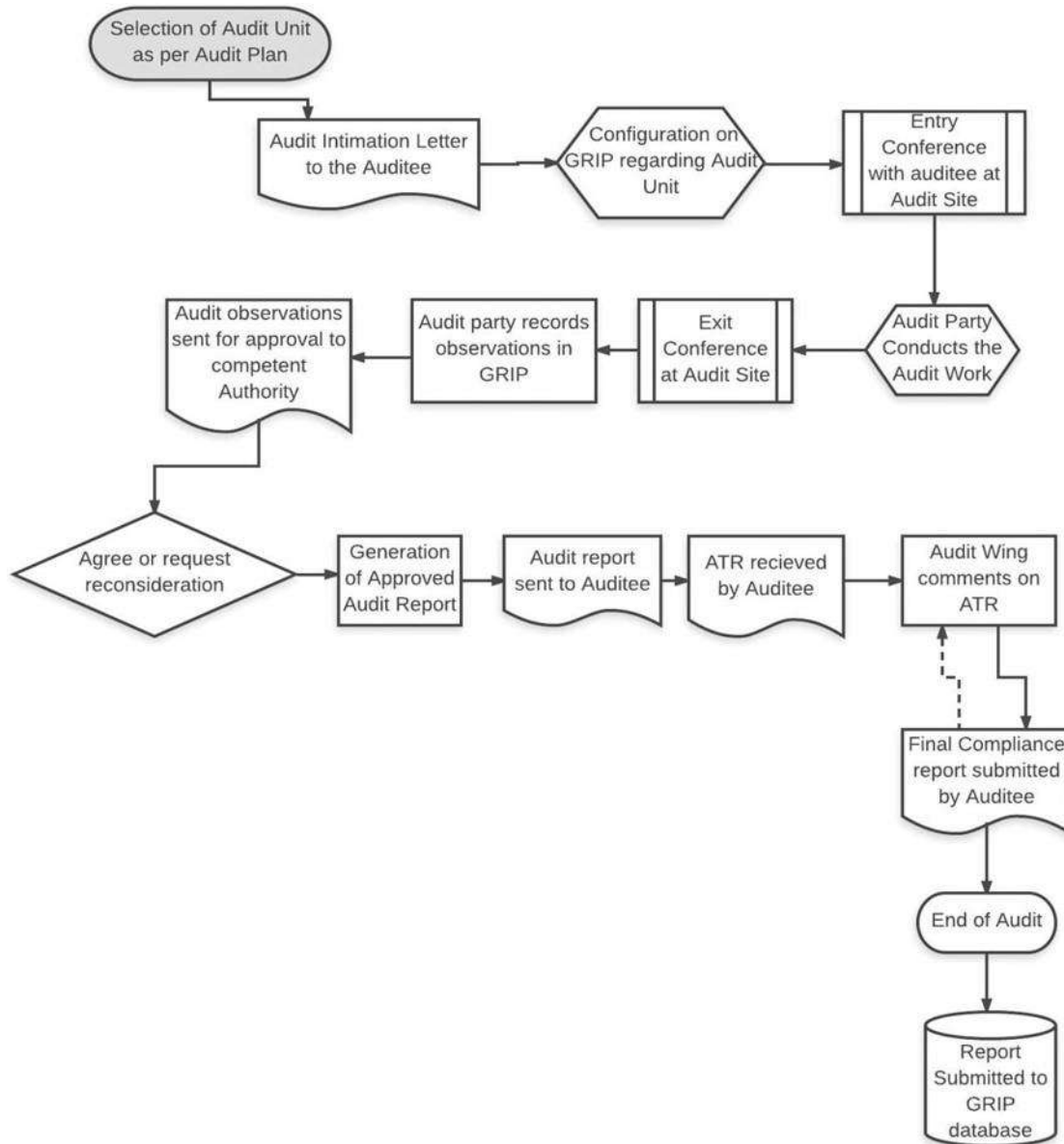
GRIP AUDIT PROCESS FLOW ACTIVITIES USING ADMIN USER

GRIP supports the following activities through Admin user of the software.

CATEGORIES/SUB CATEGORIES

Enables qualitative tags for audit observations into categories/sub categories

DYNAMIC FORM DESIGNER

Dynamic Form Designer allows designing the forms for Case Record and Fact Sheet easily and dynamically keying in the formulae's and necessary fields with required validations.

MANAGES AUDIT TEAM & AUDIT SCHEDULE

Enables easy constitution & managing of audit teams and preparing the audit schedule by assigning team to an Auditee.

EASY COMMUNICATION & FOLLOW-UP

Captures complete process of the audit and enables reply and follow up instantaneously and amenable for analysis and monitoring.

Defining various categories and sub categories in which auditor would categorize the recorded observations.

Defining dynamic forms i.e. case sheet and fact sheet to capture Auditor's input as per the defined parameters. Fact sheet basically defines the parameters/fields on which Auditor records the observations against each category and sub category. For each category and sub category there can be only one form with many fields which audit department can create which would be used for recording certain figures/data.

Audit scheduler for formation of Audit Team, defines audit schedule by assigning Auditee to the audit team.

Facilitates configuring the notification for SMS/Email based alerts by defining the various trigger points on which department wish to be notified. The notification could be configured depending on the requirement for individual modules like Process flow, Audit schedule, etc. Depending on stakeholder level of roles, in accessing and using application, user account is created through admin user, with appropriate privileges.

- Administrator can create Audit Team with selection of desired members.

- One Member can be part of the multiple teams.

- User is created for each member/designation which is uniquely identified as per valid e- mail id. For any Audit team, each member is given user account, and he/she will perform task as assigned by the team.

- Defining the process flow which would be followed during the audit process, defining tasks and its mapping i.e., flow of movement of task from one designation to another and finally freezing the process flow.

3.3 AUDIT SUPPORT TASKS

In order to enable audit process through GRIP different tasks are made available in the software at the bottom line of audit processing.

After team formation for conducting internal audit at field in auditee place, the following tasks are taken through GRIP software modules.

- Entry conference with auditee

- Recording of Audit Observation

- Uploading evidences

- Exit conference with auditee

- Competent Authority Approve Audit Paras

- Generation of audit Report

- Intimation to Auditee

- Action Taken Report (ATR) submission by Auditee

- Follow-up of Audit observation

3.4 RECORD OF ENTRY CONFERENCE WITH AUDITEE

- Facilitates Auditor team member to record Entry Conference at auditee Office during the field visit.

- Date of Meeting is specified, the Date on which entry meeting conducted.

- Participants can be selected among the list of configured participants as per designation.

- Attach Files option to attach any supportive Files (PDF, JPG)

- Agenda's Text area is provisioned to record the agenda points agreed upon between auditee and audit party.

3.5   RECORD OF AUDIT OBSERVATIONS

- Audit Observation can be recorded in the Editor provided with the software module.

- Supporting documents can be uploaded via Attach Files.

- Default Consequences and Recommendation will be shown as already recorded in the application. These can be further changed as per the requirement

3.6   RECORD OF EXIT CONFERENCE

- Facilitates auditor team to record, the exit conference once field audit is completed.

- Exit date of meeting can be recorded.

- Various files can be attached using attach files link.

- Discussion points can be recorded.

3.7   VERIFY DRAFT AUDIT PARAS

- It facilitates Sr Audit member, in the team to verify audit paras recorded by junior team member.

- It facilitates verifier to review every observation and classify every observation into Accept, Reject and Discard. The verifier can operate and Accept for satisfactorily recorded observations.

- Reject if verifier is not satisfied and observations are to be updated.

- Discard if the observation is recorded by mistake and the observation will not reflect in the report.

3.8   RESPONSE ON UNVERIFIED OBSERVATION

- Facilitate   the concerned Audit Team member to make   necessary changes, on rejected observations by the verifier as per workflow.

- After making changes the observation is re-submitted to verifier.

- Verifier again verifies the proposed changes, if satisfied then forward to approver.

3.9   DRAFT PARA APPROVAL BY ACA, CA, CCA

•   Facilitates approver to approve the Audit Para s after recording its own comment.

•   The approver can ACCEPT or REJECT or DISCARD depending on draft Para Analysis

3.10   RESPONSE ON UNAPPROVED OBSERVATION

•   Facilitates the concerned Audit Team member in making the necessary changes once the observations have been rejected by the Approver.

•   Provision to make copy of previous member remarks as it is facility to view the upload supportive document.

3.11   RESPONSE ON UNAPPROVED OBSERVATION BY ACA

•   Facilitates ACA in making the necessary changes once the observations have been rejected either by CCA or CA.

3.12   AUDIT REPORT GENERATION

•   The software facilitates to generate recorded audit paras in configured format with attachable document provision for file format pdf / jpeg.

3.13   PROVISION FOR AUDITEE RESPONSE ON AUDIT REPORT

•   Facilitates Auditee to prepare response against each Audit Para in the text editor area provided against each observation.

•   Provision is also given in the software module, attaching supportive documents to substantiate the response.

•   Review on follow up observations by Auditee is also provisioned.

4.   COMMUNICATION SUPPORT AND REPORTS

4.1   COMMUNICATION SUPPORT

Facilitates configuring the notification for SMS/Email based alerts by defining the various trigger points on which department wish to be notified. The notification could be configured depending on the requirement for individual modules like Process flow, Audit schedule, etc.

4.2   REPORTS

Reports can be generated on Audit Team Schedule, Office wise pending observation, category and sub category wise list of pending Observations. These reports can be generated in Excel and PDF formats. Various Reports such as Resource Management Dashboard and Observation Dashboard for Analysis purposes are also provisioned.

5.   ADVANTAGES OF GRIP

• Migrating Internal Audit process from manual system to on line ICT based GRIP software addresses many problems in conventional system.

• GRIP curtails time and enables speedy review of Audit reports, and timely corrective actions will take place for audit objections.

• Fixing accountability is effective and quick follow up action for audit objections.

• Committing mistakes is reduced in audit process and cross check across the offices is easily possible.

• Reduces paper-based process and enables for good governance.

(Information about the updated version of GRIP is attached as Annexure –II)

1. Expand acronym G R I P and mention the purpose of GRIP.

2. Mention any five objectives to use GRIP for Internal Audit.

3. Mention technology features of GRIP

4. Mention internal Audit process flow using GRIP

5. What activities can be taken up with admin user of GRIP to support internal audit?

6. List internal audit support tasks by GRIP - at field level at auditee office.

7.   Mention feature of record of audit observations with GRIP software.

_____

_____

_____

8.   Provision for Draft Para approval by------, ----------,   is given in software.

_____

_____

_____

9.   What provision is given in the software for Auditee response on Audit report?

_____

_____

_____

10.   List benefits for internal audit with GRIP.

_____

_____

_____

Unit - 3

Basic Concepts of Internal Audit: Definition, types and Code of Ethics for Internal Auditors

Index	
Para No.	**Title**
1	Definitions
2	Internal Audit & External Audit
3.1	Types of Internal Audit
3.2	Regularity Audit
3.3	Proprietary Audit
3.4	Performance Audit
3.5	Risk Based Audit Approach
4.1	Codes of Ethical Conduct for Internal Auditing Professionals
4.2	Typical Components of a code of Ethical Conduct
5	Internal Audit Charter

Learning Outcomes:

- ♦ Definition of Internal Audit

- ♦ Principles of Internal Audit

- ♦ Types of Internal Audit

- ♦ Code of Ethics for Internal Audit Professionals.

1. DEFINITIONS

The Institute of Internal Auditors (IIA) defines Internal Audit as follows: "Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes".

As per the CGA's Internal Audit Handbook, Internal Audit can be explained as an appraisal activity, which is established or provided as an assurance service to the Central Civil Ministries/Departments. Its functions include examining, evaluating and monitoring the adequacy of internal control. In other words, internal audit is a function aimed at evaluating the adequacy and effectiveness of risk management, governance and control processes thereby adding value and improving an organization's operations. In the context of Government and public sector functioning, serving "public interest" must be the overriding objective guiding these operations.

Guideline No. 8 of the Internal Audit Guidelines (CGA's Internal Audit Handbook) stated that: '***Based on the Engagement Objectives, the Internal Audit Wing (IAW) performs Assurance Services to meet Audit objectives and advisory services. These services are performed by using the appropriate frameworks and procedures.***'

Assurance services are the internal auditor's objective assessment of evidence to provide an independent opinion or conclusion regarding processes, systems or mechanisms put in place by the Executive to ensure achievement of objectives and accomplishment of goals. Advisory services, on the other hand, are focused on positive recommendations to improve performance and/or controls and are generally performed at the specific request of the government agency. The internal auditors should maintain objectivity and not assume responsibility of Ministry officials.

The Internal Audit Wings (IAWs) are expected to articulate their Mission and aspire to accomplish within the Ministry '**to enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight'.**

The Core Principles, taken as a whole, articulate the effectiveness of internal audit. For an Internal Audit Wing to be considered effective, all principles should be present and operate effectively. The core principles have been enunciated in the Guidelines for internal audit of Central Civil Ministries/Departments.

IIA's Core Principles for the Professional* Practice of Internal Auditing

For an Internal Audit Wing (IAW) to be considered effective, all these principles should be present and operate effectively:

- ∗ Demonstrates integrity

- ∗ Demonstrates competence and due professional care

* Is objective and free from undue influence (independent)

* Aligns with the strategies, objectives, and risks of the programs

* Is appropriately positioned and adequately resourced

* Demonstrates quality and continuous improvement

* Communicates effectively

* Provides risk-based assurance

* Is insightful, proactive, and future-focused

* Promotes organizational improvement

It may be noted that use of the word "professional" includes the "function" of internal audit viewed from the perspective of Civil Ministries.

Thus, internal audit focuses on whether Governance, Risk management and control processes provide reasonable assurance that

* Significant financial, managerial and operating information is accurate, reliable and timely;

* Resources are acquired economically and used efficiently;

* Assets are safeguarded;

* Actions of the Ministry are in compliance with policies, procedures, contracts, applicable laws and regulations; and

* Significant plans and objectives of programs and schemes will be achieved.

2.   Internal audit and External audit

The internal and external audits, though appear to be similar in the nature of audit, there are some differences. A few of them are mentioned below.

Internal audit	External audit
Internal auditors are generally the employees of the Ministry/Department or have been engaged by the Ministry/Department for this purpose. Here they are responsible and accountable to the Ministry/ Department. They submit their reports to the Ministry/Department for their use to provide assistance or advice. Functions of internal audit include examining and evaluating the adequacy of internal controls to achieve the objectives of the Ministry.	External auditors are generally independent from the Ministry/Department. In respect of Ministries/ Departments of Government of India, CAG does this work. Reports of the external auditors are used by the stakeholders of the audited entity. (E.g.: Parliament, Legislature, publicin general). External auditors also examine the financial statements and express an opinion whether they represent a true and fair picture of the state of affairs of the audited entity, wherever required.

3.1 TYPES OF INTERNAL AUDIT

Based on the objective of audit, internal audit is primarily of three types, (i) Compliance audit, (ii) Propriety audit and (iii) Performance audit. Internal audit may be of any one or acombination of more than one type depending on the audit objectives and scope of audit.
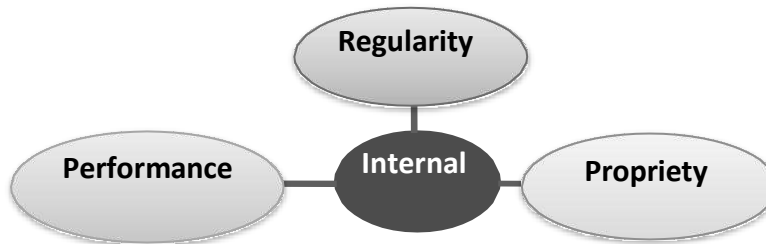
3.2 REGULARITY AUDIT

- Regularity or Compliance Audit primarily focuses on verifying that the expenditure conforms to the laws, rules, regulations and orders governing the powers to incur and sanction expenditure and the procedure to be followed by government servants in dealing with government transactions. Such audits also verify whether the rules and orders regulating the conditions of service, pay and allowances and pensions of Government servants are adhered to.

3.3 PROPRIETY AUDIT

- During Propriety Audit, the scope of audit extends beyond regularity audit to identify cases of improper expenditure or waste of public money, even if such expenditure is covered under existing rules and regulations; and no obvious irregularity may appear to have been committed. Propriety Audit 'extends beyond the formality of the expenditure to its wisdom, faithfulness and economy'.

- As stated in the CGA's Internal Audit Handbook, Financial audit is conducted as a part of Propriety audit. Review of Financial transactions always has a test of propriety, to identify cases of improper or infructuous expenditures which may have been incurred in conformity with existing rules and regulations. It can take form of (A) Grant and contract audits or (B) Fraud and financial irregularity audit depending on requirement.

- **Grant and contract audit:** Grant and contract audits are designed to evaluate complaints with the conditions of grants, the contracting process and third-party contractual performance.

- **Fraud and financial irregularity audit:** Fraud and financial irregularity audits are designed to verify the existence and magnitude of suspected fraud and financial irregularities. Internal audit may be requested to conduct a fraud and financial irregularity audit as a result of discovery or suspicion of a fraud or financial irregularity having taken place.

3.4 PERFORMANCE AUDIT

- The focus of Performance Audit is to ascertain whether the stated objectives of Ministry/Department have been achieved with due regard to economy (The expenditure incurred was not in excess of the requirement), efficiency (Output has been achieved with the minimum amount of inputs or that maximum possible output has been

achieved for given amount of inputs), and effectiveness (The expenditure incurred was resulted in achievement of the intended objective). This audit examines the relationship between inputs, outputs and outcomes in development schemes.

- Such audits provide information to improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability.

3.5   RISK BASED AUDIT APPROACH

- "Risk based Auditing" is an approach to internal audit. It focuses on the Ministry's response to the risks it faces in achieving its goals and objectives. The context for audits is thus provided by the Department's objectives, the associated risks and the risk management process rather than on "controls" and deviations there from. The role of the internal auditor too shifts from an examination of compliance with controls to review of the risk management processes.

- In the absence of an explicit recognition of risks and of well-designed and sufficiently robust risk management processes embedded within government systems, it would not be possible yet for Internal Audit to rely on the Department's own view of risks while determining the scope of an audit engagement. A pragmatic approach requires that Internal Audit, in conjunction with Ministry undertakes the risk assessment exercise and accordingly draws up its audit plan. Over time, it should be possible to place greater reliance on the risk assessment done by Departments and the risk- control matrices developed by them.

- The CGA's Handbook on Internal Audit defined the risk as 'the possibility of an event occurring that will have an adverse impact on the achievement of organization's objectives.   Thus, every risk has two components, namely (i) Likelihood of occurrence and (ii) impact of occurrence.

- Risk analysis needs the following three questions to be asked.

    ◊   What can go wrong? (Risk identification)

    ◊   What is the probability of it going wrong? (Risk likelihood)

    ◊   What are the possible consequences? (Risk impact)

4.1   CODES OF ETHICAL CONDUCT FOR INTERNAL AUDITING PROFESSIONALS

INTRODUCTION:

The primary purpose of a code of ethical conduct for a professional organization is to promote ethical culture among professionals who serve others. A code of ethics is necessary and appropriate for the profession of internal auditing, founded as it is on the trust placed in its objective assurance about governance, risk management and control.

The additional functions of a code of ethical conduct for a professional organization include

- Communicating acceptable values to all members,

- Establishing objective standards against which individuals can measure their own performance; and

- Communicating the Ministry's values to outsiders.

The mere existence of a code of ethical conduct does not ensure that its principles are followed or that those outside the Ministry will believe that it is trustworthy. A measure of the cohesion and professionalism of a Ministry is the degree of voluntary compliance with its adopted code. A code of ethical conduct worded so as to reduce the likelihood of members being sued for substandard work would not earn the confidence of the public. A code of ethical conduct can help establish minimum standards of competence, but it is impossible to require equality of competence by all members of a profession. To be effective, the code must provide for disciplinary action for violators.

4.2   TYPICAL COMPONENTS OF A CODE OF ETHICAL CONDUCT

A code of ethical conduct for professionals should contain at least the following:

i)   Integrity: A refusal to compromise professional values for personal gain. Another facet of integrity is performance of professional duties in accordance with relevant laws. The integrity of internal auditors establishes trust and thus provides the basis for reliance on their judgment.

 The Internal Auditors

- ⇒   Shall perform their work with honesty, diligence and responsibility.

- ⇒   Shall observe the Law and make disclosures expected by the Law and the profession.

- ⇒   Shall not knowingly be a party to any illegal activity, or engage in acts that are discreditable to the profession of internal auditing or to the organization.

- ⇒   Shall respect and contribute to the legitimate and ethical objectives of the organization

ii)   Objectivity: A commitment to providing stakeholders with unbiased information. Another facet of objectivity is a commitment to independence from conflicts of economic or professional interest. Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the activity or process being examined.

Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgments.

- ⇒   Shall not participate in any activity or relationship that may impair or be presumed to impair their unbiased assessment. This participation includes those activities or relationships that may be in conflict with the interests of the organization.

- ⇒   Shall not accept anything that may impair or be presumed to impair their professional judgment.

- ⇒   Shall disclose all material facts known to them that, if not disclosed, may distort the reporting of activities under review.

For example, if Ministry overrides of an important control and creates exposure to a material risk, the internal auditor is ethically obligated to report the matter to senior officials charged with performing the governance function.

iii)   Conflict of Interest Policy: A conflict of interest policy should

    a)   Prohibit the transfer of benefits between a Government official and those with whom the Ministry deals;

    b)   Prohibit the use of official information for private gain.

iv)   Confidentiality: A refusal to use organizational information for private gain. Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.

    ⇒   Shall be prudent in the use and protection of information acquired in the course of their duties.

    ⇒   Shall not use information for any personal gain or in any manner that would be contrary to the Law or detrimental to the legitimate and ethical objectivities of the organization.

v)   Competency: A commitment to acquiring and maintaining an appropriate level of knowledge and skill. Internal auditors apply the knowledge, skills and experience needed in the performance of internal audit services.

    ⇒   Shall engage only in those services for which they have the necessary knowledge, skills and experience.

    ⇒   Shall perform internal audit services in accordance with the International Standards for the professional practice on Internal Auditing.

    ⇒   Shall continuously improve their proficiency and the effectiveness and quality of their services.

The Code of Ethics applies to both entities and individuals that perform internal audit services. The Guidelines (2) to (5) on Internal Audit in the CGA's Handbook on Internal Audit stipulate the following.

    ⇒   The distinguishing mark of a Government Internal Auditor is acceptance of responsibility to serve the public interest. In this regard, the Government of India rules and ethical guidelines issued by the CVC must be adhered to by the internal auditor.

    ⇒   The internal audit activity must be independent and internal auditors must be objective in performing their work[1].

    ⇒   Engagements must be performed with proficiency and due professional care.

    ⇒   Auditors must use professional judgment in planning and performing audits, advisory engagements and in reporting the results. Auditors must document significant decisions that affect audit objectives, scope and methodology; findings; conclusions and recommendations resulting from professional judgment.

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[1]IIA Standard.

5.   INTERNAL AUDIT CHARTER

The Internal Audit Charter is the reference point for internal audit activity at the Ministry as it defines the purpose, authority and responsibility. The charter is reference to the IIA Definition of Internal Auditing, the Code of Ethics and the Standards (through the CGA Internal Audit policies contained in the Generic Audit Manual) thereby aligning the Ministry's Internal Audit Wing with global standards and best practices.

The Internal Audit Charter establishes the position of the IAW within the Ministry's organization, including the nature of the **Pr. CCA/CCA/CAs (in their capacity as CAE)** relationship with the Secretary and Audit Committee, authorizes access to records, personnel and physical properties relevant to the performance of engagements and defines the scope of the internal audit engagement.

The CAE prepares the Ministry's Audit Plan in accordance with the guidelines/framework contained in Generic Internal Audit Manual issued by O/o CGA. The nature of assurance services and consulting services provided to the Ministry must be defined in the internal audit plan and should be within the Ministry's Internal Audit Wing's capability as assessed using the Internal Audit Capability Maturity Model (IA - CM).

The CAE should present to Audit Committee an annual review of the Ministry's Internal Audit Plan and whether any changes are required to it. Also, an assessment of the Internal Audit Wing's (IAWs) current status on the Internal Audit – Capability Maturity Model (IA-CM) is also required.

WORKBOOK (Session-3)

1.   What is the primary function of Internal Audit?

2.   How does the IIA define internal audit?

3.   What are the different types of internal audit?

4.   What are the typical components of a code of ethical conduct?

5.   Internal Audit provides reasonable assurance that:

1. _____ is accurate, reliable and timely

2. _____ are acquired economically

3. _____ are safeguarded

4. Compliance with _____ and _____

5. _____ will be achieved.

6.   Name the three E's of performance audit

_____

_____

_____

7.   Financial audit provides reasonable assurance that financial statements of the ministry Present a _____

and _____ view.

8.   How do you understand the words 'risk 'and 'risk analysis'?

_____

_____

_____

9.   In   risk-based   auditing,   the   role   of   internal   auditor   shifts from   examination of

_____ to review of the risk management process

_____

_____

_____

10.   The primary purpose of a code of ethical conduct is to

_____

_____

_____

11.   How many core principles are there for the professional practice of internal auditing? Name any five.

_____

_____

_____

Unit - 4

Introduction to Internal Auditing Guidelines/Standards

Index	
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Guideline-31	Communicating the Results of the Engagement
Guideline-32	Monitoring Progress and Communicating Acceptance of Risks

Learning Outcomes:

Application of:

♦   International Standards for the Professional Practice of Internal Audit.

♦   IIA Standards on Internal Audit.

♦   Guidelines on Internal Audit of Central Civil Ministries

♦   Internal Audit Standards of ICAI.

After learning the basics of Internal Audit in Unit 2, let us have a look at the standards and guidelines to be followed for conducting Internal Audit in Ministry of Rural Development.

An Overview of the International Standards for the Professional Practice of Internal Auditing (ISPPA)

The broad schema/ layout of ISPPA also known as the Standards helps in a better understanding especially for new auditors as it gives an overview of what is internal audit, the different phases of the internal audit process (also known as Internal Audit cycle) and the minimum performance levels in the activities therein to qualify as effective Internal Audit. By grasping the broad schema, the new internal auditor would be able to form a holistic view and comprehend as to how his work fits into the whole piece.

Internal audit as defined by The Institute of Internal Auditors (The IIA) lays down the boundaries on what can be considered as a legitimate internal audit activity, to include risk, control and governance processes only. It lays down that the fundamental objective of internal audit is to help in improving the Ministry's operations by providing an assurance (or lack of it) that the activities are being carried out in a manner as envisaged by those in charge of Governance, i.e. the Secretary and the Ministry. In addition, the internal auditors may perform an advisory role to improve opportunities for the program/scheme management in meeting business objectives. The output of the Assurance activity is an internal audit report that contains an opinion on the area of the program/scheme under review and of the Advisory activity the output is usually an insight or advice.

The Definition of Internal Audit is elaborated through the Standards, which are of two types, viz. Attribute and Performance Standards. The Attribute Standards lay down the qualities that an individual internal auditor should display and what the internal audit function (IAW) should display as a whole. Individual auditors must display PROFICIENCY and being OBJECTIVE while carrying out their work. The Internal Audit Wing (IAW) has an Audit Charter so that all within the Program/ Scheme know the role, responsibility and authority of internal audit. Also the IAW should have a well-defined and operational Quality Assurance and Improvement

Program (QAIP) which needs to be well publicized so as to foster trust and reliability of the internal audit reports and other communication issued by IAW.

The Performance Standards are a basis against which the internal audit operations can be measured. They broadly fall in the below three types:

1.   *Standard for managing the internal audit activity:* This is the responsibility area of the Head of Internal audit and a basis to measure his/her performance.

2. *Standard on the nature of work of internal audit:* This clearly defines Risk, Control and Governance processes. Anything beyond this is outside the ambit of internal audit.

3. The next few standards define the minimum set of activities within the four stages of the audit cycle, viz. *Planning, Performance, Communicating and Monitoring*. For each of these phases there are short standards that briefly state as to how these minimum activities should be performed.

The Standards are the minimum requirements of performance. For e.g. one of the standards requires that the Head of Internal Audit reports to the Audit Committee every year, wherein he/she discloses whether a Quality Assessment was carried out on internal audit and what were the main findings.

Periodic reporting on Quality Assessment improves trust and confidence the executive management can place on internal audit. The IIA has guidance in the manner in which Quality Assessment on internal audit is to be carried out by assessing the level of compliance of the internal audit activities against each standard.

In addition to the Standards, The IIA takes out position papers, and one of the most well-read position papers is titled 'T*he three lines of defense in effective risk management and control*.' The first line of defense in risk management is management control; various risk control and compliance oversight functions established by management are the second line; and independent assurance, i.e. Internal Audit is the third line of defense.

The Definition of Internal Audit, the Standards, Guidance, Position papers is part of the IIA Professional Practices Framework (IPPF). While IIA's International Standards is essential for meeting the responsibilities of internal auditors and internal audit, the other elements of IPPF create a framework to support this responsibility. The IPPF is in two parts, viz. those elements that require mandatory compliance and those of non-mandatory compliance.

Suggested readings:

IIA International Professional Practices Framework

IIA International Standards for the Professional Practice of Internal Audit.

1. Introduction to the Internal Audit Guidelines

The Internal Audit guidelines for Internal Auditing at Central Civil Ministries/Departments of Government of India are discussed in detail in the Internal Audit Handbook of the CGA. There are 32 guidelines in four sections to ensure effective internal audit. By reading these guidelines, any internal auditor can, in a few days, form a clear insight of what is expected from him/her. The guidelines are to be read along with the theoretical concepts and explanations contained in the Generic Internal Audit Manual.

The potential value that effective internal audit brings to Central Civil Ministries/Departments is significant considering the large annual budgetary outlay that these Ministries collectively expend on a yearly basis. Even a small improvement in achieving objectives can provide a significant yearly impact. Effective performance and governance is clearly a priority at these Ministries and internal audit needs to play its assurance role effectively. Hence, the effectiveness of these internal audit guidelines in promoting effective internal auditing should be tested continuously and changes carried out periodically, as and when required.

Section-1

Introduction to Internal Audit Guidelines (IAG) for effective internal auditing

The guidelines are based on expectations by stakeholders of Government Internal Auditing in India, are aligned with international standards in internal auditing issued by 'The Institute of Internal Auditors' (IIA) as well as benchmarked with global best practices followed by Government internal auditors in other countries.

The principal stakeholder of Government audit is the general public. The current times encourage innovative disruption in order to deliver order of magnitude results. Given the current challenges facing Central Civil Ministries/Departments and their programs along with the heightened expectations of the general public, the oversight provided through auditing is more critical than ever. Effective Government internal auditing provides objective analysis and information required to make the decisions necessary to help create a better future for the public by reducing the risks in achieving the Government's objectives.

The overarching objective of the IAGs is to decrease Audit Risk in internal audit at Ministries both at an engagement level and whilst providing an overall opinion on a particular Ministry's portfolio of significant risks. Compliance with these internal audit guidelines is hence mandatory for meeting the expectations from the Pr. CCA/CCA/CA in their capacity as CAE and the Internal Audit Wings at Central Civil Ministries.

2.1 Based on their applicability, the types of IAGs are as follows:

a. General guidelines create a platform for providing objective and risk based assurance.

b. CGA level guidelines promote effective audit in Central Civil Ministries.

c. Ministry level guidelines assist the Pr. CCA/CCA/CA in their capacity as CAE in managing the internal audit activity at individual Ministries.

d. Engagement level guidelines minimize audit risk while performing the engagement.

2.2 The purpose of the internal audit guidelines is to:

a. Guide the Internal Audit Wings (IAWs) in carrying out an effective internal audit through an objective risk-based assurance in the areas of Governance, Risk Management and Control processes.

b. To provide a set of best practices which, when followed, mitigate Audit Risk to within a tolerable level as specified by the Ministry's Audit Committee. Audit risk is the risk of giving false positives (i.e. giving a positive assurance over a subject matter when there is a substantial issue) or a false negative (where an adverse opinion is given over a subject matter while the actual conditions are satisfactory).

c. Establish the basis for the evaluation of internal audit performance.

d. Foster improved organizational processes and operations.

The IAGs are a set of principles-based, mandatory requirements consisting of statements of core requirements for the functional practice of internal auditing at the Central Civil Ministries/Departments and for evaluating the effectiveness of performance.

The IAGs employ terms as defined specifically in the Glossary to the IIA Standards. To understand and apply the IAGs correctly, it is necessary to consider the specific meanings from the Glossary. Furthermore, the IAGs use the word "must" to specify an unconditional requirement and the word "should" where conformance is expected unless, when applying functional judgment, circumstances justify deviation.

The IAGs apply to individual internal auditors and the internal audit activity. All internal auditors are accountable for conforming with the IAG related to individual objectivity, proficiency, and due functional care and the standards relevant to the performance of their job responsibilities. Pr. CCA/CCA/CA in their capacity as CAEs are additionally accountable for the internal audit activity's overall conformance with the Internal Audit Guidelines.

In the IAGs the word Program is used to denote programs, schemes, departments, units, processes, structures, PSUs and any other auditable unit at the Ministry which is the subject matter under Internal Audit.

Section-2

General Guidelines

This Section establishes General Guidelines to be followed in internal audit of Central Civil Ministries/Departments and related organizations of the Government of India. These guidelines are Audit Risk minimization measures as they lay down a solid foundation for objective and risk based assurance services. In order that these guidelines are current to the present environment the Controller General of Accounts (CGA) regularly reviews the veracity of these internal audit guidelines in promoting effective internal auditing, based on stakeholder surveys at Central Civil Ministries. The CGA also benchmarks these guidelines with changes in global internal audit standards that promote effective internal auditing.

Guideline Number	Guideline
1	**Internal Audit Principles for Effective Auditing**
2	**Code of Conduct and Ethical Guidelines in Government Auditing**
3	**Independence and Objectivity**
4	**Proficiency and Due Professional Care**
5	**Use of Professional Judgement**
6	**Definition of Internal Audit**
7	**Nature of Work**
8	**Types of Services**

Guideline No. 1

INTERNAL AUDITING PRINCIPLES FOR EFFECTIVE GOVERNMENT AUDITING IN CIVIL MINISTRIES

The Controller General of Accounts (CGA) issues Internal Audit Guidelines for effective internal auditing, the compliance of which is mandatory. These Guidelines are based on internal auditing principles which are framed and updated by the CGA. These principles must be adhered to in all aspects of internal auditing.

IIA's Core Principles for the Professional2 Practice of Internal Auditing

The core principles taken as a whole, articulate to effective internal audit. For an internal audit wing (IAW) to be considered effective, all principles should be present and operating effectively. Achievement of the core principles may vary from Ministry to Ministry, but failure to achieve any one of the principles would imply that an internal audit activity was not as effective as it could be in achieving internal audit's mission.

These core principles are as follows:

◊ Demonstrates integrity

◊ Demonstrates competence and due professional care

◊ Is objective and free from undue influence (independent)

◊ Aligns with the strategies, objectives, and risks of the programmes

◊   Is appropriately positioned and adequately resourced

◊   Demonstrates quality and continuous improvement

◊   Communicates effectively

◊   Provides risk-based assurance

◊   Is insightful, proactive, and future-focused

◊   Promotes organizational improvement

In order to conform to the principles, some guidelines have been formulated which are being specified below.

It may be noted that use of the word "professional" includes the "function" of internal audit viewed from the perspective of Civil Ministries.

Guideline No. 2

CODE OF CONDUCT AND ETHICAL GUIDELINES IN GOVERNMENT AUDITING

The distinguishing mark of a Government Internal Auditor is acceptance of responsibility to serve the public interest. In this regard, the Government of India rules and ethical guidelines issued by the CVC must be adhered to by the internal auditor.

The public interest is defined as the collective well-being of the community of people and its entities the auditors serve. Observing integrity, objectivity, and independence in discharging their functional responsibilities assists auditors in meeting the principle of serving the public interest and honoring the public trust. The principle of the public interest is fundamental to the responsibilities of auditors and critical in the Government environment. The ethical principles that guide the work of auditors who conduct audits are a) the public interest; b) integrity; c) objectivity; d) proper use of Government information, resources, and positions; and e) professional behavior[3].

The Government of India through the various rules and guidelines discusses the behavioral norms for Government officials and establishes an expectation that Government officials would carry out public functions ethically. A periodic evaluation should be made of the ethics programme at the Internal Audit Wings and a yearly declaration of its adherence should be taken from individual Internal Auditors.

Guideline No. 3

INDEPENDENCE and OBJECTIVITY

The internal audit activity must be independent and internal auditors must be objective in performing their work[4]. The CGA's Office issues guidance on independence and objectivity, compliance of which is mandatory.

The focus is on the Pr. CCA/CCA/CA and Internal Audit Wings (IAWs) having the organizational independence to be able to carry out the engagements in an unfettered manner and ensure that the internal auditor maintains individual objectivity whereby he/she has an impartial, unbiased attitude and avoid any conflict of interest. Impairments to independence and objectivity can be either internal or external impairments. Impairment to organizational independence and individual objectivity may include, but is not limited to, personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations, such as funding[5].

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[3]Adapted from US Government Accountability Office (GAO), Yellow Book IIA Standard.

[4]Also Organizational independence and individual objectivity should be in fact and appearance.

[5]Interpretation to IIA Standard

Independence is the freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the chief audit executive has direct and unrestricted access to senior management and the board.

This can be achieved through a dual-reporting relationship. Threats to independence must be managed at the individual auditor, engagement, functional, and organizational levels.

Objectivity is an unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditor don't subordinate their judgement on audit matters to others. Threats to objectivity must be managed at the individual auditor, engagement, functional, and organizational levels.

At the Central Civil Ministries, the Pr. CCA/CCA/CA in their capacity as CAE and IAWs are subject to administrative direction of the Integrated Financial Advisor. Ministries are encouraged to use the IIA's International Standards for the Professional Practice of Internal Auditing in conjunction with CGA's Internal Audit Guidelines (IAG). Under IAG a Ministry's IAW can be presumed to be free from organizational impairments to independence for reporting internally, if the CAE meets ALL of the following criteria

a.   Is accountable to the Secretary

b.   Reports the audit results to both the Secretary and the Audit Committee

c.   Is located outside the staff or line management of the Ministry

d.   Has access to the audit committee

e.   Is sufficiently removed from political pressure to conduct audits and reports findings, conclusions, opinions and conclusions objectively without fear of political reprisal.

Guideline No. 4

PROFICIENCY AND DUE PROFESSIONAL[6] CARE

Engagements must be performed with proficiency and due professional[6] care.

Proficiency is a collective term that refers to the knowledge, skills and other competencies required of internal auditors to effectively carry out their functional responsibilities. It encompasses consideration of current activities, trends, and emerging issues, to enable relevant advice and recommendations.

Internal auditors must exercise due professional care by considering the:

•   Extent of work needed to achieve the engagement's objectives.

•   Relative complexity, materiality, or significance of matters to which assurance procedures are applied.

•   Adequacy and effectiveness of governance, risk management, and control processes.

•   Probability of significant errors, fraud, or non-compliance.

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[6]It may be noted that use of the word "professional" includes the "function" of internal audit viewed from the perspective of Civil Ministries.

- Cost of assurance in relation to potential benefits.

In exercising due professional care, internal auditors must consider the use of technology- based audit and other data analysis techniques.

Internal auditors must be alert to the significant risks that might affect objectives, operations, or resources. However, assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.

Guideline No. 5

USE OF PROFESSIONAL[6] JUDGEMENT

Auditors must use professional judgement in planning and performing audits, advisory engagements and in reporting the results. Auditors must document significant decisions that affect audit objectives, scope and methodology; findings; conclusions and recommendations resulting from professional judgement.

Exercising professional judgement is a basic expectation from an internal auditor and is the result of independence, objectivity, integrity, proficiency and use of professional skepticism. Additionally internal auditors must demonstrate critical thinking capabilities and develop their own point of view on subject matter under audit in order to arrive at professional judgements.

*It may be noted that use of the word "Professional" includes the "function" of internal audit viewed from the perspective of Civil Ministries.

Guideline No. 6

DEFINITION OF INTERNAL AUDIT[7]

Internal Auditing is an independent, objective assurance and advisory activity designed to add value and improve an Organization's Operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of Risk Management, Control, and Governance processes.

The definition of internal auditing is the statement of fundamental purpose, nature and scope of Internal Auditing.

Guideline No.7

NATURE OF WORK[8]

Nature of Work:

The internal audit activity must evaluate and contribute to the improvement of the organization's governance, risk

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[6]It may be noted that use of the word "professional" includes the "function" of internal audit viewed from the perspective of Civil Ministries.

[7]As per IIA Definition.

[8]As per the IPPF. Numerical references (other than Policy numbers) are to the corresponding standards specified by the IPPF. Reference to IIA Standard 2100.

management, and control processes using a systematic, disciplined, and risk- based approach. Internal audit credibility and value are enhanced when auditors are proactive and their evaluations offer new insights and consider future impact.

Governance[9]

The internal audit activity must assess and make appropriate recommendations to improve the organization's governance processes for:

- Making strategic and operational decisions.

- Overseeing risk management, governance and control.

- Promoting appropriate ethics and values within the organization.

- Ensuring effective organizational performance management and accountability.

- Communicating risk and control information to appropriate areas of the organization.

- Coordinating the activities of, and communicating information among, the board, external and internal auditors, other assurance providers, and management.

The internal audit activity must evaluate the design, implementation and effectiveness of the organization's ethics-related objectives, programmes, and activities.

The internal audit activity must assess whether the information technology governance of the organization supports the organization's strategies and objectives.

Risk Management[10]

The internal audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes.

Determining whether risk management processes are effective or not is a judgement resulting from the Internal Auditor's assessment that:

- *Organizational objectives support and align with the organization's mission.*

- *Significant risks are identified and assessed.*

- *Appropriate risk responses are selected that align risks with the organization's risk appetite.*

- *Relevant risk information is captured and communicated in a timely manner across the organization, enabling staff, management, and the board to carry out their responsibilities.*

The Internal Audit activity may gather the information to support this assessment during multiple engagements. The results of these engagements, when viewed together, provide an understanding of the organization's risk management processes and their effectiveness.

Risk management processes are monitored through ongoing management activities, separate evaluations or both.

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[9] As per the IPPF. Numerical references (other than Policy numbers) are to the corresponding standards specified by the IPPF. Reference to IIA Standard 2110.

[10] Reference from IIA Standard 2120.

The internal audit activity must evaluate risk exposures relating to the organization's governance, operations, and information systems regarding the:

- Achievement of the organization's strategic objectives.

- Reliability and integrity of financial and operational information.

- Effectiveness and efficiency of operations and programmes.

- Safeguarding of assets.

- Compliance with laws, regulations, guidelines, procedures, and contracts.

The internal audit activity must evaluate the potential for the occurrence of fraud and how the organization manages fraud risk.

During advisory engagements, internal auditors must address risk consistent with the engagement's objectives and be alert to the existence of other significant risks.

Internal auditors must incorporate knowledge of risks gained from advisory engagements into their evaluation of the organization's risk management processes.

When assisting management in establishing or improving risk management processes, internal auditors must refrain from assuming any management responsibility by actually managing risks.

Control[11]

The internal audit activity must assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

The internal audit activity must evaluate the adequacy and effectiveness of controls in responding to risks within the organization's governance, operations, and information systems regarding the:

- Achievement of the organization's strategic objectives.

- Reliability and integrity of financial and operational information.

- Effectiveness and efficiency of operations and programmes.

- Safeguarding of assets.

- Compliance with laws, regulations, guidelines, procedures, and contracts.

Internal auditors must incorporate knowledge of controls gained from advisory engagements into evaluation of the organization's control processes.

Guideline No.8

TYPES OF SERVICES:

Based on the Engagement Objectives, the Internal Audit Wing (IAW) performs Assurance Services (to meet audit objectives

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[11]Reference from IIA Standards 2130.

and advisory services. These services are performed by using the appropriate frameworks and procedures[12].

Assurance services involve the internal auditor's objective assessment of evidence to provide opinions or conclusions regarding an entity, operation, function, process, system, or other subject matters. The nature and scope of an assurance engagement are determined by the internal auditor. Generally, three parties are participants in assurance services: (1) the person or group directly involved with the entity, operation, function, process, system, or other subject matter — the process owner, (2) the person or group making the assessment — the internal auditor, and (3) the person or group using the assessment — the user.

Advisory services are generally performed at the specific request of Ministry/ Department. The nature and scope of the advisory engagement are subject to agreement with the Ministry/ Department. Advisory services generally involve two parties: (1) the person or group offering the advice — the internal auditor, and (2) the person or group seeking and receiving the advice the Ministry/ Department. When performing advisory services, the internal auditor should maintain objectivity and not assume management responsibility.

The framework/procedures used in internal audit depend upon the objectives to be tested. The audit objectives vary widely and include assessments of programme effectiveness, economy and efficiency, risk and internal control evaluation and compliance review. The procedures used for meeting audit objectives can either be an *examination, review or agreed upon procedures*.

An *examination* is a common procedure followed while assessing internal controls or regulatory compliance to form an opinion on whether the subject matter being audited is in conformance with the criteria in all material respects. In a review of any performance area, the internal auditor does sufficient testing to express a conclusion whether any information came to his/her attention that the subject matter is not based on or in conformity with the criteria.

An *agreed-upon procedure* engagement, the Internal Auditor does not express an opinion or a conclusion but only reports the findings based on the *Agreed-upon procedure* applied. Advisory engagements are usually to decrease risk or improve the opportunities for achieving the programme objectives. Depending upon the engagement objectives, the appropriate methodology and procedures are used.

In performance of assurance services, internal audit is expected to focus on assessing whether governance, risk management and control processes provide reasonable assurance that:

a.   Significant programmes, plans, and business objectives will be achieved;

b.   Financial, managerial, and operating information is accurate, reliable, and timely;

c.   Resources are acquired economically and used efficiently;

d.   Assets are safeguarded; and

e.   The organization is in compliance with guidelines, procedures, contracts, and applicable laws and regulations.

In the process of evaluating whether public agencies are accomplishing their objectives, auditors gather and analyses information and thereafter report on events and developments which affect adequacy and effectiveness of elements of the control systems. These reports provide an opportunity to the Government to initiate necessary remedial measures and take steps for improvement in programme delivery. Further, they provide a reasonable assurance that improprieties have not occurred and if they have, they will be reported for appropriate follow-up action.

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[12]Reference from IIA Standards.

An efficient and effective internal audit practice therefore warrants that the Internal Audit Wings in Ministries have trained and competent staff and supervisory officers. Simultaneously, its independence should be ensured through an internal audit charter and a clear mandate. The quality of internal audit and performance of the Internal Audit Wings should be assured by instituting an effective oversight mechanism in the Ministry by establishing an Audit Committee in the Ministry and through an external review conducted by the office of Controller General of Accounts. Ultimately, the utility of an Internal Audit practice rests on an adequate appreciation of its role by the Government and an effective follow up system to implement the suggestions of Internal Audit.

Section-3

CGA Level Guidelines for managing Government Internal Audit in India

This Section establishes the pre-eminent role of the Controller General of Accounts (CGA) and his/her Office in developing, advocating and promoting the function of Government Internal Audit in the Central Civil Ministries, Government of India.

The Office of the CGA organizes training programmes / issues guidelines from time to time to ensure proficiency in internal auditing, risk management, governance, internal control, information technology audit, data analytics, auditing tools and techniques education, protection against frauds, information security and other knowledge areas.

Guideline Number	Guideline
9	**Managing Government Internal Audit in Central Civil Ministries**
10	**Establishing Best Practices in Government Internal Audit in India**
11	**Supporting engagement of Pr.CCAs/CCAs/CAs with the Audit Committees at Ministries/Departments**
12	**Technical Support (including Data Analytics) to Pr. CCA/CCA/CAs in their capacity as CAEs at Ministries**
13	**Encouraging to maintain Proficiency levels in Internal Audit**

Mission

The stated mission of the Internal Audit Division (IAD) in O/o Controller General of Accounts in the area of internal audit is to provide "dynamic leadership" (initiatives and direction) for the function of Government Internal Auditing in Central Civil Ministries, Government of India and includes

- Advocating and promoting the culture of objective and risk based assurance in Government internal auditing;

- Advocating and promoting the value that internal audit officers add to the Civil Ministries of the Government of India;

- Providing comprehensive functional education, capacity building and development opportunities; internal audit guidelines and other functional practice guidance; and certification programmes;

- Researching, disseminating, and promoting to practitioners and stakeholders knowledge concerning internal auditing and its appropriate role in control, risk management, and governance within the context of the Central Civil Ministries, Government of India;

- Educating Government Internal Audit Officers and other relevant auditees on best practices in Government internal auditing;

- Bringing together internal auditors from all Government bodies in India whether at a Central or State level to share information and experiences.

Guideline No. 9

MANAGING GOVERNMENT INTERNAL AUDIT IN CENTRAL CIVIL MINISTRIES

The Controller General of Accounts exercises an effective oversight over the internal audit activity at the Central Civil Ministries/Departments to ensure that this assurance and advisory activity adds value to the respective Ministries and, on an overall basis, to the accomplishment of the yearly Finance Budget of the Government of India.

The Internal Audit Division (IAD) at CGA office performs all the activities of a Central function for strengthening the internal audit activity of Central Civil Ministries/Departments of Government of India. They provide oversight and support in capacity building, laying down the internal audit guidelines and procedures. The CGA office reviews the performance of Internal Audit Wings by way of obtaining the Annual Reviews from Central Civil Ministries/ Departments. Compiles the information and reports the major findings [Annual Review at a Glance] to the Finance Secretary / Secretary (Expenditure).

Guideline No. 10

ESTABLISHING BEST PRACTICES IN INTERNAL AUDIT

The Controller General of Accounts lays down the best practices for effective internal auditing at the Central Civil Ministries/ Departments of the Government of India including Internal Audit Guidelines (IAG)as laid down in the Generic Internal Audit Manual (GIAM).

The New Charter of duties issued by the Secretary, Department of Expenditure, Ministry of Finance lays down the purpose, authority and responsibility of internal audit at Ministries and compliance of the observations should be ensured for speedy settlement. The New Charter of duties and responsibilities is to be adopted by individual Ministries / Department.

Guideline No. 11

SUPPORTING ENGAGEMENT OF PR.CCAS/CCAS/CAS WITH THE AUDIT COMMITTEES AT MINISTRIES

The Controller General of Accounts plays a coordinating / supporting role in the interaction of Pr.CCAs/CCAs/CAs(I/c.) of line Ministries / Departments with their respective Audit Committees to create a working relationship between the Audit committee and internal audit, so that an objective and risk based assurance is available for decision making.

In its endeavor for strategic and operational excellence, management takes support from internal audit through their audit, analysis and insight. Internal audit has a synergistic relationship with the audit committee which also reviews the governance function. The PR. CCA/CCA/CA in their capacity as CAE and audit committee mutually determines important risks and objectives for the Internal Audit Wings (IAWs). The audit committee is essential for building and supporting an independent, competent and effective internal audit function, while on the other hand, internal audit must deliver high valued internal audit services to the audit committee and programmes to sustain the needed level of support.

Guideline No. 12

TECHNICAL SUPPORT TO Pr. CCA/CCA/CAs IN THEIR CAPACITY AS CAEs AT MINISTRIES

At the Controller General of Accounts office having technical capability to provide guidance and support to the Pr. CCA/CCA/CA in their capacity as CAE and the internal audit activity at the Ministries is delivered through an Internal Audit Centre of Excellence (IA-CoE). This professional guidance will be based on research using surveys, interviews relating to the Ministry/ Area for which the guidance is sought and review of global technical literature for its suitable applicability. The IA-CoE will rapidly develop Data Analytics capabilities and support internal audit of Ministries.

Guideline No. 13

ENCOURAGE TO MAINTAIN PROFICIENCY LEVELS IN INTERNAL AUDIT

Through assessment of the internal audit needs at individual Ministries, the Office of the Controller General of Accounts will review plans that ensure proficiency both at an individual Government internal auditor level and engagement team level through Government Internal Auditor certification programmes and other certifications conducted by its training and development institute, INGAF. Where the CGA concludes that the resource gap is unlikely to get filled with such trainings and the concerned Ministry carries a significant audit risk, the CGA Office would nominate and/or recommend proficient auditors or outsourced service providers to that Ministry's engagement team for period of time that it may deem necessary.

The CGA Office continuously assesses skill needs to consider whether the workforce of internal auditors in the IAWs of Central Civil Ministries/Departments has the necessary competencies that match those that are necessary to fulfill particular audit mandates or scope of audits to be performed. The CGA office has a process for recruitment, hiring, continuous development, assignment and evaluation of staff to maintain a competent workforce.

Section-4

Ministry level Guidelines for managing the Internal Audit Wing

This Section establishes requirements and provides guidance for managing the internal audit wing at the Ministry. It identifies the role of the Pr. CCA/CCA/CA in their capacity as CAE and lays down guidelines for interactions with the Audit Committee, Secretary, Integrated Financial Adviser and senior officials at the Ministry. The Section also lays down the minimum requirements for the effective management of the Internal Audit Wing (IAW).

Guideline Number	Guideline
14	**Role of the Pr. CCA/CCA/CA in their capacity as CAE**
15	**Reporting by the Pr. CCA/CCA/CA in their capacity as CAE to the Secretary, Integrated Financial Advisor and Audit Committee**
16	**Annual Audit plan and 3-year Audit Programme**
17	**Communication and approval of internal audit plans**
18	**Resource management**
19	**Mandatory compliance with internal audit Guidelines**
20	**Receiving Technical Support from IA-CoE in O/o CGA**
21	**Internal Audit of Governance Processes**
22	**Obtaining External Service Providers to support / complement the Internal Audit Activity**
23	**IAW adds value to the Risk Management Process**
24	**Quality Assurance and Improvement Program**

Guideline No. 14

ROLE OF Pr. CCA / CCA/ CA IN THEIR CAPACITY AS CAE

The Pr. CCA/CCA/CA in their capacity as CAE, must effectively manage the Internal Audit Wing to ensure it adds value to the organization.

The Pr. CCA/CCA/CA in their capacity as CAE will perform all the activities as head of the Internal Audit Wing (IAW) at the Ministry. These are planning the internal audit, communication and approval of the plans, resource management, laying down the guidelines and procedures for the IAW, coordination, and reporting to the senior management and audit committee and Quality Assurance.

Adds value: - The internal audit activity adds value, when it considers the Ministry's strategies, objectives and risks, strives to offer ways to evaluate and enhance governance, risk management and control processes and objectively provides relevant assurance.

Guideline No. 15

REPORTING BY THE PR. CCA/CCA/CA IN THEIR CAPACITY AS CAE TO THE SECRETARY, INTEGRATED FINANCIAL ADVISOR and AUDIT COMMITTEE

The Pr. CCA/CCA/CA in their capacity as CAE must report regularly to the Integrated Financial Advisor and periodically to secretary and audit committee on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan and on its conformance with the internal audit guidelines in the CGA Generic Manual. Reporting must also include significant risk and control issues, including fraud risks, governance issues and other matters that require the attention of management /audit committee.

Guideline No. 16

ANNUAL AUDIT PLAN AND 3-YEAR AUDIT POGRAMME

The Pr.CCA/CCA/CA in their capacity as CAE should submit to the audit committee a risk based annual audit plan by January 15 which is consistent with the Ministry's goals. The plan should be updated and kept current during the year for significant risk changes in the business environment and risk exposures. This should be accompanied with an updated three-year rolling Audit Programme to ensure adequate visibility on the coverage of risks in the Audit Universe.

The internal audit activity's plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process.

The chief audit executive must identify and consider the expectations of senior management, the board, and other stakeholders for internal audit opinions and other conclusions[13].

Internal Audit Capability Maturity Model (IA - CM)

The IIA IA-CM assists the Pr. CCA/CCA/CA in their capacity as CAE to conduct a self- assessment of the Ministry's existing internal auditing capabilities on six elements, viz existing services and role of internal audit, existing people management, existing professional practices[14] existing performance management, existing organizational relationships and culture and existing organizational structure. The strategy and action plans to progress to higher maturity levels needs to be incorporated in the Annual Plans of the Internal Audit Wings.

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[13] Reference from IIA Standards 2010.

[14]It may be noted that use of the word "professional" includes the "function" of internal audit viewed from the perspective of Central Civil Ministries.

Guideline No. 17

COMMUNICATION and APPROVAL OF INTERNAL AUDIT PLANS

The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to the secretary, Integrated Financial Advisor and the audit committee for review and approval.

By March 1st of every year the Pr. CCA/CCA/CA in their capacity as CAE should present the Annual Internal Audit plan and 3-year rolling audit programme to the audit committee, along with the impact of resource limitations. The audit committee would then on the basis of its risk appetite consider either rolling forward certain audit areas and /or supplement its audit team by engaging external consultants/firms and follow a co-source approach to its auditing activities.

Guideline No. 18

RESOURCE MANAGEMENT

The Pr. CCA/ CCA/ CA in their capacity as CAE must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan. Where the CAE observes any present/future gaps, he/she must bring it to the notice of the CGA office.

Appropriate refers to the mix of knowledge, skills and other competencies needed to perform the plan. Sufficient refers to the quantity of resources needed to accomplish the plan. Resources are effectively deployed when they are used in a way that optimizes the achievement of the approved plan[15].

Proficiency of the internal audit team must be considered so that any reasonable person can go through the annual audit plan, arrive at a view that there are adequate resources available to the CAE. Also the competency of the individual auditor must have a mandatory element of critical thinking capabilities.

Guideline No. 19

MANDATORY COMPLIANCE WITH INTERNAL AUDIT GUIDELINES

The Pr. CCA/CCA/CA in their capacity as CAE must follow the Guidelines and procedures as per the CGA Generic Internal Audit Manual and Advisories to guide the internal audit activity. During an engagement, where there is a non-conformance, the same should be mentioned in the audit report.

The compliance of the CGA's Internal Audit Guidelines is a mandatory requirement and forms an important part of the CAE's performance appraisal. Where there is a lack of clarity, the CAE must forward his/her query to the CGA's Centre of Excellence (CGA-CoE) in a timely manner for interpretation/direction. The responsibility for achieving the Annual Audit plan remains with the CAE.

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[15]References from IA Standards.

Guideline No. 20

RECEIVING TECHNICAL SUPPORT FROM IA-CoE IN O/o CGA

The Centre of Excellence (IA-CoE) in the IAD in O/o CGA has been set up to provide guidance and support to the Pr. CCA/ CCA/CA in their capacity as Chief Audit Executive (CAE) and to the Internal Audit Wings (IAW) in the Central Civil Ministries. This guidance will be provided by competent staff and outsourced subject matter experts who will carry out research and also review global technical literature for its suitable applicability. The IAW's will support the research, through surveys, interviews and insights relating to the Ministry/ Area for which the guidance is sought.

The IA-CoE will also rapidly develop Data Analytics capabilities and support Internal Audit Wings of Central Civil Ministries.

Centre of Excellence in the IAD of the CGA

The IA-CoE in the IAD is a central repository for propagation of best practices in internal audit (including governance, risk and control). It will also function as a technical support on internal audit to IAWs in Central Civil Ministries/ Departments and Departments in meeting their objective of adding value to the functioning of their respective Ministries.

To achieve this the ***Pr. CCA/CCA/CA in their capacity as CAEs*** of their respective Ministries would need to provide timely information, feedback and seek support/guidance on areas relating to internal audit and related consultancy. This would be achieved by the CAE:

- Preparing their own Internal Audit Manual for their respective Ministries. and updating the same from time to time.

- Facilitating the Ministry in maintaining an updated Risk Register.

- Reporting on the current level of capability of the IAW and seeking direction and support on plans to move up the Internal Audit Capability Maturity Model (IIA-CM).

- Responding to surveys on the state of implementation of the Generic Internal Audit Manual (GIAM) within Ministries and Departments.

- Sharing of best practices and case studies from the Ministry with the IA-CoE in IAD.

- Reporting on Annual Plans on internal audit, consultancy and capacity building and progress against them.

- Having workshops and meetings with other Pr. CCA/CCA/CA in their capacity as CAEs and IAWs from synergistic clusters of Ministries to ensure that the synergies of common/similar strategies, issues, risks and learning's in internal audit may be leveraged for common gain. Parameters should be devised by the IA-CoE of the IAD with inputs from Ministries concerned.

- Working with the IA-CoE for identifying outsourced service providers with expertise in Risk Management, Control Evaluation, Governance Audits, Information Security, Data Analytics and such other areas of competency constraints as may be required, from time to time.

- Seeking advice and support on capacity building of internal auditors through training, certification, seminars, exchanges, etc.

- Seeking guidance and support from help desk in O/o CGA on areas of complexity, inadequate competence, consultancy, governance, etc., as and when required.

Guideline No. 21

INTERNAL AUDIT OF GOVERNANCE PROCESSES

The Pr. CCA/CCA/CA in their capacity as CAE must report to the secretary, Integrated Financial Advisor and the audit committee on the adequacy and effectiveness of governance processes at the Ministry, toward the achievement of its objectives.

Governance at the Ministry would be the combination of guidelines, processes and structures implemented under the directives of the secretary to inform, direct, manage, and monitor the activities of the Ministry to achieve its objectives. These would also include activities that ensure the Ministry's credibility, establish equitable provision of services, and assure that the code of conduct is complied with in accordance with Government rules.

Guideline No. 22

OBTAINING EXTERNAL SERVICE PROVIDERS TO SUPPORT/COMPLEMENT THE INTERNAL AUDIT ACTIVITY

Prior to the commencement of an audit engagement, the Pr.CCA/CCAof Central Civil Ministries, in their role as Chief Audit Executive, must assess whether the audit team has the knowledge, skills, and other competencies needed to perform an effective audit of the subject matter and must fill the competency gap where it exists through internal resources and/or external service providers.

Where required, activities should be coordinated with other internal and external providers of assurance and advisory services to ensure coverage and minimize duplication of efforts.

Each member of the internal audit activity need not be qualified in all disciplines but collectively the audit team should possess the requisite competency to conduct an effective audit of that particular engagement. Where there is a gap, the internal audit activity may use external service providers qualified in disciplines such as risk management, internal auditing, information technology, environmental affairs and other areas as needed to meet the internal audit activity's responsibilities.

Guideline No. 23

IAW ADDS VALUE TO THE RISK MANAGEMENT PROCESS

The Internal Audit Wing should play a valuable role to assist the Ministry in improving its understanding and management of risk; by providing training and capacity building, evaluating the effectiveness of risk management processes and reviewing significant risk exposures to the governance, operations and information systems of programmes/schemes and the adequacy of controls therein.

Under Guideline No 7, Nature of Work references from IIA Standards on scope of work on risk management processes have been discussed. Pr. CCAs/CCAs in their role as CAEs, gather insights across the Ministry's activities and hence may be in a position to offer valuable suggestions on Enterprise wide Risk Management (ERM) activities of the Ministry. While internal auditors do not have primary responsibility for ERM implementation or their maintenance, the IAW's activities may include:

- Reviewing the adequacy and effectiveness of the existing ERM processes in the programmes/schemes/SBUs of the Ministry and providing recommendations for improvement.

- Reviewing critical control systems and risk management processes and responses for adequacy and effectiveness.

- Advising on the design and improvement of control systems and risk mitigation strategies.

- Implementing a risk-based approach to planning and executing the internal audit process.

- Reviewing the assumptions in management's risk assessments, responses and assurances.

- Providing assurances on the completeness, accuracy, and appropriateness of management's classification and reporting of risks.

- Facilitating Risk Self - Assessment workshops.

For this, risk competencies among internal auditors must continue to grow to support the growing expectations from stakeholders. However, where the ERM capabilities of the IAWs are still inadequate the Pr. CCA/CCA/CA in their capacity as CAE should seek the services of in-house resources from other areas and/or outsourced subject matter experts. The services of the CoE in the IAD of the O/o CGA may be utilized to identify such service providers.

Guideline No. 24

QUALITY ASSURANCE AND IMPROVEMENT PROGRAM

The Pr. CCA/CCA/CA in their capacity as CAE is responsible for maintaining and developing a Quality Assurance Programme that covers all activities of the Ministry's Internal Audit Wings. The CAE must communicate annually the results of the quality assurance and improvement programme to the Integrated Financial Advisor and the audit committee. Disclosure should include the scope and frequency of the internal and external assessments, the qualifications and independence of the assessor(s) or assessment team, including potential conflicts of interest, conclusions of assessors and corrective action plans.

The processes and tools used for ongoing internal quality assessments include engagement supervision, compliance with checklists and procedures, feedback from audit customers and other stakeholders, selective peer review of working papers by staff not involved in the respective audits, project budgets, audit plan completion, cost recoveries, performance metrics, etc.

Section-5

Guidelines for Performing Internal Audit Engagements

Guideline No.	Guideline
25	**Engagement Planning Guidelines**
26	**Engagement Work Program Guidelines**
27	**Engagement Supervision Guidelines**
28	**Guidelines on Obtaining Sufficient and Appropriate Evidence**
29	**Guidelines on Performing internal audit field work**
30	**Guidelines on Documenting the Engagement activities**
31	**Guidelines on Communicating the result of the Engagement**
32	**Guidelines on Monitoring Progress and Communicating the Acceptance of Risks**

The above framework of the internal audit guidelines is to be read with the CGA's Internal Audit Handbook for detailed understanding.

Guideline No. 25

ENGAGEMENT PLANNING

Prior to the commencement of the engagement the internal auditor must adequately plan the audit so as to achieve the audit objectives and based on this submit, before the field visit, a Terms of Reference (TOR) to the audited organization.

The Internal Audit Wing develops and documents a plan for each engagement to include objectives, scope, timing and resource allocations

Planning considerations: While planning the audit, the following aspects are also considered so as to identify opportunities for making significant improvements, viz.

- The objectives of the programme/activity under audit and controls to ensure performance/achievement of these programme objectives

- An assessment of significant risks relating to

- The activity under audit

- Its objectives

- Resources, and operations and how the potential impact is kept to acceptable levels.

Understanding the governance, risk management and control process at the programme/ activity under audit along with a comparison with a framework like COSO so as to assess and conclude on their adequacy and effectiveness.

- Engagement Objectives: Based on the preliminary survey, the internal auditor identifies what the audit intends to achieve through a statement of objectives. Engagement objectives could be thought as questions about the activity/programme under audit, which the auditors seek answers for based on evidence obtained and assessed against some criteria. These questions are usually on the significant risks observed by the internal auditor during audit planning.

- Engagement Scope is the subject matter of the programme, scheme, and activity from where the evidence is to be collected and identifies the type of records, time period, locations, etc., and is the boundary of the auditor's field work.

- Assigning staff and other resources should collectively as a team has the requisite proficiency and time availability for accomplishing the audit objectives thereby completing the audit in a satisfactory manner.

Steps:

- During planning the auditor does a preliminary survey to become familiar with the activities, risks, controls and to identify the areas of emphasis of the programme/ activity under audit. Comments and suggestions are invited from the staff. Based on the risk assessment report, the auditor frames the audit objectives and scope and issues a Terms of Reference (TOR) on the engagement to the audited organization.

- A key activity in planning the audit of schemes/programmes is that the internal auditor must conduct a preliminary risk assessment of the scheme/program under review and the significant risks must be covered as part of the engagement objectives.

    ◊ In order to accomplish this activity, the internal auditor also considers

    ◊ the reliability of the scheme/programme management's assessment of risk

    ◊ the scheme/programme process for monitoring, reporting and resolving risk and control issues

    ◊ Scheme/programme management's reporting of events that exceed the limit of the Ministry's risk appetite and the Ministry's response to those reports

    ◊ Risks in related activity to the activity under review

- Internal auditors must summarize the results of the review of management's assessment of risk, the background information and any survey work as a separate section titled Auditor's Risk Assessment Report (RAR).

Documents:

Before commencement of field work, the following documents need to be in the Engagement's working papers file

- Audit Planning Memo (APM)

- Preliminary Survey findings report

- Includes Auditor's Risk Assessment Report (RAR)

- Engagement Terms of Reference (TOR)

Guideline No. 26

ENGAGEMENT WORK PROGRAMME

The internal auditor must prepare a written audit programme for each audit and update it as necessary so as to achieve the audit objectives.

Prior to the audit, the internal auditor must develop and document work programme that include procedures for identifying, analyzing, evaluating and documenting information during the engagement to include

- Audit objectives

- Risks, processes, transactions that are to be examined

- Nature of testing required

- Documents the information to be examined and the internal auditor's procedures to be applied on it.

Before commencement of the field visit, the audit programme should be ready for use in all material respects except the selection of sample size. Also the audited organization should be informed in advance of the scope of review including interviews, records to be seen, information requirements, etc.

Guideline No. 27

ENGAGEMENT SUPERVISION

Audit supervisors must demonstrate adequate oversight on the audit engagement and in a manner to mitigate audit risk.

During field work the Audit supervisor should be in contact with the field staff and get updates on critical aspects in order to decrease Audit Risk.

The extent of supervision will depend upon the proficiency and experience of the internal auditors and the complexity of the engagement.

Guideline No. 28

OBTAINING SUFFICIENT AND APPROPRIATE EVIDENCE

The internal auditor must obtain sufficient and appropriate evidence to provide a reasonable basis for their findings and conclusions on the audit objectives.

Evidence to be collected is around the subject matter under testing. Auditors should identify criteria relevant to the audit objectives that permit consistent assessment of the subject matter.

After establishing the criteria, the auditors should identify potential sources of information that could be used as evidence and choose the appropriate source. Appropriateness is the measure of quality of evidence and includes relevance, reliability and usefulness while concluding on the audit objectives. Sufficiency is a measure of quantity and whether enough evidence has been obtained to persuade a knowledgeable person that the findings are reasonable. The auditor should determine the amount and type of evidence needed to address the audit objectives and adequately plan the audit work.

Auditors should determine the overall sufficiency and appropriateness of the evidence to form a reasonable basis for the findings and/or conclusions within the context of the internal audit objectives. An overall assessment of evidence is important.

Evidence is not sufficient or appropriate when

- Using that evidence carries an unacceptable high risk that it could lead to improper findings or conclusions

- The evidence has significant limitations

- The evidence does not provide an adequate basis for addressing the audit objectives

When auditors identify limitations or uncertainties in evidence that is significant to the audit findings and conclusions, they should apply additional procedures as appropriate, to include

- Seek independent corroborating evidence

- Presenting the findings and conclusions with a disclosure in the report describing the limitations or uncertainties with the validity or reliability of evidence

- Determining whether to report the limitations or uncertainties' as a finding including any related internal control deficiencies, programme deficiencies, etc.

Guideline No. 29

PERFORMING INTERNAL AUDIT FIELD WORK

To obtain sufficient and appropriate evidence, the internal auditor must identify, analyze, evaluate and document information within the context of the internal audit objectives. The engagement supervisor must ensure due discussion and adequate consideration of audited organization feedback along with a proper closure of the field visit through an exit meeting.

While obtaining audit evidence to meet the audit objectives, the internal auditor will perform the below mentioned activities for identifying, analyzing and evaluating information, viz.

- Gathering input from audited organization's staff through survey, interviews, internal control checklist, etc.

- Analyzing relationships amongst financial and/or non-financial information through analytical procedures

- Review of process maps for evaluating the efficiency of processes and controls

- Checklists to ensure that the auditor has completed diligently the audit procedures that were planned to be completed.

- Where required, computerized audit tools and techniques should be used to perform auditing activities, including using

- Generalized Audit Software (GAS) to perform various analytical procedures on the audited organization's data.

- Using continuous monitoring techniques for online real time monitoring of Systems and transactions.

- The Pr. CCA/CCA/CA in their capacity as CAE should encourage the usage of computerized working papers and

audit management software. While using electronic working papers, adequate security should be ensured and the working papers should be protected from unauthorized change.

- Auditors need to draw conclusions on the transactions in the activity under audit. By applying statistics, the auditor can test relatively small samples to draw these conclusions. While many auditors may prefer to engage experts for statistical sampling, however the internal auditor should be proficient in deciding when to use which sampling method, viz. statistical, judgmental, discovery sampling.

- The CAE must control access to engagement records, develop retention requirements for engagement records, regardless of the medium in which these records are stored.

- Before commencing the engagement, the work programme should be documented and approved. The work programme should include technology based audit and sampling techniques.

- The process of collecting, analyzing, interpreting and documenting information should be supervised to provide reasonable assurance that the engagement objectives are met and that the internal audit's objectivity is maintained.

Guideline No. 30

DOCUMENTING ENGAGEMENT ACTIVITIES

Engagement activities should be documented in sufficient detail to enable an experienced auditor with no previous connection to the audit to understand from the audit documentation the nature, timing, extent and results of audit procedures performed, the audit evidence obtained and its source and the conclusions reached, including evidence that supports the auditors' significant judgements and conclusions.

Auditors need to document significant decisions affecting the audit objectives, scope and methodology; findings; conclusions and recommendations.

The Pr. CCA/CCA/CA in their capacity as CAE needs to approve a documentation policy which covers the custody and retention of advisory engagement records, as well as their release to internal and external parties. These guidelines must be consistent with the Ministry's Guidelines and any pertinent regulatory or other requirements. The Guidelines must cover:-

- Need for Internal Audit Wings to document sufficient, reliable and relevant information to support their engagement results and conclusions.

- Need for controlled access to engagement records. The Pr. CCA/CCA/CA in their capacity as CAE must obtain the approval of senior management and/or legal counsel prior to releasing such records to external parties, as appropriate.

Retention requirements for engagement records, regardless of the medium in which each record is stored. These retention requirements must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

Documenting Information

Internal auditors must document sufficient, reliable, relevant, and useful information to support the engagement results and conclusions.

The chief audit executive must control access to engagement records. The chief audit executive must obtain the approval of senior management and/or legal counsel prior to releasing such records to external parties, as appropriate.

The chief audit executive must develop retention requirements for engagement records, regardless of the medium in which each record is stored. These retention requirements must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

The chief audit executive must develop guidelines governing the custody and retention of advisory engagement records, as well as their release to internal and external parties. These guidelines must be consistent with the organization's guidelines and any pertinent regulatory or other requirements16.

Guideline No. 31

COMMUNICATING THE RESULTS OF THE ENGAGEMENT

The internal auditors must communicate the results of the audit in a timely manner. Final communication by the internal auditor of the engagement results must contain an opinion and/ or conclusions. Where also an overall opinion is issued on an audit area or activity it must take into account the expectations of the Ministry and must be supported by sufficient, reliable, relevant and useful information. The reason for an unfavorable overall opinion must be stated.

While communicating the results of the audit, the following matters should be taken care of, viz.

- Where certain audit observations are of a nature that delaying, the reporting may impact the achievement of programme/scheme objectives, and then the auditor should communicate to the concerned authority their findings at an early date and even during the course of audit.

- The audit reports structure should include the engagement's objectives and scope as well as applicable conclusions, recommendations and action plans. In case there is a scope limitation, this should be brought out in the reports.

- Internal auditors are encouraged to acknowledge satisfactory performance and best practices being followed by the audited organization.

- To ensure quality of the audit reports they must be clear, accurate, and concise and issued in a timely manner. The internal audit wing should bring objectivity in the observations and their recommendations should be constructive and complete.

All reports should be issued by the Pr. CCA/CCA/CA in their capacity as CAE as he/she retains the overall responsibility even if some duties have been delegated to others. Where there is an error or omission in the report, the CAE must circulate corrected information to all the recipients of the earlier communication.

- In case there is full conformance of CGA Internal Audit Guidelines during the audit engagement, this should be mentioned in the report.

- Overall opinions could be ratings, conclusions or other descriptions of results. Such an opinion may be in relation to controls around a specific process, risk or business acceptance of unit.

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16 Reference from IIA Standard 2330.

Guideline No. 32

MONITORING PROGRESS AND COMMUNICATING ACCEPTANCE OF RISKS

The Pr. CCA/CCA/CA in their capacity as CAE must establish and maintain a system to monitor the satisfactory disposition of the results communicated to the programme/scheme management. Where there is inordinate delay in resolving issues, the CAE may conclude that the programme/ scheme management has accepted the risk of not taking action. The CAE should include these open issues as part of his/her yearly reporting to the audit committee on risks unacceptable to the Ministry.

After issue of the audit report, the role of addressing the issues raised and accepted by the programme/scheme management. It is not uncommon that the internal auditor sends reminders to know the follow-up status of these outstanding issues. However after a reasonable time the Pr. CCA/CCA/CA in their capacity as CAE may conclude that the issues still remaining open imply that the programme/scheme management has for the time being accepted the risk of not taking action and hence should be included in the portfolio of unacceptable risks for the purposes of reporting to the Ministry.

Standards on Internal Audit Issued by ICAI

SIA 1

Planning an Internal Audit

The basic objective of the SIA is to establish standards and provide guidance in respect of planning an Internal Audit and helping in achieving the objective of an Internal Audit function. Adequate planning ensures that appropriate attention is devoted to significant areas of audit, potential problems are identified, and that the skills and time of the staff are appropriately utilized. Planning also ensures that the work is carried out in accordance with the applicable pronouncements of the Institute of Chartered Accountants of India. Planning should also be based on the knowledge of the entity's business.

SIA 2

Basic Principles Governing Internal Audit

The purpose of this standard on Internal Audit (SIA) is to establish standards and provide guidance on the general principles governing internal audit. This standard explains the principles, namely integrity, objectivity and independence, confidentiality, due professional care, skill and competence, work performed by others, documentation, planning, evidence and reporting, which governs the internal auditor's professional responsibilities.

SIA 3

Documentation

The purpose of the Standard on Internal Audit is to establish standards and provide guidance on the documentation requirements in an internal audit. Adequate documents act as basis for the planning and performing the internal audit. Documents provide the evidence of the work of the internal auditor. This standard provides guidance regarding the form and content of the internal audit documentation, detention and retention of the same and identification of the preparer and reviewer.

SIA 4

Reporting

The purpose of the Standard on Internal Audit (SIA) 4, Reporting is to establish standards on the form and content of the internal auditor's report issued as a result of the internal audit performed by an internal auditor of the systems, processed, including the items of financial statements of an entity. This SIA describes the basic elements of an internal audit report such as opening, objectives, scope paragraphs and executive summary. This SIA also deals with the different stages of communication and discussion of the report and describes the reporting responsibilities of the internal auditor when there is a limitation on the scope. The standard also lays down the reporting responsibilities of the internal auditor when there is restriction on usage and circulation of the report.

SIA 5

Sampling

Sampling provides the guidance regarding the design and selection of an audit sample and also on the use of the audit sampling in the internal audit engagements. This SIA also deals with the evaluation of the sample results. The standard also provides guidance on the use of sampling in risk assessment procedures and test of controls performed by the internal auditor to obtain an understanding of the entity, business and its entity, business and its environment, including mechanism of its internal control. The areas covered by the SIA include design of sample tolerable and expected error, selection of sample, evaluation of sample results, analysis of errors in the sample, projection of errors, re-assessing sample risk. This also describes the internal auditor's documentation requirements in the context of the sampling.

SIA 6

Analytical Procedure

The Standard on Internal Audit (SIA) 6 Analytical Procedures provide the guidance regarding the application of analytical procedures during internal audit. The SIA deals with the aspects such as, the nature and purpose of analytical procedures, analytical procedures as risk assessment procedures and in planning the internal audit, analytical procedures as substantive procedures, analytical procedures in the overall review at the end of the internal audit, extend of reliance on analytical procedures and investigating unusual items or trends.

SIA 7

Quality Assurance in Internal Audit

The Standard on Internal Audit (SIA) 7, Quality Assurance in Internal Audit establishes standards and provide guidance regarding quality assurance in internal audit. A system for assuring the quality in internal audit should provide reasonable assurance that the internal auditors comply with professional standards, regulatory and legal requirements so that the reports issued by them are appropriate in the circumstances. This Standard provide the guidance to the person entrusted with the responsibility for the quality of the internal audit whether in-house internal audit or a firm carrying out internal audit. This standard also provides the extensive knowledge about the internal quality review, external quality reviews and communicating the results thereof.

SIA 8

Terms on Internal Audit Engagement

The terms of engagement define the scope, authority, responsibilities, confidentiality, limitation and compensation of the internal auditors. Terms of Internal Audit Engagement lay down clarity between the internal auditors and the users of their services for inculcating professionalism and avoiding misunderstanding as to any aspect of the engagement. This Standard on Internal Audit (SIA) 8, Terms of Internal Audit Engagement Provides guidance in respect of terms of engagement of the internal audit activity whether carried out in house or by any external agency. This SIA describes the elements of the terms of engagement viz., scope, responsibility, authority, confidential, limitation, reporting, compensation and compliance with standards.

SIA 9

Communication with Management

The Standard on Internal Audit (SIA) 9, Communication with Management provides a framework for the internal auditor's communication with management. It identifies some specific matters to be communicated with the management as described in the terms of engagement like the internal auditor's responsibilities in relation to the terms of engagement, planned scope and timing of the internal audit, significant findings from the internal audit. The Standard also provides the extensive knowledge about the communication process to make the two-way communication effective like the forms and timing of communication process. This Standard also provides the guidance for the documentation of the same.

SIA 10

Internal Audit Evidence

The purpose of this Standard is to establish standards on the basic principle that the internal auditor should obtain sufficient appropriate audit evidence through compliance and substantive procedures to substantiate his checking and findings and enable him to draw reasonable conclusion there from. The SIA also explains the concept of sufficient appropriate internal audit evidence, procedures to be performed to obtain internal audit evidence namely, inspection, observation, inquiry and confirmation, computation and Analytical review.

SIA 11

Consideration of Fraud in an Internal Audit

As the name indicates the purpose of this Standard is to establish Standards on consideration of fraud in an internal audit. This Standard provides guidance on the designing and implementation of the internal controls in an entity that would also help the internal audit to assess the risk of frauds. The Standards also establishes the responsibilities of the internal auditor relating to the fraud prevention and detection. The SIA also provide guidance regarding the communication and documentation of fraud.

SIA 12

Internal Control Evaluation

The purpose of this Standard on Internal Audit is to establish standards and provide guidance on the procedures to be followed by internal auditor in evaluating the system of internal control in an entity and for communicating weaknesses therein to those charged with governance. The Standard also extensively deals with aspects such as meaning and inherent limitations of internal controls, control environment, risk assessment, tests of control and communication of weaknesses. The SIA also describes role of the internal auditor in evaluating internal controls.

SIA 13

Enterprise Risk Management

The purpose of this Standard on Internal Audit is to establish standards and provide guidance on review of an entity's risk management system during an internal audit or such other review exercise with the objective of providing an assurance thereon.

The Standard establishes process of enterprise risk management and the role of the internal auditor. This Standard also provides guidance regarding the internal audit plan and information which internal auditor should provide in this report.

SIA 14

Internal Audit in an Information Technology Environment

The purpose of this Standard on Internal Audit is to establish standards on procedures to be followed when an internal audit is conducted in an Information Technology (IT) Environment. This Standard describes skill and competence needed by the internal auditor to conduct an internal audit in an information technology environment, factors to consider while planning such internal audit, matters that may affect audit in an IT environment, assessment of risk, audit procedures, review of the IT environment and Documentation.

SIA 15

Knowledge of the Entity Its Environment

The purpose of this Standard is to establish standards and provide guidance on what constitutes the knowledge on an entity's business, its importance to the various phases of an internal audit engagement and the techniques to be adapted by the internal auditor in acquiring such knowledge about the client entity and its environment, prior to commencing an internal audit engagement and subsequently thereafter, at all stages of the internal audit process. This Standard also sets out the guidelines regarding the application, usage and documentation of such knowledge by the-internal auditor.

SIA 16

Using the Work of an Expert

The purpose of this Standard is to establish standards and provide guidance where the internal auditor uses the work performed by an expert. The Standard also explains situations in which the need for using the work of an expert might arise, factors to consider when deciding whether to use the work of an expert or not, evaluating the skills and competence and objectivity of an expert, procedures for evaluating the work of an expert, references to an expert in the internal auditor's report, etc.

WORKBOOK

1.   Elaborate the term: ISPPA

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2.   What are the two types of standards?

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3.   What is the main role objective of Internal Auditing Guidelines?

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4.   Who is principal stakeholder of Government Audit?

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5.   Internal Audit wings need ——————————————— independence to carry out their engagements

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6.   Proficiency is a collective term referring to which 3 aspects of internal auditors?

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7. Effective risk management requires that significant risks are _____ and _____

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8. Who are the 3 participants in assurance services?

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9. Before commencing field work which documents need to be in the working papers file?

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10. What audit engagement activities should the auditor document?

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11. Internal Audit must communicate the results of the audit in a _____manner.

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Unit - 5

Control Environment and Evaluation of Internal Controls

Learning Outcomes:

♦ What are Internal Controls?

♦ Types of Internal Controls.

♦ Need for Internal Controls.

♦ Internal Control Framework.

♦ Internal Control Evaluation.

♦ Limitations of Internal Controls.

♦ Role of Internal Audit in Internal Control.

1.1 INTRODUCTION

Internal Control is a process effected by the Auditee, Head of the Office, concerned Ministry and other audit personnel, designed to provide reasonable assurance that the following general objectives relating to operations, reporting and compliance are being achieved:

• fulfilling accountability obligations;

• complying with applicable laws and regulations;

• executing orderly, ethical, economical, efficient and effective operations; and

Safeguarding resources against loss, misuse and damage "Simply defined, internal control is the process by which an organization governs its activities to effectively and efficiently accomplish its mission." – INTOSAI (International Organization of Supreme Audit Institutions).

As per COSO (Committee of Sponsoring Organizations), Internal Control is a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives.

In simple terms, internal controls are activities and safeguards that are put in place by a Ministry to ensure that its activities are proceeding as planned. Internal controls are essential for Good Governance.

1.2 The objectives of internal control are three-fold:

a) Operations: Operations objectives relate to achieving the entity's mission. Appropriate objectives include improving (i) financial performance (ii) productivity (iii) quality innovation and (v) Beneficiary satisfaction/Public satisfaction in general. Operations objectives also include safeguarding of assets;

b) Reporting: Objectives relate to financial and non-financial reporting and Internal or external reporting; and

c) Compliance: Objectives relate to laws, rules and regulations that set minimum standards of conduct.

2.1.1 FULFILLING ACCOUNTABILITY OBLIGATIONS: Accountability is the process whereby public service bodies and the individuals within them are held to account for their decisions and actions including their stewardship of public funds, fairness, and all aspects of performance. This will be realized by developing and maintaining reliable and relevant financial and non-financial information and by means of a fair disclosure of that information in timely reports to internal as well as external stakeholders.

Non-financial information may relate to the economy, efficiency and effectiveness of policies and operations (performance information), and to internal control and its effectiveness.

2.1.2 COMPLYING WITH LAWS AND REGULATIONS: Government Ministries are required to follow many laws and regulations. Examples include the Constitution, Finance Act, International treaties, laws and regulations on proper administration, accounting law, environmental protection and civil rights law, tax laws, anti-corruption law. Similarly implementing agencies need to follow the programme/scheme guidelines during implementation achieving the scheme programme objectives.

2.1.3 EXECUTING ORDERLY, ETHICAL, ECONOMICAL, EFFICIENT AND EFFECTIVE OPERATIONS:

The Ministry's operations should be orderly, ethical, economical, efficient and effective. 'Orderly' means in a well-organized or methodical way.

'Economical' means not wasteful or extravagant. It means getting the right amount of resources of the right quality delivered at the right time and place at the lowest cost.

'Effective' refers to the accomplishment of objectives or to the extent to which the outcome of an activity matches the objectives or the intended effects of that activity.

'Efficient' refers to the resources used to achieve the objectives. It means the minimum resource inputs to achieve a given quantity and quality of output, or a maximum output with a given quantity and quality of resource inputs.

'Ethical' relates to moral principles. The importance of ethical behaviour, prevention and detection of fraud and corruption in the public sector has become more emphasized since the nineties. General expectations are that public servants should serve the public interest with fairness and manage public resources properly. Citizens should receive impartial treatment on the basis of legality and justice. Therefore, public ethics is a prerequisite to, and underpins public trust and is a keystone of good governance.

Control Objective Questionnaire

♦ Is the activity protected from avoidable
  • Losses
  • Wastages
  • Fraud

♦ Is the information
  • Adequate
  • Accurate
  • Timely
  • Meaningful
  • Circulated

♦ Is the activity conducted
  • Effectively
  • Efficiently
♦ Are the systems and policies sound and adhered to
♦ Are assets safeguarded from losses
♦ Accomplishment of established

2.1.4 SAFEGUARDING OF RESOURCES AGAINST LOSS, MISUSE AND DAMAGE:

i)   The significance of safeguarding the resources in the public sector needs to be stressed. This is due to the fact that budgetary accounting or accounting on cash basis, which is still widespread in the public sector, does not provide sufficient assurance related to the maintenance of records of the resources. As a result, the Ministry does not always have a record of all their assets, which makes them more vulnerable. Therefore, controls should be embedded in each of the activities related to the management of resources of the entity, from the entry until the disposition.

ii)   Other resources such as information, source documents and accounting records are also in danger of being stolen, misused or accidentally destroyed. Safeguarding such resources and records has become increasingly important since the arrival of computer systems. Sensitive information stored on computer media can be destroyed, copied, distributed and abused if care is not taken to protect it.

2.2 TYPES OF INTERNAL CONTROLS:

- Preventive: Prevents or minimizes errors/ irregularities from occurring. For example: segregation of duties, dual cheque signing authority, and purchase policy.

- Detective: Highlight errors or irregularities after they have occurred. For example: Bank reconciliation, Audit, Physical verification of Fixed Assets.

- Reconstructive: Effective backup and disaster recovery plans. For example: Disaster Recovery Procedures.

2.3 NEED FOR INTERNAL CONTROLS IN GOVERNMENT:

The size and scale of government operations calls for effective internal controls over its activities. Internal controls help strengthen the public accountability of government and help balance the competing demands of delivering a responsive and quality service to the community while recognizing fiduciary responsibilities and maintaining standards of probity, prudence and ethics.

2.4 INTERNAL CONTROL FRAMEWORK

Committee of Sponsoring Organizations (COSO) has developed an internal control framework that is widely accepted across organizations and countries, the world over. The key concepts of COSO framework include:

2.5   RELATIONSHIP BETWEEN OBJECTIVES AND COMPONENTS

The relationship between objectives and components of internal control can be depicted with the help of the COSO Cube as given in the figure. As per COSO:

1)   There is a direct relationship between the objectives, which represent what a Ministry, strives to achieve, and the internal control components, which represent what is needed to achieve them. The relationship is depicted in a three-dimensional matrix, in the shape of a cube. The three objectives – accountability, compliance, and operations – are represented by the vertical columns, the five components are represented by horizontal rows, and the Ministry and its departments are depicted by the third dimension of the matrix.

2)   Each component row "cuts across" and applies to all three objectives. For example, financial and non-financial data generated from internal and external sources, which belong to the information and communication component, are needed to manage operations, to report and fulfill accountability purposes, and to comply with applicable laws.

3)   Similarly, looking at the objectives, all five components are relevant to each objective. Taking one objective, e.g. effectiveness and efficiency of operations, it is clear that all five components are applicable and important to its achievement.

4)   Internal control is not only relevant to an entire Ministry but also to an individual department of such Ministry. This relationship is depicted by the third dimension, which represents entire Ministries and Departments. Thus, one can focus on any of the matrix's cells.

5)   The five components of internal control are briefly explained in the subsequent paragraphs.

(A)   Control Environment: Internal controls are thus a continuous process, and not isolated efforts or events, which provide a reasonable assurance that controls are in place to mitigate identified risks. According to the COSO Framework, everyone in a Ministry/Department has responsibility for internal control to some extent. Virtually all employees produce information used in the internal control system or take other actions needed to affect control. The commitment of people in the Ministry, especially those at the top, is critical to implementation of internal controls within the Ministry. This control environment sets the tone and includes integrity, ethical values of the individuals and of the Ministry as a whole.

1)   Control environment means the overall attitude, awareness and actions of Ministry regarding the internal control system and its importance in the Ministry.

2)   The control environment is the foundation for the entire control system. It provides the discipline and structure as well as the climate which influences the overall quality of internal control. It has overall influences on how objectives and strategy are established, and control activities are structured.

3)   The control environment sets the tone of a Ministry, influencing the control consciousness of its staff. It is the foundation for all other components of internal control, providing discipline and structure.

4)   Elements of the control environment are:

- The personal and professional integrity and ethical values of the Ministry, including a supportive attitude toward internal control;

- Commitment to competence;

- The "tone at the top" i.e. management philosophy and operating style;

- Organizational structure;

- Assignment of authority and responsibility, and

- Human resource policies and practices.

(B)   Risk assessment:

1)   This refers to the process of identifying and analyzing relevant risks which threaten achievement of the Ministry's objectives and determining the appropriate response. As stressed in the definition, internal control can provide only reasonable assurance that the objectives of the Ministry are being achieved. Risk assessment, as a component of internal control plays a key role in the selection of the appropriate control activities to undertake.

2)   Elements of risk assessment are:

- risk identification;

- risk evaluation (assessing the likelihood and significance of the risk and then categorizing the risk as High, Medium and Low), and

- risk acceptance (understanding and defining the level of risk, the Ministry is able to live with).

This is important because control activities designed to mitigate risks have a cost and hence it may sometimes be prudent to live with a risk — since the costs of eliminating these risks may be much more than the benefits which are likely to accrue from these efforts.

3) Consequently, setting objectives is a precondition to risk assessment. Objectives must be defined before the risks to achievement of these objectives can be identified and necessary actions need to be taken to manage the risks. That means, having in place, an on- ongoing process for evaluating and addressing the impact of risks in a cost-effective way and having staff with the appropriate skills to identify and assess the potential risks.

Indicators of weak controls:

- Govt. policies set out in Acts, Rules, Statutes and Regulations, etc. (Weak control; policies poorly understood/improperlyfollowed)

- Employees' codes of conduct(Weak control, violation of codes)

- Clear systems like budget, treasury, etc. (Weak control, wrong budgetary assumptions, inadequate treasury control, etc.)

- Identification and control of internal and external risk factors (personnel policy, economic changes, calamities, etc.) (Weak control: potential or real risk factors not controlled)

- Cost-benefit analysis of major activities (Weak controls absenceof CBA)

(C) Control Activities: Control activities are the policies and procedures established and executed to address risks and to achieve the Ministry's objectives.

To be effective, control activities need to:

- be appropriate (that is, the right control in the right place and commensurate to the risk involved);

- function consistently according to plan throughout the period (that is, be complied carefully by all employees involved and not bypasses when key personnel are away or the workload is heavy).

- be cost effective (that is, the cost of implementing the control should not exceed the benefits derived);

- be comprehensive, reasonable and integrated into the overall organizational objectives.

Indicators of weak controls:

- Reviews of performance against objectives (Weak controls absence of reviews)

- Documentation of activities (Weak controlsabsence of proper documentation)

- Prescription of performance indicators (Weak controls lack of performance indicators)

- Key reconciliations like basic reconciliation, cash reconciliation, asset reconciliation, etc. (Weak controls erratic or non-reconciliation)

Control activities include a range of policies and procedures as indicated below:

i) Authorization and approval procedures: Authorizing and executing transactions and events should be only done by persons acting within the scope of their authority. Authorization is the principal means of ensuring that only valid transactions and events are initiated as intended. Authorization procedures, which should be documented and clearly communicated to managers and employees, should include the specific conditions and terms under which authorizations are to be made. Conforming to the terms of an authorization means that employees act in accordance with directives and within the limitations established by Ministry.

ii) Segregation of duties (authorizing, processing, recording, and reviewing): To reduce the risk of error, waste, or wrongful acts and the risk of not detecting such problems, no single individual or section should control all key stages of a transaction or event. Rather, duties and responsibilities should be assigned systematically to a number of individuals to ensure that effective checks and balances exist. Key duties include authorizing and recording transactions, processing, and reviewing or auditing transactions. Collusion, however, can reduce or destroy the effectiveness of this internal control technique. A small Department may have too few employees to fully implement this technique. In such cases, the Ministry must be aware of the risks and compensate with other controls. Rotation of employees may help ensure that one person does not deal with all the key aspects of transactions or events for an undue length of time. Also, encouraging or requiring annual holidays may help reduce risk by bringing about a temporary rotation of duties.

iii) Controls over access to resources and records: Access to resources and records is limited to authorized individuals who are accountable for the custody and/or use of the resources. Restricting access to resources reduces the risk of unauthorized use or loss to the government and helps to achieve objectives. The degree of restriction depends on the vulnerability of the resource and the perceived risk of loss or improper use, and should be periodically assessed. When determining an asset's vulnerability, its cost, portability and exchangeability should be considered.

iv) Verifications: Transactions and significant events are verified before and after processing. e.g., when goods are delivered, the number of goods supplied is verified with the number of goods ordered. Afterwards, the number of goods invoiced is verified with the number of goods received. The inventory is verified by performing physical stock verification.

v) Reconciliations: Records are reconciled with the appropriate documents on a regular basis, e.g. the accounting records relating to bank accounts are reconciled with the corresponding bank statements.

vi) Reviews of operating performance: Operating performances are reviewed against a set of standards on a regular basis, assessing effectiveness and efficiency.

vii) Review of operations, processes and activities: Operations should be reviewed. This type of review of the actual operations of a Ministry is different from the monitoring of internal controls.

viii) Supervision (assigning, reviewing and approving, guidance and training): Competent supervision ensures that internal control objectives are achieved. Assignment, review, and approval of an employee's work encompass:

- Clearly communicating the duties, responsibilities an accountability assigned to each staff member;

- Systematically reviewing each member's work to the extent necessary;

- Approving work at critical points to ensure that it flows as intended.

Delegation of work should not diminish the accountability of person delegating the work. Superiors also provide their subordinates with the necessary guidance and training to help ensure that errors, waste, and wrongful acts are minimized and that directives are understood and achieved.

The above-mentioned list is exhaustive but enumerates the most common preventive and detective control activities.

Once a control activity is implemented, it is essential that assurance about its effectiveness is obtained. Moreover, it must be clear that control activities form only a component of internal control. They should be integrated with the components of internal control.

ix).   Information Technology Control Activities:

1)   As information technology has advanced, Ministries have become increasingly dependent on computerized information systems to carry out their operations and to process, maintain, and report essential information. As a result, the reliability and security of computerized data and of the systems that process, maintain, and report these data are a major concern to the Ministry and its auditors.

2)   The use of automated systems to process information introduces several risks that need to be considered by the Ministry. These risks arise, inter alia, from:

- uniform processing of transactions;

- information systems automatically initiating transactions;

- increased potential for undetected errors;

- existence, completeness, and volume of audit trails;

- the nature of the hardware and software used; and recording of unusual or non- routine transactions.

For example, an inherent risk from the uniform processing of transactions is that any error arising from computer programming problems will occur consistently in similar transactions. Effective information technology controls can provide the Ministry with reasonable assurance that information processed by its systems meets desired control objectives, such as ensuring the completeness, timeliness, and validity of data and preserving its integrity.

3)   Information systems imply specific types of control activities. Therefore, information technology controls consist of two broad groupings:

- General controls; and

- Application controls

3.1   General Controls

1)   General controls are the structure, policies and procedures that apply to all or a large segment of an entity's information systems and help ensure their proper operation. They create the environment in which application systems and controls operate.

2) The major categories of general controls are:

- Entity-wide security program planning and management,

- access controls,

- controls on the development, maintenance and change of the application software,

- system software controls,

- segregation of duties, and

- service continuity.

3.2 Application Controls

1) Application controls are the structure, policies and procedures that apply to separate, individual application systems, and are directly related to individual computerized applications. These controls are generally designed to prevent, detect, and correct errors and irregularities as information flows through information systems.

2) General and application controls are interrupted and both are needed to ensure complete and accurate information processing.

3) Because information technology changes rapidly, the associated controls must evolve constantly to remain effective.

Some examples of control activities:

- Segregation of duties -separating authorization, custody, and record keeping roles.

- Authorization of transactions - review of particular transactions by an appropriate level.

- Retention of records - maintaining documentation to substantiate transactions.

- Supervision or monitoring of operations.

- Physical safeguards - use of cameras, locks, physical barriers, etc. to protect property.

- Top-level reviews-analysis of actual versus planned, periodic and regular operational reviews, metrics, and other key performance indicators.

- IT Security controls - Controls to ensure that access to systems and data is restricted to authorized personnel, such as usage of passwords and review of access logs.

- IT application controls - Controls over information processing enforced by IT applications, such as edit checks to validate data entry, accounting for transactions in numerical sequences, and comparing file totals with control accounts.

An efficient internal control system is immensely useful to the Ministry in reducing misuse and waste of resources and facilitates the achievements of the stated goals and objectives of the Ministry/Department.

(D)   Information and Communication:

Information and communication are essential to the realization of all the internal control objectives. For example, one of the objectives of internal control in a Government Ministry is fulfilling public accountability obligations. This can be achieved by developing and maintaining reliable and relevant financial and non-financial information and communicating this information by means of a fair disclosure in timely reports. Information and communication relating to the Ministry's performance will create the possibility to evaluate the orderliness, ethicality, economy, efficiency and effectiveness of operations. In many cases, certain information or communications have to be provided in order to comply with laws and regulations.

Information

1.   A precondition for reliable and relevant information is the prompt recording and proper classification of transactions and events. Pertinent Information should be identified, captured and communicated in a form and timeframe that enables staff to carry out their responsibilities (timely communication to the right people). Therefore, the internal control system and all transactions and significant events should be fully documented.

2.   Information systems produce reports that contain operational, financial and non-financial, and compliance related information and that make it possible to run and control the operations. They deal not only with internally generated data, but also information about external events, activities and conditions necessary to enable decision-making and reporting.

3.   Ministry's ability to make appropriate decisions is affected by the quality of information which implies that the information is:

- Appropriate (Is the needed information thereof);

- Timely (Is it there when required?);

- Current (Is it the latest available?);

- Accurate (Is it correct?);

- Accessible (Can it be obtained easily by the relevant parties?).

Communication:

1.   Effective communication should occur in all directions, following down, across and up in the Ministry, throughout all components and the entire structure.

2.   All personnel should receive a clear message from the top that control responsibilities should be taken seriously. They should understand their own role in the internal control system, as well as how their individual activities relate to the work of others.

3.   Information is a basis for communication, which must meet the expectations of groups and individuals, enabling them to carry out their responsibilities effectively.

4.   One of the most critical communications channels is that between the senior officials of the Ministry and their staff. The senior officials must be kept up to date on performance, developments, risks and the functioning of internal control, and other relevant events and issues. In the same way, they should communicate to their staff what information it needs and provide feedback and direction.

5. In addition to internal communications, Ministry should ensure that there are adequate means of communicating with, and obtaining information from external parties, as external communications can provide input that may have a highly significant impact on the Ministry achieving its goals.

(E) Monitoring:

1. Monitoring internal controls ensures that controls are operating as intended and that they are modified appropriately for changes in conditions. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of both in order to ensure that internal control achieves the desired results.

2. Ongoing monitoring occurs in the course of normal, recurring operations of a Ministry. It is performed continually and on a real-time basis, it reacts dynamically to changing conditions and is ingrained in the entity's operations. As a result, it is more effective than separate evaluations. Since, separate evaluations take place after the fact, problems will often be identified more quickly by ongoing monitoring routines.

3. The scope and frequency of separate evaluations should depend primarily on the assessment of risks and the effectiveness of ongoing monitoring procedures. When making that determination, the Ministry should consider the nature and degree of changes, from both internal and external events, and their associated responses and related controls; and the results of the ongoing monitoring. Separate evaluations of control can also be useful by focusing directly on the effectiveness of the controls at a specific time. Separate evaluations may take the form of self-assessments as well as a review of control design and direct testing of internal control. Separate evaluations may also be performed by the external auditors.

4. Usually, some combination of ongoing monitoring and separate evaluations will ensure that internal control maintains its effectiveness over time.

5. All deficiencies found during ongoing monitoring or through separate evaluations should be communicated to the appropriate level of the Ministry to take necessary action. The term "deficiency" refers to a condition that effect on entity's ability to achieve its general objectives. A deficiency, therefore, may represent a perceived potential or real shortcoming, or an opportunity to strengthen internal control to increase the likelihood that the entity's general objectives will be achieved.

6. Monitoring internal control should include policies and procedures that ensure that the findings of audits and other reviews are adequately and promptly resolved. Managers are required to:

   i. Promptly evaluate findings from audits and other reviews, including those showing deficiencies and recommendations reported by auditors and others who evaluate agencies' operations,

   ii. Determine proper actions in response to findings and recommendations from audits and reviews; and

   iii. Complete, within established time frames, all actions that correct or otherwise resolve the matters brought to their attention.

7. The resolution process begins when audit or other review results are reported to Ministry, and is only completed after action has been taken that

   • corrects the identified deficiencies,

   • produces improvements, or

   • demonstrates that the findings and recommendations do not warrant Ministry action. The relation between the components of internal control and objectives of internal control is shown in the following diagram.
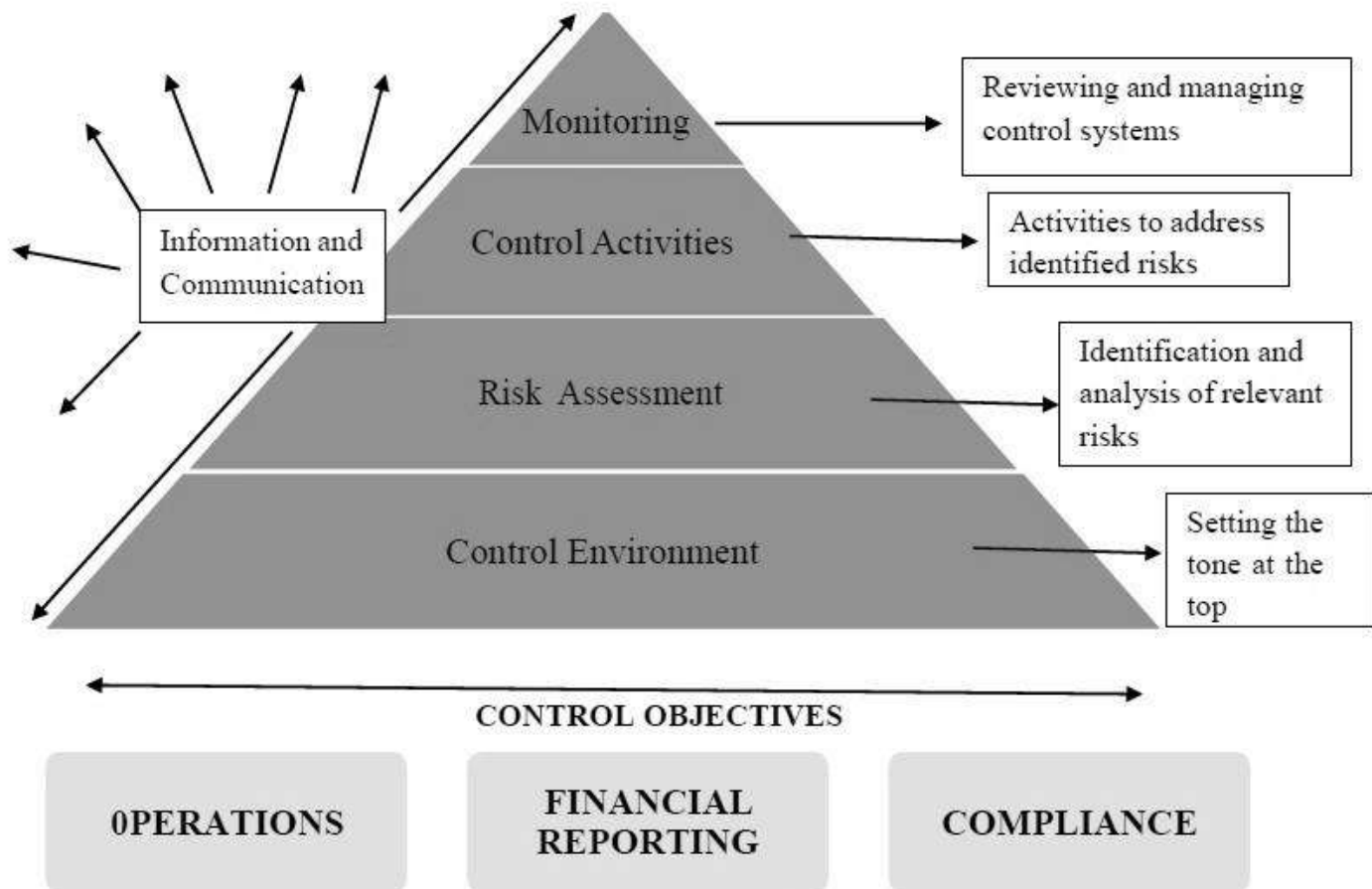
In the above context:

"Internal Control System means all the policies and procedures [internal controls] adopted by the Ministry to assist in achieving the objective of ensuring, as far as possible, the orderly and efficient conduct of operations, including adherence to policies, the safeguarding of assets, the prevention and detection of fraud and error, the accuracy and completeness of the accounting records, and the timely preparation of reliable financialinformation. The internal audit function constituted a separate component of internal control with the objective of determining whether other internal controls are well designed and properly operated." (Refer AAS 6 issued by the ICAI)

For controls to function effectively, Ministry must receive feedback about control activities in a timely and reliable manner. Hence, communication should flow down, across and up the Ministry, through all components and the entire structure. The internal control system should also be monitored through a well-designed process of review to ensure that it functions in an optimal manner. Monitoring activities normally comprise ongoing monitoring activities and /or separate evaluations. The scope and frequency of separate evaluations will depend primarily on an assessment of risks and the effectiveness of ongoing monitoring procedures. Internal control is most effective when controls are "built in" and not "superimposed" on the Ministry's systems and operations.

In-built controls support quality and empowerment initiatives, avoid unnecessary costs and enable quick response to changing conditions. By building internal control, it becomes part and integrated within the basic management processes of planning, executing and monitoring.

Internal control is not one vent or circumstance, but a series of actions that permeate an entity's activities. These actions are ongoing basis. They are pervasive and inherent in the way the Ministry runs.

Internal Audit, itself a critical component of the internal control system, is entrusted with this review function. As it is evident, like all controls, internal audit activities also entail costs and hence in keeping with overall objective of economy, efficiency and effectiveness of expenditure, the internal audit function must also be conducted with due regard to these principles.

4.1   INTERNAL CONTROL EVALUATION:

Evaluation is the process Ministry uses to determine whether:

- The Ministry/Department will likely achieve its goals and objectives;

- The elements of the organization's system of internal control are functioning effectively; and

- Risks to the organization and opportunities for improvement are being identified.

Evaluation involves periodic assessment of the Ministry's performance compared to established expectations or measurement standards.

Distinction between Monitoring and Evaluation:

Monitoring involves performing daily or routine procedures- like supervision. It helps to ensure operations are in compliance with the Ministry's system of internal control.

Evaluation involves doing periodic assessments of the Ministry's performance compared to established expectations or measurement standards.

4.2   MEANS OF INTERNAL CONTROL EVALUATION:

- Questionnaire/Checklists

- Flow Charts/Narratives

- Facilitated Workshops

- Control Self-Assessment

4.3   EFFECTED BY PEOPLE:

1) Internal control is accomplished by individuals within a Ministry. Consequently, internal control is effected by people. They should know their roles and responsibilities, and limits of authority. Although the Senior Officials primarily provides oversight, they also have overall responsibility for the internal control system. As internal control provides the mechanism needed to help understand risk in the context of the Ministry's objectives, the personnel will put internal control activities in place and monitor and evaluate them. Therefore, internal control is a tool used by the Ministry and is directly related to its objectives. Thus, all personnel in the Ministry play an important role in making it happen.

2) Similarly, internal control is affected by human nature. People do not always understand, communicate or perform consistently. Each individual brings to the workplace a unique background and technical ability, and has different needs and priorities. These realities affect, and are affected by, internal control.

5.1 INTERNAL CONTROLS PROVIDE ONLY REASONABLE ASSURANCE AND NOT ABSOLUTE ASSURANCE

1) No matter how well designed and operated, internal controls cannot provide an absolute assurance regarding the achievement of a Ministry's objectives. Reasonable assurance equates to a satisfactory level of confidence under given considerations of costs, benefits and risks.

2) Determining how much assurance is reasonable, requires judgment. In exercising that judgment, Ministry should identify the risks inherent in its operations and the acceptable levels of risk under varying circumstances, and assess risks both quantitatively and qualitatively.

3) Reasonable assurance reflects the notion that uncertainty and risk relate to the future, which no one can predict with certainty. Also factors outside the control or influence of the Ministry can affect the ability to achieve the objectives. Limitations also result from the following realities:

- human judgment in decision making can be faulty;

- breakdowns can occur because of simple errors or mistakes;

- controls can be circumvented by collision of two or more people;

- senior officials may override the internal control system; and

- decisions on risk responses and establishing controls need to consider the relative costs and benefits.

- These limitations preclude Ministry from having absolute assurance that objectives will be achieved.

4) Reasonable assurance recognizes the fact that the cost of internal control should not exceed the benefit derived. Cost refers to the financial measures of resources consumed in accomplishing a specified purpose like rupees spent and to the economic measure of lost opportunity, such as delay in operations, decline in service levels or productivity, or low employee morale. Benefit is measured by the degree to which the risk of failing to achieve stated objective is reduced. Examples include increasing the probability of detecting fraud, waste, abuse, or error; preventing an improper activity; or enhancing legal and regulatory compliance.

5) Designing internal controls that are cost beneficial while reducing risk to an acceptable level requires that officials clearly understand that overall objectives should be achieved. Systems with excessive controls in one area of operations may adversely affect other operations. For example, employees may try to circumvent burdensome procedures, inefficient operations may cause delays, and excessive procedures may stifle employee creativity and problem solving or impair the timeliness, cost or quality of services provided to beneficiaries. Thus, benefits derived from excessive controls in one area may be outweighed by increased costs in other activities.

5.2 LIMITATIONS ON THE EFFECTIVENESS OF INTERNAL CONTROLS

1) An effective internal control system, no matter how well conceived and operated, can provide only reasonable and not absolute assurance about the achievement of the Ministry's objectives or its survival. It can give information about the Ministry's progress, or lack of it, towards the achievement of the objectives. But internal control cannot change inherently poor personnel into a good one.

2) An effective system of internal control reduces the probability of not achieving the objectives. However, there will always be the risk that internal controls fail to operate as designed.

3) Because internal control depends on the human factor, it is subject to flaws in design, errors of judgment or interpretation, misunderstanding, carelessness, fatigue, distraction, collusion, abuse or override.

4) Shifts in government policy or programs, demographic or economic conditions are typically beyond management's control.

5.3 THE ROLE OF INTERNAL AUDIT IN INTERNAL CONTROL

1) Internal audit is very important component of internal control. Internal auditors examine the effectiveness of internal control and recommend improvements, but they do not have primary responsibility for establishing or maintaining it.

2) To achieve effective internal control, best practice requires a robust internal audit function complementary with other tools such as fraud controls, safety audit and program evaluation. Thus, one of the principal functions of internal audit is the examination of internal control systems. Internal audit provides the senior officials, with a valuable resource to evaluate internal control systems, and to provide assurance concerning the effectiveness of control systems. Internal audit is, in effect, part of the performance monitoring process.

WORKBOOK

1. What are the 3 general objectives of internal control?

   _____

   _____

   _____

2. Which is a widely accepted internal control frame work?

   _____

   _____

   _____

3. What are the 5 key components of internal control?

   _____

   _____

   _____

4. List 4 element of control of environment.

   _____

   _____

   _____

5. List five control activities.

   _____

   _____

   _____

6. What are the 2 groups of IT controls?

   _____

   _____

   _____

1387/198

7. Five categories of it general controls are

_____

_____

_____

8. Five examples of application controls.

_____

_____

_____

9. Quality of information is implied if the information is ?

_____

_____

_____

10. What do you mean by "tone at the top"?

_____

_____

_____

Unit - 6

Introduction to Risk Management and Fraud Risk Awareness

Learning Outcomes:

♦ Risks and Controls.

♦ Risk Management.

♦ Role of Internal Audit.

♦ Internal Auditor's Role in Risk Management.

♦ Fraud: Nature, Prevention and Detection.

♦ Fraud Indicators

Understanding Risk

A risk is anything that could jeopardize the achievement of objectives of a Ministry. The following questions should be asked by the Senior Officials while formulating a Ministry-wide policy/activity. The auditors, on the other hand, while evaluating internal control need to see if such issues have been considered while formulating policies and control activities.

• What could go wrong?

• How could we fail?

• What must go right for us to succeed?

• Where are we vulnerable?

• What assets do we need to protect?

• Do we have liquid assets or assets with alternative uses?

• How could someone steal from the Department?

• How could we know whether we are achieving our objectives?

• On what information do we must rely?

• On what do we spend the most money?

• How do we bill and collect our revenue?

• What decisions require the most judgment?

• What activities are most complex?

• What activities are regulated?

• What is our greatest legal exposure?

1.1 INTRODUCTION

(Refer the relevant Guidelines on Internal Audit provided in Draft Handbook on Internal Audit of the CGA, given in Unit 2 of this material)

The objective is to establish controls that prevent misuse and wastage of resources and facilitate achievement of objectives of Government of India. Thus, the present system of government financial management has a mechanism in place to guide departments in their day to day operations.

Audits, both external and internal, have traditionally sought to report on deviations from those controls by offices and officials in performance of their duties as part of regular work. Such audits, known as Compliance Audits or Regularity Audits have thus tried to improve governance, build up the public's trust in government and thereby strengthen democracy.

The primary difference between the traditional and modern approach to Internal Audit lies in the explicit recognition of the concepts of "risks" and "controls" in modern internal audit practice.

1.2 RISKS AND CONTROLS

Risks can be understood as the possibility of an event occurring that will have an adverse impact on the achievement of objectives. Every risk has two components, namely likelihood and impact. Hence, for the Ministry to be protected from the adverse impact of such risks, it is necessary that each risk identified is assessed and measured in terms of its impact (significance) and likelihood of occurrence (probability) and then an appropriate response is developed to address these risks.

For analyzing risks, the following questions can be asked:

i.   What can go wrong? (Risk Identification)

ii.   What is the probability of it going wrong? (Risk Likelihood)

iii.   What are the consequences? (Risk Impact)

Some activities are inherently more prone to risk than others, e.g. procurement activities would be more prone to risks than accounting for expenditure. Similarly, in other cases a change in circumstances may affect the risk structure, e.g. year-end expenditure may be driven by considerations to avoid lapse of budget and hence may necessitate closer monitoring of controls. The Ministry needs to identify its own risks as well as parameters for their categorisation as High, Medium and Low. Refer Figure below for an indicative categorization of risk likelihood. Similar categorisations would also be required for risk impact. Also refer later section on assessing risks.

Risk Likelihood	How Likely is the Risk to Occur?
High	It is highly likely to occur.
	Performance data shows evidence of an inability to meet the requirements.
	The process is extremely difficult to perform.
Moderate	It is probable or likely to occur.
	No data available to show the ability to meet requirements.
	The process is somewhat difficult to perform.
Low	It is unlikely that the risk will occur.
	Performance data shows evidence that the requirementswill be met.
	It is a common process and not difficult to perform.
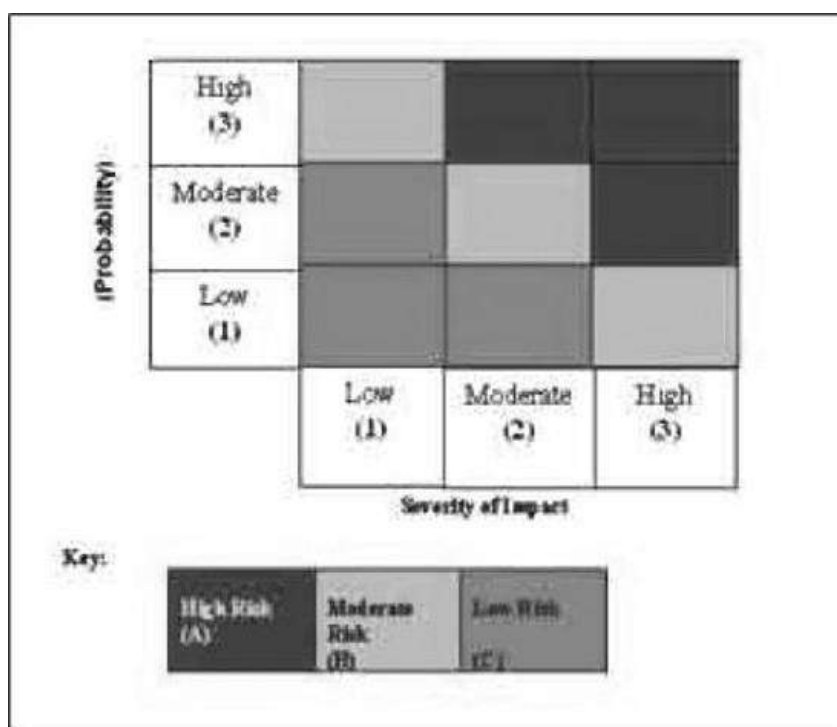
3.   RISK MANAGEMENT

3.1   RISK IDENTIFICATION

The first step in Risk management is identification. A strategic approach can be, identifying risks against key Ministry objectives. Risks relevant to the objectives are then considered and evaluated, resulting in a small number of key risks. Identifying key risks is important in order to allocate responsibility for management of these risks.

A Ministry's performance can be at risk due to internal or external factors at both the Ministry and activity levels. It is, therefore, important that risk identification is comprehensive.

Risk identification should be an ongoing, interactive process and is often integrated with the planning process.

3.2   RISK ASSESSMENT

1)   Risk assessment is the process of identifying and analyzing risks relevant to the achievement of the Ministry's objectives and determining the appropriate response. As stressed in the definition, internal control can provide only reasonable assurance that the objectives of the Ministry are being achieved. Risk assessment as a component of internal control, plays a key role in the selection of the appropriate control activities to undertake.

2)   Consequently, setting objectives is a precondition to risk assessment. Objectives must be defined before the risks to the achievement of these objectives can be identified and the necessary actions to manage the risks can be taken. That means having in place an ongoing process for evaluating and addressing the impact of risks in a cost - effective way and having staff with the appropriate skills to identify and assess the potential risks. Internal control activities are a response to risk and are designed to contain the uncertainty of outcome that has been identified.

3.3   RISK EVALUATION

1)   In order to decide how to handle risk, it is essential not only to identify in principle that a certain type of risks exist, but to evaluate its significance and assess the likelihood of the risk event occurring. The methodology for analyzing risks can vary, largely because many risks are difficult to quantify (e.g. risk to reputation and image) while others lend themselves to quantification (particularly financial risks). As such, risk evaluation, especially for the former is a subjective exercise.

2)   One of the key purposes of risk evaluation is to inform the Ministry about areas of risk where actions need to be taken and their relative priority. Therefore, it will usually be necessary to develop some framework for categorizing all risks. Generally, such categories will be as high, medium, and low. It is better to minimize the categories, as over refinement may lead to spurious separation of levels which in reality cannot be separated clearly.

3.4   RISK PROFILE

The result of the actions outlined above will be a risk profile for the Ministry.

3.5   DEVELOPMENT OF RESPONSES

After having identified and evaluated the risks, Ministries/ Departments need to develop a response to either eliminate the risk or to contain it within acceptable limits i.e. manage the risk. Internal control is one of the principal means by which risk is managed. Other devices used to manage risk include the transfer of risks to third parties, sharing risks, contingency planning and the withdrawal from unacceptably risky activities. The options available at this stage are to transfer, tolerate, terminate or treat the risk.

•   Obtaining insurance is an example of transferring the risk;

•   Risk may also be tolerated if the cost of appropriate control is so high as to outweigh the consequential benefits;

•   Termination of a risk may be necessitated if there is likelihood that presence of such risk may result in grave consequences or even in complete failure of the project/ scheme. This may sometimes call for cessation of the

activity itself - a decision not always possible in Governments because of the political and social sensitivities involved;

- However, treatment of risks through appropriate control activities is often the most obvious choice. Risk assessment should play a key role in the selection of appropriate control activities to undertake.

Some risk may still remain, even after instituting necessary controls, but it may be advisable to tolerate such "residual risk" especially if the costs to eliminate these are very high and they are within acceptable limits.

Acceptable risk is a risk that is understood and tolerated usually because the cost or difficulty of implementing an effective counter measure exceeds the expectation of loss. What is "acceptable risk" is a judgment exercised by the Ministry. Since controls have associated costs, it is important to ensure that the benefits of risk reduction are greater than the cost of controls.

Since governmental, economic, industrial, regulatory and operating conditions continually change, the risk environment of a Ministry is constantly changing, and priorities of objectives and the consequent importance of risks will shift and change. An ongoing, interactive process to identify changed conditions and take actions as necessary is fundamental to risk assessment. Risk models and related controls have to be regularly revisited and reconsidered in order to have assurance that the risk profile continues to be valid, that responses to risk remain appropriately targeted and proportionate, and mitigating controls remain effective as risks change over time.

The internal audit activity must evaluate risk exposures relating to the Ministry's governance, operations, and information systems regarding the:

- Achievement of the Ministry's strategic objectives;

- Reliability and integrity of financial and operational information;

- Effectiveness and efficiency of operations and programs;

- Safeguarding of assets; and

- Compliance with laws, regulations, policies, procedures, and contracts.

Determining whether risk management processes are effective is a judgment resulting from the internal auditor's assessment that:

- Ministry's objectives support and align with its mission;

- Significant risks are identified and assessed;

- Appropriate risk responses are selected that align risks with the Ministry's risk appetite; and

- Relevant risk information is captured and communicated in a timely manner across the Ministry; enabling employees to carry out their responsibilities.

The internal audit activity may gather the information to support this assessment during multiple engagements. The results of these engagements, when viewed together, provide an understanding of the Ministry's risk management processes and their effectiveness.

Risk management processes are monitored through ongoing management activities, separate evaluations, or both.

4.1 ROLE OF INTERNAL AUDIT

There must be a reasonable assurance that risks, which may adversely impact the achievement of Ministry's objectives, have been identified, assessed and have been "controlled" or managed within acceptable levels i.e. within the "risk appetite" of the Ministry. An effective internal audit mechanism is required to constantly evaluate these controls, report upon their adequacy and efficacy and ability to ensure mid-course corrections through an institutionalized follow up system.

Audits, both external and internal, have traditionally sought to report on deviations from these controls by offices and officials in performance of their duties as part of regular work. Such audits, known as Compliance or Regularity Audits have thus tried to improve governance, build up the public's trust in Government.

The primary difference between the traditional and modern approach to Internal Audit lies in the explicit recognition of the concepts of "risks" and "controls" in modern internal audit practice.

4.2 INTERNAL AUDITOR'S ROLE IN RISK MANAGEMENT

Below are specified 12 key actions for Pr. CCAs/CCAs in their role as CAEs and Internal Audit Wings to consider. By focusing on these key actions, Internal Audit Wings will be better positioned to meet the growing stakeholder requirements around risk.

The Internal Audit Wings are recommended to:

a.   Be advocates for the advancement of formal risk management processes in the Ministry/Department.

b.   Seek opportunities to help expedite the implementation of formal risk management, and sustain it when it is already in place.

c.   Strive to provide assurance on risk management as a whole, not just on individual risks.

d.   When providing risk management assurance, ensure the criteria for such assurance is well understood.

e.   When conducting a risk-based audit, link the scope and results to specific risks faced by the Ministry/Department.

f.   Continue to increase the percentage of the audit plan focused on risk management.

g.   Explore ways to integrate assurance with other internal assurance providers; combined and integrated assurance can be more effective and efficient.

h.   Periodically discuss with the Ministry/Department, the key risk areas to ensure internal audit's focus aligns with that of the Ministry/Department.

i.   Work with risk-related functions, where existing outside of Internal Audit Wings, to ensure appropriate leveraging and reliance on risk assessment efforts by all such functions.

j.   The risk assessment should, ideally, be updated as and when risks arise and not as per specified periodicity.

k.   While requests from Ministry/Department should typically be considered for an audit plan, be cautious to ensure such requests do not divert valuable internal audit resources from higher-risk areas.

Continue to grow internal audit capabilities around risk to ensure internal audit functions can meet the changing stakeholder expectations of the future in an environment that increasingly becomes more complex and riskier.

5.1   FRAUD – NATURE, PREVENTION AND DETECTION

DEFINITION FROM THE IIA GLOSSARY

Fraud is "any illegal act characterized by deceit, concealment, or violation of trust. These acts are not dependent upon threat of violence or physical force. Frauds are perpetrated by parties and organizations to obtain money, property, or services; to avoid payment or loss of services; or to secure personal or business advantage."

5.2   EFFECTS OF FRAUD

a.   Monetary losses from fraud are significant, but its full cost is immeasurable in terms of time, productivity, and reputation, including customer relationships.

b.   Thus, a Ministry should have a fraud control programme that includes awareness, prevention, and detection programs. It also should have a fraud risk assessment process to identify fraud risks.

5.3   CAUSATIVE FACTORS OF FRAUD

a.   Pressure or incentive is the need the fraudster, thereby trying to satisfy by committing the fraud.

b.   Opportunity is the fraudster's ability to commit fraud. This characteristic is the one that the organization can most influence, e.g., by means of controls and procedures.

c.   Rationalization is the fraudster's ability to justify the fraud.

5.4   EXAMPLES OF FRAUD

a.   Asset misappropriation is stealing cash or other assets (supplies, inventory, equipment, and information). The theft may be concealed, e.g., by adjusting records. An example is embezzlement, the intentional appropriation of property entrusted to one's care.

b.   Skimming is theft of cash before it is recorded, for example, accepting payment from a customer but not recording the sale.

c.   Disbursement fraud involves payment for fictitious goods or services, overstatement of invoices, or use of invoices for personal reasons.

d.   Expense reimbursement is payment for fictitious or inflated expenses, for example, an expense report for personal travel, non-existent meals, or extra mileage.

e.   Payroll fraud is a false claim for compensation, for example, overtime for hours not worked or payments to fictitious employees.

f.   Financial statement misrepresentation often overstates assets or revenue or understates liabilities and expenses. Management may benefit by selling stock, receiving bonuses, or concealing another fraud.

g.   Information misrepresentation provides false information, usually to outsiders in the form of fraudulent financial statements.

h. Corruption is an improper use of power, e.g., bribery. It often leaves little accounting evidence. These crimes usually are uncovered through tips or complaints from third parties. Corruption often involves the purchasing function.

i. Bribery is offering, giving, receiving, or soliciting anything of value to influence an outcome. Bribes may be offered to key employees such as purchasing agents. Those paying bribes tend to be intermediaries for outside vendors.

j. A conflict of interest is an undisclosed personal economic interest in a transaction that adversely affects the organization or its shareholders.

k. A diversion redirects to an employee or outsider a transaction that would normally benefit the organization.

l. Wrongful use of confidential or proprietary information is fraudulent.

m. A related party fraud is receipt of a benefit not obtainable in an arm's-length transaction.

n. Tax evasion is intentionally falsifying a tax return.

6.1 DIVISION OF RESPONSIBILITIES

a) Control is the principal means of preventing fraud.

1) Management is primarily responsible for establishing and maintaining control.

2) Internal auditors are primarily responsible for preventing fraud by examining and evaluating the adequacy and effectiveness of control.

3) They are not responsible for designing and implementing fraud prevention controls.

4) Internal auditors are not expected to detect all fraud.

5) Internal auditors must exercise due professional care by considering, among other things, the "probability of significant errors, fraud, or noncompliance."

6) Thus, internal auditors must consider the probability of fraud when developing engagement objectives

6.2 COMPONENTS OF A FRAUD PREVENTION SYSTEM

a. Fraud prevention involves actions to discourage fraud and limit the exposure when it occurs. A strong ethical culture and setting the correct tone at the top are essential to prevention.

b. Overlapping control elements of a fraud prevention program are presented below and on the next page. They are based on the COSO control framework.

1) The control environment includes such elements as a code of conduct, ethics policy, or fraud policy.

2) A fraud risk assessment generally includes the following:

a) Identifying and prioritizing fraud risk factors and fraud schemes. The internal audit activity must evaluate the potential for the occurrence of fraud and how the organization manages fraud risk.

b)   Mapping existing controls to potential fraud schemes and identifying gaps

c)   Testing operating effectiveness of fraud prevention and detection controls

d)   Documenting and reporting the fraud risk management

3)   Control activities are policies and procedures for business processes that include authority limits and segregation of duties.

4)   Fraud-related information and communication practices promote the fraud risk management program and the organization's position on risk. The means used include fraud awareness training and confirming that employees comply with the organization's policies.

a)   A fraud hotline can open the channel of communication for employees to report suspected improprieties.

5)   Monitoring evaluated antifraud controls through independent evaluations of the fraud risk Management program and use of it.

6.3   RESPONSIBILITY FOR DETECTION

a.   Internal auditors are not responsible for the detection of all fraud, but they always must be alert to the possibility of fraud.

b.   An internal auditor's responsibilities for detecting fraud include evaluating fraud indicators and deciding whether any additional action is necessary or whether an investigation should be recommended.

6.4   FRAUD –INDICATORS

Understanding the link between weak internal control and fraud.

•   Weak internal controls not only permit fraud; they actually encourage it.

Costs of fraud:

•   Loss of public confidence in Government

•   Loss of reputation of the innocent

•   Punishment of fine perpetrator

Fraud prevention:

•   Commitment to maintain good controls

•   Elected officials' support for Ministry's commitment to controls

How to control the fiduciary risk of fraud:

•   Follow-up on adverse indicators

- Check the control documents

- Careful examination of unusual transactions

- Analytical review of transactions through sources

Most common types of fraud:

- Missing assets/inventory

- Pilfering

- Inflated travel claims

- Double payments

- False claims

- Payroll fraud

In short, bypassing the regulatory framework is the most common anatomy of any fraud. The audit trail will be available through control documents like cash back, stock ledger, bin cards, etc.

6.5 LOW-LEVEL FRAUD VS. EXECUTIVE FRAUD

a) Fraud committed by staff or line employees most often consists of theft of property or embezzlement of cash. The incentive might be relief of economic hardship, the desire for material gain, or a drug or gambling habit. Stealing petty cash or merchandise, lapping accounts receivable, and creating non-existent vendors are common forms of low-level fraud.

Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the Ministry, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

b) Fraud at the executive level is very different. The incentive is usually either maintaining or increasing the stock price, receiving a large bonus, or both. This type of fraud consists most often of producing false or misleading financial statements.

6.6 TERMINOLOGY OF FRAUD INDICATORS

a. A document symptom is any kind of tampering with the accounting records to conceal a fraud. Keeping two sets of books or forcing the books to reconcile are examples.

b. Situational pressure can be personal (e.g., financial difficulties in an employee's personal life) or organizational (e.g., the desire to release positive news to the financial media).

c. Opportunity to commit is especially a factor in low-level employee fraud. Poor controls over cash, merchandise, and other organizational property, as well as lack of compensating accounting controls, are enabling factors.

d. A lifestyle symptom is an unexplained rise in an employee's social status or level of material consumption.

e. Rationalization occurs when a person attributes his or her actions to rational and creditable motives without analysis of the true and especially unconscious motives. Feeling underpaid is a common rationalization for low-level fraud.

f. A behavioral symptom (i.e., a drastic change in an employee's behavior) may indicate the presence of fraud. The guilt and the other forms of stress associated with perpetrating and concealing the fraud may cause noticeable changes in behavior.

6.7 PROCEDURES FOR DETECTION

The nature and extent of the procedures performed to detect fraud depend on the circumstances of the engagement, including the features of the Ministry and the internal auditor's risk assessment. Accordingly, no text can feasibly present lists of all procedures relative to fraud. However, analytical procedures are routinely performed in many engagements. They may provide an early indication of fraud. Analytical procedures are performed to assess information collected in an engagement. The assessment compares information with expectations identified or developed by the internal auditor.

6.8 SOME INDICATORS OF POSSIBLE FRAUD

Frauds and their indicators (often called "red flags") take different norms:

1. Lack of employee rotation in sensitive positions such as cash handling

2. Inappropriate combination of job duties

3. Unclear lines of responsibility and accountability

4. Unrealistic sales or production goals

5. An employee who refuses to take vacations or refuses promotion

6. Established controls not applied consistently

7. High reported profits when competitors are suffering from an economic downturn

8. High turnover among supervisory positions in finance and accounting areas

9. Excessive or unjustifiable use of sole-source procurement.

10. An increase in sales far out of proportion to the increase in cost of goods sold.

11. Non-maintenance of records (accounting/beneficiary selection).

12. Non-maintenance of entries by competent Authority.

13. False reporting, lack of correlation between physical and financial achievements.

14. Very low effectiveness can also be a fraud indicator. Ex. 1000 beneficiaries trained and out of them some 10-20 succeeded and got employment or self-employment.

15. Anything unusual in normal circumstances may be the indicator and need to be paid attention.

WORKBOOK

1.   The primary difference between the traditional and modern approach to internal audit lies in the recognition of

_____ and _____ in modern internal audit?

2.   What are the 2 components of risk?

_____

_____

_____

3.   What are the 3 categories for likelihood and impact of risk?

_____

_____

_____

4.   What is the first step in the risk management process?

_____

_____

_____

5.   What are the four options to respond to a risk?

_____

_____

_____

6   Fraud is characterized by _____ , _____ and _____ .

7.   Monetary losses for fraud are significant but its full cost is _____ ?

8.   Name the 3 causative factors of fraud?

_____

_____

_____

9.   Give 5 examples of fraud.

_____

_____

_____

10.   _____ is the principal means of preventing fraud.

11.   Internal audit is expected to detect all frauds. (True or false)

_____

_____

_____

12.   What are internal audit's responsibilities for detecting fraud?

_____

_____

_____

13.   What are the costs of fraud?

_____

_____

_____

14.   Most common types of fraud.

_____

_____

_____

15.   Name 3 red flags.

_____

_____

_____

Unit - 7
Conduct of Internal Audit - Planning and Execution

Learning Outcomes:

♦ How to conduct a Government Internal Audit/ Stages in Government Internal Audit:

♦ Planning and Preparation of Audit Engagement.

♦ Performing the Audit Engagement.

♦ Reporting and Follow-up.

♦ Quality in Internal Audit Reporting.

♦ Review of Pending Audit Issues in Audit Committee Meeting.

INTRODUCTION

The internal audit process comprises five main phases:

● Planning the audit engagement;

● Preparing for Audit;

● Performing the audit engagement;

● Reporting upon the audit engagements; and

● Follow-up Action

(Refer the relevant Guidelines on Internal Audit provided in Draft Handbook on Internal Audit of the CGA, given in Unit 2 of this material)

These phases can be seen at the level of the individual audit engagements and also for the internal audit function for the Ministry.

At the individual audit engagement level, the internal auditor:

- establishes what is going to be audited (planning),

- gathers relevant information from internal and external sources and prepares a work programme (preparation),

- implements the approved plan (performing),

- communicates the results achieved (reporting) and reports on implementation of agreed improvement measures (follow up).

It should also be noted that while internal auditing consists of the above-noted phases, detailed methodology including audit programs and relevant testing may need to be tailored to a specific internal audit, e.g. information technology, finance, operations, etc. For ease of understanding, these phases can be compressed into the planning, execution and reporting phase. Further, if the primary focus of the internal auditing engagement is advisory rather than assurance, the process may be amended in consultation with the Chief Audit Executive of the Ministry.

1.2   Planning of the audit engagements should include preliminary survey and research about the unit to be audited. The input of senior officials and the Board is typically included in this process. Background study about the scheme/operations/activity of the audited unit will give an idea about the activities undertaken and controls present in the system and would help in deciding the focus and approach of the audit engagement. The appropriate level of testing and evaluation of Controls would be decided upon, depending on the time and resources available. Some basis for this testing exercise must also be considered and documented (Random sampling, judgmental sampling etc.).

1.3   The audit report or the final engagement communication should be issued mentioning the key findings of audit. The report should be concise and bring out all significant and material observations. The findings should be supported by audit evidence which should form a part of the working papers. There should be proper indexing of working papers given as annexures to the report. Also, the audit observations included in the main body of the report and evidence mentioned in the annexure should be appropriately referenced and the cross-referenced.

2.1   TYPICAL INTERNAL AUDIT ASSIGNMENT INVOLVES THE FOLLOWING STEPS:

1. Establish and communicate the scope and objectives for the audit to appropriate management.

2. Develop an understanding of the operational area under review. This includes objectives, measurements and key transaction types. This involves review of documents and interviews. Flowcharts and narratives may be created if necessary.

3. Describe the key risks facing the business activities within the scope of the audit.

4. Identify control procedures used to ensure each key risk and transaction type is properly controlled and monitored.

5. Develop and execute a risk-based sampling and testing approach to determine whether the most important controls are operating as intended.

6. Report the problems identified and negotiate action plans with management to address the problems.

7. Follow-up on reported findings at appropriate intervals. Internal audit departments maintain a follow-up database for this purpose.

Duration of audit assignments vary based on the complexity of the activity being audited and internal Audit resources available. Many of the above steps are inter relative and may not all occur in the sequence indicated. By analyzing and recommending business improvements in critical areas, auditors help the organization to meet its objectives. In addition to assessing business processes, Information Technology (IT) Auditors also review information technology controls.

2.2   PLANNING AND PREPARING FOR AUDIT ENGAGEMENTS

Audit planning comprises both development of a macro plan (Annual Audit Programme) and audit plans for specific audit assignments. The plan establishes the priorities of the internal audit activity, consistent with the Ministry's goals and objectives.

2.3   ANNUAL AUDIT PROGRAMME

The Annual Audit Programme is developed in consultation with Senior Officials of the Ministry/Department after factoring in the changes in external and internal environment. To facilitate smooth conduct of audit engagements, annual audit programmes should be finalized by 15th January every year and communicated to various auditee units and other stakeholders giving sufficient notice. A copy of the annual plan should also be sent to the O/o CGA. Since it would not be possible for the Internal Audit Wings to audit all units every year, prioritization is necessary. Risk analysis and availability of audit resources are important considerations while deciding audit priorities. Efforts should be made however to audit key activities or units every year while ensuring that other units are also covered within a defined period.

 While preparing the Annual Audit Programme, it would be safe to plan for about 210 working days (after deducting weekly holidays, public holidays, eligible leave, time required for travel, preparation of reports, follow up activities, training etc.,). If previous experience suggests that special audits may also need to be undertaken, then the requirements thereof should also be factored in. Working days required for each unit may be decided on the risk analysis specific to the unit. Ex: Expenditure is more; number of beneficiaries is more may require more days. An average of 10 working days may be kept for regular audits and 15-23 days for special audits. Given the number of audit teams (1 Sr.AO/AO, 2AAOs, 2 Accountants) available in the Ministry, the number of units to be audited can be decided. The parameters mentioned earlier could be used to select the units to be audited in the audit cycle covered by the Annual Audit Programme.

2.4   DEVELOPMENT OF ANNUAL AUDIT PROGRAMME

The annual work program outlines a prioritized list of proposed audit engagements, including the indicative audit scope for each engagement and an estimate of required resources.

2.5   REVIEW AND UPDATING OF AUDIT UNIVERSE

The audit universe is the aggregate of all areas that are available to be audited within the Ministry / Department. To define the universe, the Ministry can be organized / segregated into auditable activities/ units, which may be defined by function or activity, by organizational unit or division, or by project or program, etc. Some examples of auditable activities include information systems, major contracts and functions such as procurement, payment and accounting. The

budgetary allocations to the units/ schemes etc., are also a consideration in deciding upon the audit universe. The audit universe should be carefully selected and emphasis should be on Risk Assessment and critical areas of operations of the Ministry. The annual assessment of risks within the audit universe and the identification of manageable audit engagement entities establish the internal audit priorities.

3.1   RISK ASSESSMENT AND PRIORITIZATION

The Risk Assessment process should be an elaborate exercise conducted in coordination with various executive authorities of the Ministry. This should decide upon the processes/units/activities/schemes which should be audited. The priorities should be on the basis of risk perception and rating of the Ministry. While selecting the number of units of similar types to be audited, a random sampling technique should be used so that the selected sample is representative of the actual population. A part of judgmental sampling may also be used for selecting areas, States and/ or Districts for auditing. The risk assessment and work program preparation process should be reviewed regularly and refined as necessary to ensure that it remains efficient and comprehensive and provides adequate documentation of key decisions. This should be decided in consultation with the Audit Committee. The detailed audit program assigning resources for the individual audits would be decided by the Chief Audit Executive of the Ministry.

3.2   IDENTIFICATION OF PROCESSES AND AREAS WITH HIGH RISK RATING

Based on the risk rating exercise the work program of internal audit would be finally developed. In the initial stages, this exercise would involve substantial judgment of the auditors and executive authorities. The process would mature once Risk Registers are developed in the Ministries and Risk Committees are put into place and become functional and active.

3.3   INCLUSION OF SPECIAL AUDIT ENGAGEMENTS INTO WORK PROGRAMS

Special audits, as and when assigned by the Ministry, would be undertaken by the Internal Audit Wing as per Terms of Reference given by the Ministry. The Audit Committee should be informed about these engagements subsequently.

3.4   PLANNING INDIVIDUAL AUDITS

Internal Audit activities involve expenditure of public funds. Hence, it is important that each audit engagement is conducted in an economical, efficient and effective manner. Developing an audit plan for each audit engagement is the first step in this direction.

3.5   PLANNING THE AUDIT ENGAGEMENTS

During this phase of the engagement, the supervisor and team members develop a good working knowledge and understanding of the business objectives, processes, operations and associated risks of the subject of the audit engagement, including recent changes in major systems. On completion of this phase, the audit team would have identified and documented the significant risks and key controls at the audit engagement level, evaluated the effectiveness of design of these controls and developed plans to test their operating effectiveness.

4.1   BACKGROUND STUDY AND RESEARCH BY THE AUDIT TEAM ABOUT THE AUDIT UNIT TO UNDERSTAND ITS BUSINESS OPERATIONS AND CRITICAL PRIORITY AREAS

The objectives of audit unit/scheme/activity of the government should be understood well so that the focus of audit is aligned to achievement of objectives of the audit unit/scheme/activity. Audit team members should initiate an in-depth review of the subject of the engagement so as to develop a sound understanding of its management and business processes and practices, policies, procedures, external and internal environment. It is important to keep in mind any significant and recent or proposed changes to the subject of the engagement and any issues of Ministry concern. Knowledge gained through audit engagements and other sources should be used to update this information and to develop an improved understanding, particularly in respect of schemes being implemented by the Department.

4.2   PRELIMINARY ANALYSIS OF KEY CONTROLS AND RISKS FACED BY THE MINISTRY

Risks involved in running a department depend upon operations of the department. It is important to consider information obtained from the assessment of risks and key controls at the institutional level when assessing risks and related controls at the audit unit level. In this respect, the auditors determine whether significant entity-wide risks were identified at the institutional level that must be assessed at the audit engagement level. If such entity-wide risks have been identified, the auditor documents the key controls established at the audit engagement level to address the risks and evaluates the design effectiveness of those key controls. To do so, the auditor identifies the control objectives for the relevant key activities, processes or systems under review, the auditor assesses whether the significant entity-wide risks could impact on the achievement of the identified control objectives. If so, then the auditor reviews the internal control design and identifies the corresponding key controls designed to mitigate the risks in achieving the control objectives, if so, then the auditor reviews the internal control design and identifies the corresponding key controls designed to

mitigate the risks to achieving the control objectives. Evaluation of compliance to the controls specified in the various codes, manuals and government orders is then carried out to assure effectiveness of controls in fulfilling the objectives.

4.3 DEVELOPMENT OF ENGAGEMENT OBJECTIVES ALONG WITH SCOPE, CRITERIA AND APPROACH

Once a good understanding of the subject of the engagement has been acquired, risks have been identified, key controls have been documented and the design effectiveness of controls have been evaluated, the audit team confirms the engagement's objectives and identifies the detailed scope for the next phase of the audit, taking into consideration the objectives and scope of the audit. The objectives address whether the governance risk, risk management and control processes of the subject of the engagement provide reasonable assurance that :

- Significant financial, managerial and operating information is accurate, reliable and timely;

- Resources are acquired economically and used efficiently;

- Assets are safeguarded;

- Actions of the Ministry/Department are in compliance with policies, procedures, contracts and applicable laws and regulations; and

- Significant programs, plans and business objectives will be achieved.

The engagement objective is a board statement that is often thought of as a question that the auditor seeks to answer. The auditor is expected to draw a conclusion with respect to each objective. In planning the detailed audit work to be performed, the auditor must ensure that the work will result in sufficient evidence to meet the objectives of the audit engagement.

4.4 FINALIZATION OF AUDIT PLAN

It is important that the auditor reviews each identified audit objective and determines whether after completion of the audit engagement and after sufficient evidence has been obtained, a conclusion can be arrived at. To do so, the auditor must take into consideration the extent to which significant activities, process or systems are identified to test operating effectiveness of key controls at the audit engagement level. The detailed scope statement clearly describes the areas, processes, activities or systems that will be the subject of the audit engagement and to which conclusions will apply. It also addresses the time period and locations, particularly if there are geographical limitations to the audit. The statement also indicates any issues or areas that have been excluded from the scope of the audit.

4.5 DEVELOPMENT OF SAMPLE AUDIT WORK PROGRAM FOR A FEW SCHEMES

The detailed Internal Audit Manual should identify some key schemes in the Ministry and develop standard testing and working methodology for audit of these schemes. A checklist approach may be used in developing an illustrative work program. This will facilitate an efficient audit of the selected scheme and other scheme being implemented by the Ministry.

To sum up, for any project, good planning is half the job done. Internal Audit is no exception but it is generally given a low priority because auditors are in a hurry to get on with the job. Audit plan ensures high quality of audit and provides evidence of internal audit's due diligence. The importance of audit plan cannot be overemphasized and Internal Audit Wings in Ministry/ Department would do well to make this a standard practice. Moreover, although an initial audit plan is prepared, audit planning continues throughout the audit period as additional information is gathered.

5.1 PERFORMING THE AUDIT ENGAGEMENT

Once the audit program has been finalized, the same should be communicated to the auditee units 30 days before the commencement of audit so that they are ready with records and are prepared for audit. The audit team may also send a questionnaire along with the communication.

5.2 INTIMATION OF AUDIT

Before the commencement of any audit, the concerned unit should be informed about the schedule of the audit. For this purpose, a commencement letter should be sent to the head of the audited department at least a month before the audit is to be initiated so as to provide sufficient time to arrange the necessary records and resources for a smooth conduct of the audit. The Commencement Letter should be addressed to the highest individual responsible for the function/ department and at least include the following details:

- Objective of audit
- Scope of the audit and period it shall cover
- Estimated duration of the audit
- Names of Auditors especially indicating name of the Team Leader
- Information regarding entry and exit conferences.
- Request for necessary information and documents.

5.3 OPENING MEETING (ENTRY CONFERENCE)

Internal Audit engagements normally start with an entry conference, a meeting between the internal auditors and the Head of Department/Head of Office of the Ministry being audited. The primary purpose of this meeting is to establish an appropriate environment for the audit. In this meeting, internal auditors communicate the proposed objectives and scope of the audit engagement and seek to understand the objectives and risk management practices in the Ministry. Issues or areas of special concern that the auditee Ministry/Department would like audit to address and logistical details (nodal officer to coordinate audit requirements of space, records, meetings, etc.) are also discussed in the entry conference. Thus, the audit objectives, detailed scope, approach and testing plan for performing the audit objectives, detailed scope, approach and testing plan for performing the audit, communication and reporting strategy are identified along with the Ministry's representative who would be responsible for coordinating management action plans and monitoring the status of implementation of recommendations.

The entry conference sets the tone for effective audit by establishing effective communication lines with the auditee unit. It also helps the internal auditor to validate the information he had gathered during the planning stage and assess the attitude and perception of the key personnel towards controls. Audits with an element of surprise do not have any entry conference.

5.4 DOCUMENTATION OF MEETINGS

All the meetings with the audit client should be appropriately documented and minuted. These minutes should form a part of working papers relating to the audit engagement.

5.5 REQUISITIONING APPROPRIATE RECORD AND METHODOLOGY FOLLOWED FOR TESTING OF CONTROLS

The audit team should send requisition of appropriate records from the audit client well in advance. The audit memos should clearly mention the list of records called by the audit team along with date and also give details of any statement required to be prepared by the client. If the data is present in the soft form, a copy of database may be taken for preliminary analysis. The auditor now tests the operating effectiveness of key controls identified at the audit engagement level, including those controls designed to address the significant entity-wide risks (identified at the institutional level in the relevant governance audit/s) that impact on achievement of objectives at the audit engagement level.

The detailed testing and sampling plan, audit work performed, and results from assessments of the operating effectiveness of the activities, processes or systems under review are documented. Operating effectiveness refers to the effectiveness of the operation of an internal control activity. The operation is not effective when a properly designed key control is not operating as designed (or as planned) or the person performing the control does not possess the necessary authority or qualifications to perform the key control effectively.

Because the results of several audit tests will likely be summarized to form a conclusion with respect to one or more audit criteria or objectives, results of each audit test and the evidence gathered is documented on the applicable matrix (or referenced to supporting documentation) to ensure that the following is evident: Engagement objective and criterion to which the test is linked

- Sources of information used to design the test;

- Means by which the test was conducted

- Test results and their analysis; and

- Observations and recommendations made

5.6   AUDIT EVIDENCE: is the information collected, analyzed, and evaluated by the auditor to support an audit observation audit evidence relates both to the quantity and quality (or reliability) of evidence to be obtained by auditors. It is important for auditors to obtain sufficient, appropriate and reliable audit evidence to enable them to draw reasonable conclusions on which to base their audit opinions. Sufficiency is the measure of quantity of audit evidence while appropriateness refers to reliability of the audit evidence and its relevance to a particular assertion. Evidence is considered appropriate when it is both relevant and reliable.

5.7   RELIABILITY OF AUDIT EVIDENCE

The reliability of audit evidence is influenced by its source which may either be internal or external; and by its nature which may be visual, documentary or oral. The auditor must be aware of the following matters in assessing the reliability of audit evidence:

a.   Audit evidence from external sources (for example, confirmation received from a third party) is more reliable than that obtained from the Ministry's records;

b.   Audit evidence obtained from the entity's records is more reliable when the related accounting and internal control system operates effectively;

c.   Audit evidence obtained directly by auditors is more reliable than that obtained by or from the Ministry/ Department;

d.   Audit evidence in the form of documents and written representations are more reliable than oral representations; and

e.   Original documents are more reliable than photocopies, telexes or facsimiles.

f.   Large samples are more reliable than smaller ones and statistical samples more persuasive than non-statistical samples.

Evidence collected during the process of audit should be carefully documented. When the audit evidence obtained from different sources are consistent with one another, they become persuasive to the auditor. However, when the auditor's evaluation of audit evidence suggests that evidence from one source is inconsistent with that from another, it is the responsibility of the auditor to determine what additional procedures must be undertaken to resolve the inconsistency. Decisions regarding the type of evidence to seek, the audit approach used to obtain it, and how much evidence is sufficient require both due diligence and professional judgment.

5.8   DEVELOPMENT OF WORKING PAPER FOR THE ENGAGEMENT

Working papers are the supporting documents for the entire audit engagement. They provide a complete audit trail and demonstrate, in detail, how the audit engagement was performed. Working papers also contain the evidence to support the final summary of observations and the final audit report. More specifically, working papers support the observations, recommendations and audit engagement rating and provide a demonstrable link between reports issued and the work performed. In addition, working papers can be used to:

•   justify and provide proof of work performed, and help auditors respond to questions about coverage or results;

•   document reasons for removing observations and/or recommendations that were included in earlier versions of reports;

•   facilitate supervisory quality assurance reviews;

•   provide supporting evidence when external auditors or other reviewers want to rely on the results.

The working papers should be appropriately indexed and should have the requisite evidence to support the audit observation. There should be referencing and cross-referencing of the working papers with the relevant audit observations to make it more meaningful and useful for stakeholders.

5.9   DEVELOPMENT OF AUDIT OBSERVATIONS

Audit observations emerge through a process of comparing "what should exist" (the audit criteria) with "what exists" (the audit evidence). When there is a difference between "what exists" and "what should exist," the auditor assesses the effect, impact and cause associated with the variance and documents it as an observation. The accumulating of observations provides the auditor with the necessary foundation on which to develop the audit engagement conclusions, recommendations and audit report.

Permanent Audit File contains information that is relevant to current and future audits as it consolidates all important documents at one place. It also provides a basis for consistency in testing and allows comparison of key performance indicators over time. Permanent audit files typically include (i) organizational chart; (ii) description of schemes, programs, systems, procedures and business plans; (iii) corrective action plans; (iv) legal and regulatory issues impacting the organization; (v) risk assessment; (vi) correspondence of continuing interest future audit; (vii) updated audit programmes.

Current Audit File contains record of all the audit work schedules and documents relevant to the current audit. These should represent a clear record of the audit process, procedures, findings, conclusions and reports. Current audit files typically include (i) copies of the draft and final audit reports; (ii) significant findings and issues identified during the audit and how they were resolved; (iii) audit planning documentation; (iv) administration/correspondence documents; (v) follow-up of previous audit reports; (vi) updated audit programmes; (vii) supporting documentation for the audit conclusions; (viii) minutes of entry and exit meeting.

5.10   CONDUCTING EXIT MEETING WITH THE AUDIT CLIENT

Monitoring the quality of audit work is imperative for an efficient and effective audit. The supervisor must discharge this duty with due care and especially review the documentation; evidence gathered by individual auditors and the audit conclusions. Once the supervisor has satisfied himself that audit has been completed, in accordance with the audit plan he should review all working papers, check supporting evidence for audit observations and prepare a draft report highlighting the weaknesses in design and implementation of the internal control system, instances of non-compliance with policies, prescribed procedures, rule and regulations and transactions which do not measure up to standards of propriety. The draft report should be sent to the Head of Department/Head of Office for obtaining Department's views on audit observations.

Providing a draft report with findings for review and comment by responsible officials of the audited entity and others helps the auditors to develop a report that is fair, complete, and objective. Including the views of responsible officials results in a report that presents not only the auditors' findings, conclusions and recommendations, but also the perspectives of the responsible officials of the audited entity and the corrective actions they plan to take makes the report more meaningful.

An exit meeting should be held with key officials of the Ministry/Department/Auditee unit being audited to discuss the draft internal audit report.   This meeting should aim to obtain the views of the officials on each audit observation including additional facts that the Ministry may wish to provide, which would then be analyzed and the auditor may agree to reconsider his conclusions in the light of the information provided by the management. Evaluation of the comments should also be included in the report, as appropriate. If the audited entity refuses to provide comments or is

unable to provide comments within a reasonable period of time, the auditors may issue the report without receiving comments from the audited entity. In such cases, the auditors should indicate in the report that the audited entity did not provide comments.

In case of disagreement, views of the Department and reasons for disagreement should be taken on record. It is expected that upon conclusion of this meeting, the draft internal audit report becomes an agreed document between the department and the internal audit. Discussions during the exit conference should be minute and form part of the audit working papers. A copy of the minutes should also be given to the department for their information.

6.1   REPORTING AND FOLLOW-UP

Audit reports are the end products of audit engagements. Hence, the auditors should take utmost care in drafting the report. The Audit Reports must be accurate, objective, clear, concise and complete and should be issued in a timely manner (normally within a fortnight of completion of the audit engagement) to facilitate initiation of appropriate remedial action. The reports must satisfy audit objectives and measure up to the expectations of senior officials and audit committee. Satisfactory performance of the auditee unit, whenever evident, should also be acknowledged in the Reports.

Audit Reports should carry the legend "Internal Audit Report of   name of Ministry   for the period   " on the cover page and should also mention the date of issue of the audit report. Further it should clearly mention that establishing appropriate internal controls and preparation of financial statement are the responsibilities of management and responsibility of auditor is to express opinion on efficiency of internal controls in achieving management objectives. Each Audit Report must be approved by the competent authority, signed by the authority designated for this purpose and addressed to the authority as mentioned in the internal audit charter.

It is desirable that audit reports have an executive summary which contains details of audit objectives, scope of audit, summary of audit observations and highlight the significant observations which require immediate action on part of senior officials.

6.2   REPORT DRAFTED USING 5C FRAMEWORK

The audit observations should be developed by using 5C framework with reference to engagement objectives:

Criteria: What should exist? The benchmarks or expectations identified as the basis against which audit evidence is compared.

Condition: What exists? The factual evidence found in the course of the audit. The condition identified the nature and the extent of the observation. A clear and accurate statement of condition evolves from the auditor's comparison of actual evidence with appropriate criteria.

Consequence/Effect/Impact: What effect did it have? The risk or exposure to the institution and/ or others as a result of the difference between the criteria and the condition should be recorded. The effect establishes the actual or potential impact of the condition. The significance of a condition is usually judged by its effect. It can be expressed in quantitative terms. To warrant reporting, an effect should be sufficiently serious to justify the action (and related cost) to correct the difference (the deficiency).

Cause: What did it happen? The possible or likely reason for the difference between the expected and actual condition

should be explored. The cause may be obvious or may be identified by deductive reasoning. The identification of similar causes for a number of observations may highlight an underlying them to which an audit recommendation should be addressed. Identification of the cause of an unsatisfactory condition is a prerequisite to making a meaningful recommendation for corrective action.

Corrective Action/Recommendation: What should be done? The actions suggested or required to correct the situation and prevent future occurrences. The relationship between the audit recommendation and the underlying cause of the condition should be clear and logical. In developing sound recommendations, the internal auditor ensures that the recommended action is within the scope of the client, address the cause and not just the symptoms, and is at least intuitively viable.

Audit Findings should be grouped together depending on the severity of risk. High risk areas would be those where absence of immediate corrective action may have a major negative impact on achievement of objectives. Medium risks may be those areas where failure to take action could result in significant consequences. Low risk areas are those where suggested action would bring in greater efficiency or enhanced controls at minimal additional costs.

6.3   ISSUE OF REPORT TO STAKEHOLDERS

The audit reports should be issued to all the stakeholders who are required to take action on the report and who are included in the distribution list approved by the Audit Committee. This would necessarily include the head of the organization of the audit unit and head of the concerned administrative division.

6.4   QUALITY IN INTERNAL AUDIT REPORTING

Internal Audit Reports should be issued in the format prescribed by the O/o Controller General of Accounts. To ensure that these reports are effective, they should be complete, concise, accurate and objective and should be issued in a timely manner. The reports should be based on facts and free from any personal criticism. The audit findings should be worded constructively and the recommendations should focus on achievement of objectives.

 Other details which should be kept in mind include:

- The reports should have proper spelling, grammar and punctuation.

- Fonts and formatting should be proper and consistent.

- Report addressee name and title should be proper and spelt correctly.

- Report number and subject title should be included correctly on the report.

7.1   FOLLOW-UP ACTIONS

The true achievement of an audit engagement is reflected in implementation of the recommendations and an improved control system. The importance of this phase should therefore not be underestimated. The detailed manual should bring out a procedure for developing and monitoring of significant internal audit observations and issues raised. Clearly defined systems should be laid out.

System of monitoring and resolution of audit issues needs to be established: There should be a defined time-frame for submission of Action Taken Reports on the audit observations made by the Internal Audit Wing of the Ministry. These ATRs should be examined and IAWs should offer its comments/ recommendations to the administrative division of the Ministry for taking it up further. The monitoring of Audit paras should also aim to resolve old audit paras and the progress in their settlement should be closely watched by the Pr. CCA/CCA/CA.

7.2   REVIEW OF PENDING AUDIT ISSUES IN AUDIT COMMITTEE MEETINGS

Issues which could not be resolved within a period of six months through communication with the administrative division/ audit client should be reported to the Audit Committee. Chairman of the Audit Committee would issue further directions on the issue.

WORKBOOK

1. What are the five main phases of internal audit process?

   _____

   _____

   _____

2. If the primary focus of internal auditing engagement is advisory, then the audit process may be amended in consultation with _____ .

3. What should a commencement letter include?

   _____

   _____

   _____

4. List any four matters an auditor must be aware of while assessing the reliability of audit evidence.

   _____

   _____

   _____

5. What does current audit file typically include?

   _____

   _____

   _____

6. The appropriate level of testing and control evaluation depends on availability of which two factors?

   _____

   _____

   _____

7.   Audit findings need to be supported by?

_____

_____

_____

8.   Audit observations need to be included in which part of the report?

_____

_____

_____

9.   Audit planning comprises of two phases. Specify?

_____

_____

_____

10.   Annual audit plans need to be finalized by _____ .

11.   The annual audit programme outlines three items, namely

_____

_____

_____

12.   What is the audit universe?

_____

_____

_____

13.   Internal audit priorities are established on the basis of _____ and _____ .

Unit - 8

Conducting Internal Audit Engagement- Audit Tools and Techniques

Learning Outcomes:

♦ Knowledge & Skill requirements from Internal Auditors.

♦ Usage of Auditing tools and techniques.

♦ Types of Tools and Techniques.

⇒ Electronic Work papers

⇒ Data Extraction/ Data Analytics Tools

⇒ Automated Self Assessments Tools

⇒ Online Audit Management Software

⇒ Continuous Monitoring Tools/ Business Intelligence.

1.1 Knowledge and skill requirements from Internal Auditors

Internal Auditors are expected to be proficient in internal audit and perform their work with due professional care. Additionally, they must have sufficient knowledge to evaluate the risk of fraud and the way it is managed within the programs/schemes but are not expected to have expertise of person whose primary responsibility is detecting and investigating fraud. Also, they must have sufficient knowledge of key information technology risks and controls of the scheme/program. Further the auditor should have knowledge in using automated auditing techniques.

While performing the audit, the field internal auditor is concerned with planning, analyzing and managing evidence to support his/her audit conclusions. Hence an understanding on the different types and sources of evidence and then selecting the appropriate source is the starting point. This is followed by proficiency in the use of tools and techniques required for the audit. Also as information is mainly available through the auditee team, hence developing a healthy working relationship between the auditee and auditor would usually result in an effective audit. Hence personal skills are a necessary quality of the internal auditor.

1.2 Knowledge on the usage of Auditing Tools and Techniques

With the introduction of risk based internal audit approach in Ministries/Departments, increasing computerization and focus on digital technology, the thrust and the influx of Big Data in Government, it is essential that internal auditors understand the following areas and are able to use the tools and techniques that are provided to them, viz.

a. Evaluation of internal controls, identifying fraud indicators and auditing in an IT environment.

b. Risk based audit, risk assessment, design and development of risk matrix, mapping risks with controls.

c. Application of professional standards.

d. Sampling techniques.

e. Report writing techniques.

f. Usage of Computer assisted auditing techniques (CAATs).

To meet the above, internal auditors need to periodically do self-assessment on whether they are adequately skilled for the internal audit reviews/engagements that they are to perform and continuously update their knowledge skills and usage of tools and techniques, by either self-study or getting themselves enrolled for specialized training courses through NIRDPR.

2.1   TYPES OF TOOLS AND TECHNIQUES

Auditing Tools and Techniques are available for all the 4 stages in the audit cycle, viz. Planning, Performing, Communicating and Monitoring and can be classified into the below three types

- *Soft skill techniques* – these are soft skill techniques developed through training courses that help internal auditors interact effectively with auditee team

- *Frameworks* – these are methodologies which assist the internal auditor develop specific questionnaires, programs, checklists, audit programs, testing routines, audit reports, etc. for the specific review/engagement

- *Automated tools* –these are software applications that assist in auditing digital data and performing activities on IT.

2.2   Soft Skill Techniques

In all the 4-stages of the audit cycle, internal auditors are interacting with Auditee and these interactions can be classified as interviewing, negotiating and presentations. For example, a questionnaire is a document through which a written interview is conducted. Again, negotiating skills are helpful while an audit recommendation is under discussion with management. Also, an audit report is a written presentation. Over time specific techniques relevant to internal auditors have been developed on interviewing, negotiating and presentations for which courses are available at NIRDPR.

2.3   Frameworks

In the 1970s, there was a standard Internal Control Questionnaire (ICQ) issued by ICAI which was modified to fit the business for which the audit engagement was being carried out. This was an early framework to refer to. Since then libraries of frameworks and methodologies now exist and a google search on any aspect will usually give some results. One of the prominent global frameworks that executive management refers to is guidance issued by COSO (www.coso.org). These are on Governance and Operational Performance, Guidance on Internal Controls and Guidance on Enterprise Risk Management.

The Institute of Internal Auditors website (www.theiia.org) has detailed guidance on most aspects relating to internal audit. These are in the form of Advisories to the International Standards for the Professional Practices of Internal Auditing and other technical literature. For e.g. Guidance on various aspects of IT audit can be found in their Global Technology Audit Guide Series (GTAG)

Also, guidance on internal audit can be found on the websites of ICAI, ICSI, etc.

Using these frameworks, methodologies, guidance, advisories, etc. and the internal auditor's understanding of the program/ schemes, he/she draws up for that specific internal audit engagement, structured documentation as surveys, questionnaires, checklists, risk assessment, audit programs, testing procedures, audit report formats, etc.

2.4   Automated Tools

Since the last two decades, internal auditors are increasingly using automated tools such as electronic working papers, continuous monitoring, and continuous self-assessments. Also with ICT on a mobile phone platform and intelligent data analytics many of the internal audit departments have dramatically transformed the value proposition that they now offer to their entities. Some of the automated tools being used commonly are as

a)   Electronic work papers

These are automated work papers as linked excel sheets, with other applications as Word, PowerPoint, etc. One recent application is an automated structured audit report (ASAR). In one case field auditors release the audit report through their mobile phone within a few hours of completing the audit at a remote location using ASAR. Electronic Work papers however, have risks relating to security, privacy and their retention and the Head of Internal Audit needs to periodically review the controls.

b)   Data extraction/data analytics tools

Initially internal auditors who had auditee departments using large database were the early adapters of performing analysis using excel spreadsheets. Later, Generalized Audit software was developed by vendors as ACL, IDEA which made the data extraction and analysis easier for wide array of analytical and statistical functions and procedures, are Programmable, etc. They proved very effective and are widely used today

c)   Automated Self-Assessment Tools

One of the popular practices in surveys has been getting process teams to collectively discuss management and internal controls in that business process. These collective assessments are commonly anchored by the Internal Auditor who facilitates and oversees the whole activity. This activity is known as Control self-assessment (CSA) and to bring in objectivity originally excel was used and now certain products as Anonymous voting using keypad technology are also used which allow Instant display of results (summaries), for e.g. Option Finder® (Option Technologies Interactive). The self-assessment technique is now commonly used in different forms as Risk and Control Self-Assessment (RCSA), etc.

 (d)   Online Audit Management Software

Today the management of audit activities of the Internal Audit Wing (IAW) is online and MoRD has an online portal for this.

(e)   Continuous Monitoring Tools/ Business Intelligence

Continuous monitoring can be utilized through various applications. Almost all ERP vendor including SAP Standard Characteristics correlate various data elements and through rules create an audit file. For e.g. flag all cash payments above Rs.10,000. These rule-based file creations have become extremely sophisticated resulting in online monitoring and offering predictive insights. These are initial developments for the future application of Artificial Intelligence as Audit BOTs.

(f)   Concepts of Audit evidence and requisite quantities of audit evidence

The information collected, analyzed and evaluated by the auditor to support the audit observation. It is important for auditor to obtain sufficient, appropriate and reliable audit evidence to enable them to draw reasonable conclusions on the basis on which audit opinion formed.

CERTIFICATE COURSE ON INTERNAL AUDIT - Volume - I

WORKBOOK

1.   What are the three types of tools and techniques available for conducting the audit?

_____

_____

_____

2.   The three types of interactions between internal auditor and the auditee are:

_____

_____

_____

3.   Name the various automated tools used by internal auditors.

_____

_____

_____

4.   What are soft skill techniques?

_____

_____

_____

5.   What are the six essential areas every internal auditor should understand?

_____

_____

_____

6.   While performing the audit, the field internal auditor is concerned with _____ , _____

and _____ to support his/ her audit conclusions.

7.   What are the four stages of audit cycle?

_____

_____

_____

Unit - 9

Audit Documentation and Report Writing

Learning Outcomes:

♦　　Content and Structure of Internal Audit Report.

♦　　Report Issuance.

♦　　Report writing style considerations.

♦　　Executive Summary and its components.

♦　　Report Review Process.

♦　　Communicating Results.

♦　　Follow-up action.

1.1   INTRODUCTION

Internal audit reports provide a formal means of notifying senior management in the Ministry, the Audit Committee, and other stakeholders of audit observations, related risks, and areas for improvement. The internal audit function normally communicates engagement results via internal audit reports, which include the engagement's objectives, scope, conclusions, recommendations, and management's responses and action plans.

A well-written audit report provides senior management in the Ministry, the Audit Committee, and other stakeholders a better understanding of the audited activity's governance, risk management, and control processes. It also provides an opportunity to suggest how the potential impact of key risks can be maintained at an acceptable level and/or acknowledge the engagement client's satisfactory performance. In addition, a well-written audit report presents an opportunity to highlight the internal auditors' in-depth knowledge of the organization's business processes and provide recommendations for improvement.

It is essential that the work of the internal audit function is adequately documented to enable an auditor with no earlier connection to the audit to understand the audit procedures performed, the evidence obtained and the conclusions arrived at in the audit report. We provide below certain guidelines from the CGA's Draft Handbook on Internal Audit relating to Audit Documentation and report writing (***Communicating the Results of the Engagement***).

INTERNAL AUDIT GUIDELINE No. 30

1.2   DOCUMENTING ENGAGEMENT ACTIVITIES

Engagement activities should be documented in sufficient detail to enable an experienced auditor with no previous connection to the audit to understand from the audit documentation the nature, timing, extent and results of audit procedures performed, the audit evidence obtained and its source and the conclusions reached, including evidence that supports the auditors' significant judgements and conclusions.

Auditors need to document significant decisions affecting the audit objectives, scope and methodology; findings; conclusions and recommendations.

The Pr. CCA/CCA/CA in their capacity as CAE need to approve a documentation policy which covers the custody and retention of advisory engagement records, as well as their release to internal and external parties. These policies must be consistent with the Ministry's guidelines and any pertinent regulatory or other requirements. The policy must cover:-

- Need for Internal Audit Wings to document sufficient, reliable and relevant information to support their engagement results and conclusions.

- Need for controlled access to engagement records.

- Retention requirements for engagement records, regardless of the medium in which each record is stored. These retention requirements must be consistent with the organization's guidelines and any pertinent regulatory or other requirements.

INTERNAL AUDITGUIDELINE No. 31

1.3   COMMUNICATING THE RESULTS OF THE ENGAGEMENT

The Internal Auditors must communicate the results of the audit in a timely manner. Final communication by the internal auditor of the engagement results must contain opinion and/or conclusions. Where also an overall opinion is issued on an audit area or activity, it must take into account the expectations of the Ministry and must be supported by sufficient, reliable, relevant and useful information. The reason for an unfavorable overall opinion must be stated.

While communicating the results of the audit, the following matters should be taken care of, viz.

- Where certain audit observations are of a nature that delaying the reporting may impact the achievement of program/scheme objectives, then the auditor should communicate to the concerned authority their findings at an early date and even during the course of audit.

- The Audit Reports structure should include the engagement's objectives and scope as well as applicable conclusions, recommendations and action plans. In case there is a scope limitation, this should be brought out in the reports.

- Internal auditors are encouraged to acknowledge satisfactory performance and best practices being followed by the auditee.

- To ensure quality of the Audit reports, they must be clear, accurate and concise and issued in a timely manner. The Internal Audit Wing should bring objectivity in the observations and their recommendations should be constructive and complete.

- All reports should be issued by the Pr. CCA/CCA/CA in their capacity as CAE as he/she retains the overall responsibility even if some duties have been delegated to others. Where there is an error or omission in the report, the CAE must circulate corrected information to all the recipients of the earlier communication.

- In case there is full conformance of CGA Internal Audit Guidelines during the audit engagement, this should be mentioned in the report.

- Overall opinions could be ratings, conclusions or other descriptions of results. Such an opinion may be in relation to controls around a specific process, risk or business Acceptance of unit.

2.1   REPORT CONTENT AND STRUCTURE

The style and format of written internal audit reports varies across Ministries. The internal audit report structure could be consistent with the Ministry's reporting format. According to the IIA Standard 2420 – Quality of Communications, "Communications must be accurate, objective, clear, concise, constructive, complete, and timely." The content and level of detail should be determined by the needs of the stakeholders. The following questions about the reader(s) should be considered:

- Who are the most important readers of the report?

- How much do they know about the audited activity?

- How do they plan to use the report?

- How do the identified issues impact the reader?

The structure of a report often includes the following components:

i.   Audit report title.

ii.   Objective (purpose of engagement).

iii.   Scope (audited activities, nature and extent of work, scope limitations).

iv.   Background (brief synopsis of the activity being audited or an explanation of the process).

v.   Recognition (positive aspects of area or activity audited or appreciation of cooperation).

vi.   Engagement rating (ranking, outcome [i.e., red, yellow, green]).

vii.   Conclusions (summary opinion/assessment of the engagement, often highlighting critical observations).

viii.   Observations - each observation should be listed in order of significance (grouped by activity if applicable) and often include:

    a.   A title and reference.

    b.   Criticality rating (measure of risk significance [i.e., high, medium, low,]).

    c.   Statement of facts (condition, criteria, cause, effect/risk), which can be supported with relevant examples, data, analytics, tables, or charts.

    d.   Audit recommendations (corrective action to mitigate the risk identified in the observation).

    e.   Management's action plans (corrective action, activity owner, and target date for completion).

ix.   Distribution list.

2.2   REPORT ISSUANCE

Engagement results should be communicated according to the agreed communication timelines for submission. This allows management to take appropriate corrective action.

2.3 REPORT WRITING STYLE CONSIDERATIONS

When drafting the internal audit report, readers' needs should be considered. The results should be presented in an organized way, such as placing observations in chronological order, by significance, or grouping by topic, cause, or effect/ risk. Language used should be simple and relatively free of technical jargon and sentences should be short and to the point. Charts, graphs, diagrams, tables, illustrations and other graphics help to highlight key messages. The tone of the report should be constructive.

3. THE EXECUTIVE SUMMARY

The executive summary should provide a clear and concise overview of the engagement results delivering well supported, relevant information to stake holders. The summary should not contain technical jargon and internal audit methodologies, which can be in the detailed report .The executive summary generally contains significant observations or key messages from the

internal audit report and may include concerns encountered with senior officials of Ministry relating to implementing corrective actions. It helps to include a table that lists the number of observations/recommendations per audited activity, according to their importance. The key observations can be summarized in a positive manner (focus toward enhancement) or a negative manner (focus toward weaknesses). Internal audit is encouraged to acknowledge satisfactory performance when applicable and to show the trend (positive or negative) compared to prior audits of the same activity.

The executive summary may include repeat observations from a previous audit. Additionally, information on action plans from previous audits that have not been completed, or have implementation dates that have expired, may also be included. In such cases, it is beneficial to include historical information on the repeat observations and management's action plans. The executive summary should also highlight good practices observed during the audit and any significant steps taken by management in improving the governance, risk management, and internal controls of the programme or schemes of the Ministry.

The key components of an executive summary generally include:

• Introduction, objectives, scope, and engagement results.

• Conclusions for the audited activity/processes.

• A summary of significant observations or key messages.

• Concerns relating to establishing corrective actions, deadlines, and/or situations where the CAE concludes that management has accepted a level of risk that may be unacceptable to the organization.

4. INTRODUCTION AND SCOPE OF THE INTERNAL AUDIT ENGAGEMENT

The introduction provides basic information about the entity activities, or process audited. The Scope may indicate the period covered, the type of internal audit being conducted (i.e., compliance, assurance, performance or follow-up audit), specific risks, relevant systems, and/or the departments or functions assessed.

5. INTERNAL AUDIT ENGAGEMENT CONCLUSIONS

As specified in the Guideline No.31 above "Final communication of engagement results must include applicable conclusions, as well as applicable recommendations and/or action plans. Where appropriate, the internal auditors' opinion should be provided. An opinion must be taken into account the expectations of senior management, the board, and other stakeholders and must be supported by sufficient, reliable, relevant, and useful information." Internal auditors 'conclusion of the condition of the audited activity/process helps the reader understand the significance of the observations. The financial impact caused by the internal control weaknesses and irregularities also can be used to convey the significance of the observations.

6. OBJECTIVES AND SCOPE

The objectives and scope in the internal audit report should be consistent with the approved engagement plan. This section typically describes the audit purpose, risks, scope, and scope limitation, if any.

7. OBSERVATIONS

Observations (also referred to as findings), recommendations, and management's action plans (responses) make up the core of the written internal audit report. The starting point used to develop the observation is knowledge of the "criteria" and its variance from the "condition" observed. The goal is to develop a condition-based and a root cause-based recommendation/management action plan.

An easy way to remember the components of observations is the 5 Cs, i.e.

- Condition

- Criteria

- Cause

- Consequence and

- Corrective action and recommendations

These are described below:

- **Criteria:** Standards, measures, or expectations used in making an evaluation and/or Verification of an observation (what should exist). Criteria are used to compare and evaluate the existing condition(s) and can be written policies, procedures, laws, regulations, and/or guidelines. Choosing the appropriate criteria enables the internal auditor to reach suitable conclusions and consequently provide meaningful assurance to senior management and the board. Examples of appropriate criteria may include:

  o Internal (e.g., Ministry's policies and procedures).

  o External (e.g., laws and regulatory requirements).

  o Leading practices (e.g., Ministry best practices, professional guidelines, key performance measures).

- **Condition:** Factual evidence identified by the auditor during the course of the engagement (what exists). Condition is the key issue the internal auditor considers, and it can be measurable or observable.

- **Cause:** Underlying reason for the difference between the criteria and condition (why does the difference exist?). It answers the questions "what allows the condition to exist?" and "why did the condition occur?" It is essential that internal audit work with management to identify the root cause of the gap. Merely fixing the issue does not address what caused the issue to exist and does not improve the overall governance, risk, and control environment. Finding and appropriately addressing the root cause will reduce (and optimally eliminate) the future recurrence of the condition.

- **Consequence:** Impact, Risk or exposure encountered because the condition is not consistent with the criteria (the consequence of the difference). It can be an effective communication tool for delivering the significance of each observation and could assist management with prioritizing their action plans, and internal auditors with prioritizing follow-up.

- In determining the degree of risk or exposure, internal auditors consider the effect that the observation may have on the organization's operations and/or financial reporting process.

- Effects can be existing or potential.

    o   Existing (real) effects are factual and seen as a result of the condition.

    o   Potential effects are exposures where no real effect has yet occurred or been found.

- In addition to the internal auditors' observations and recommendations, the identified risks should be documented in the audit report, along with the impact, to provide clarity of the issue to the stakeholders.

- Consideration of the individual observation ratings within the report generally impacts the overall engagement conclusion (as mentioned above in the section entitled "Internal Audit Engagement Conclusions"). When ratings are used, rating criteria should be clearly defined and consistently applied across all internal audit reports for assurance engagements.

- **Corrective Action and Recommendations**

- Recommendations are internal auditors' suggestions for correcting conditions, and identifying the cause to prevent recurrence (or the creation of new conditions). Recommendations provide an efficient and effective way to address the gaps identified between condition and criteria. Recommendations are divided into two categories — a combination of condition and root cause based recommendations may be appropriate, depending upon the particular observation.

    o   Condition-based recommendations: Provide an interim solution for correcting the current condition (e.g., removing inappropriate access).

    o   Cause-based recommendations: Actions needed to prevent the condition/observation from occurring again. Root cause-based recommendations are typically longer-term solutions and may involve more time (e.g., creating and implementing an access review policy).

    o   Corrective Action Plans: Recommendations and/or action plans must be included in the final reports. Actions that were initiated by management during the internal audit engagement, but before the issuance of the written report, can also be acknowledged.

- Action plans arising from internal auditors' recommendations have the potential to transform Ministry processes and help meet its goals. Action plans are effective when designed and executed in a way that addresses the root cause. Validation of the action plan(s) with the Auditee is important to assure issues are effectively and efficiently addressed. Although internal auditors may be experts in governance, risk management, and internal controls, they cannot assume managerial responsibility for the action plans, or claim to understand the business better than the engagement client.

Observations should be written in such a way that the reader understands and accepts internal audit's assessment of the risk, as well as its impact on organizational objectives. Observations should be supported with evidence, brief and organized, and explain in simple language how the condition compares to a set of criteria. Recommendations, explained in the next section, should provide a practical, feasible solution to manage the risks identified in the observations, thereby eliciting a positive response from the engagement client.

A good practice is to create a preliminary draft report (also referred to as an audit memorandum, observation worksheet, or audit comment referral) as a tool for communicating with senior and line management to enhance the engagement process. It could include a draft of the condition, criteria, cause, effect, and recommendations. Such a report can assist in starting a constructive discussion for finding reasonable solutions (agreed actions), even at early stages of the internal audit engagement. If the conditions are critical, management maybe able to address the conditions before other areas of the organization are impacted. Working collaboratively with the internal auditors, management provides action plans based on internal audit's observations and recommendations, including:

o   **Agreed action:** The actions that will be taken by management to correct the current condition and causes, thereby preventing future reoccurrence. Generally, management's action plans correlate with internal audit's recommendations. If management disagrees with the observation or facts identified by internal audit, further details can be provided to reach agreement or a sound explanation should be provided by management for discussion and resolution.

o   **Responsible personnel:** Identifies the person or group responsible for the action. This may be the activity/process owner, manager, or senior management.

o   **Due date for action plan:** Target date for completing the action plan. The CAE should ensure the proposed timeline is appropriate based on the level of risk.

o   If the CAE encounters concerns with management when establishing corrective actions and deadlines and is unable to resolve the concerns after escalation to senior management, it is appropriate to discuss the concerns and resolution with the board. These concerns might pertain to the sufficiency of management's action plan, the deadline for action, or the classification or description of the observation.

8.   REPORT REVIEW PROCESS

As noted in Standard 2440 – Disseminating Results, the CAE is responsible for reviewing and approving the final engagement communication before issuance. This is an important step to assure work was performed properly and recommendations align with the organization's business objectives.

The CAE reviews and approves the final engagement communication before issuance and decides to whom and how it will be disseminated so results are given due consideration. Although the review process will vary depending on the size

of the internal audit activity, the CAE (or designee) should establish a review process for validating report observations .Depending on the size of the internal audit staff, the review process may include the following steps:

- Review engagement records to ensure:

  o   The work performed is consistent with the audit scope, engagement objectives and guidelines

  o   Observations and recommendations are clearly stated and supported by sufficient, reliable, relevant, and useful evidence.

- Draft the internal audit report with cooperation from the internal audit team.

- Validate the draft report and forward to the CAE (or designee) for review.

- The CAE (or designee) reviews the draft report and returns the report to the internal audit team if there are issues requiring clarification.

- The CAE (or designee) authorizes communication of observations to management for feedback before issuance of the final written internal audit report.

- Upon review and agreement with management's action plans and target completion dates, the CAE (or designee) authorizes issuance of the final written internal audit report.

- The CAE retains overall responsibility for the final engagement communication, even when delegating review responsibilities.

9.1   COMMUNICATING RESULTS

An integral and important part of the internal audit engagement is the presentation of the work performed and the derived results. Consequently, careful preparation is required as the final audit report shows the work of internal auditors to senior management in the Ministry, the Audit Committee, and other stakeholders, and can also be used as a reference for future assurance and/or advisory engagements. As noted in Guideline 31 "The Chief Audit Executive is responsible for communicating the final results to parties who can ensure the results are given due consideration."

9.2   PRESENTING REPORTS – TYPES OF COMMUNICATION

Organizations use many varying formats; but, general guidelines are applicable for most presentations and reports. Such presentations and/or reports should:

- Ensure the engagement's objectives, scope, and results are included.

- Be clear, concise, and easy to read and/or understand.

- Contain accurate and complete information that is presented objectively, constructively and timely.

- Ensure conclusions and engagement results are supported by sufficient, reliable, relevant, and useful information based on appropriate analyses and evaluations.

- Link the objective of the work performed with the organization's strategic objectives.

- Identify and analyze the root cause of the issues to support the recommendations and action plans that enhance the business (when applicable).

The means by which final internal audit engagement results and reports are distributed can also vary; however, they are generally presented with the use of hard copy or printouts.

9.3   FOLLOW-UP ACTIONS PLANNED BY INTERNAL AUDIT

According to Standard 2500 – Monitoring Progress, "The Chief Audit Executive must establish and maintain a system to monitor the disposition of results communicated to management." If agreed-upon action plans are not acted on by management, there is little value of the internal audit engagement's results to the organization. In accordance with Standard 2500.A1, the Chief Audit Executive must have a monitoring process in place to validate action plans are implemented effectively or confirm that senior management has accepted the risk of not taking action.

The follow-up on the action plan is performed by the internal audit activity. A best practice is to create a tracking spreadsheet or system, including the audit observation, action plan, responsible personnel, and target completion dates. As corrective actions are completed, the audit observation is closed; an ageing analysis is generated for all opened and pending observations; and communication takes place with management as needed. The tracking and aging analysis is also a good tool to share with senior management and the board.

Follow-up activities can be performed at specific time intervals, or on an ongoing basis. When performed at specific time intervals, the CAE may schedule specific assignments in the annual internal audit plan to perform a follow-up for incomplete or expired action plans from the previous year(s). When follow-up activities are performed on an ongoing basis, the follow-up process is usually performed monthly or quarterly and consists of three elements: collecting information; verifying the completion of the action plan; and reporting results to the engagement client, senior management, and periodically to the board (under certain circumstances, reporting to regulators may be required as well).

- **Collecting information:** Internal auditors charged with the follow-up process must collect information from management regarding the status of action plans (i.e., those action plans that are completed, those that are in process, and those that are not yet implemented — partially or in total — and those that are overdue).

- **Verifying completion of action plans:** For action plans reported by management as implemented, internal auditors should verify that the observations and associated risks originally raised are appropriately mitigated. Verification may be performed for all completed action plans or on a selective basis, depending on the risk significance.

- In cases where management determines certain action plans are no longer necessary, the CAE must discuss the matter with senior management. The CAE must communicate to the board if the matter is not resolved (refer to Standard 2600 – Communicating the Acceptance of Risks).

- There are several tools in the market that facilitate the follow-up process, allowing internal audit to utilize workflow from risk assessment, to report delivery, to action plan follow-up. As an example, workflow could allow the sending of automatic emails when an action plan is nearing its target completion date. Internal auditors should not lose focus that the main objective of the follow-up process is to validate that the agreed-upon actions have been implemented and are working effectively.

... Ideally Action Plans must be S.M.A.R.T. i.e. Smart, Measurable, Achievable, Relevant and Time Bound.

Model Audit Report

Internal Audit Report of

Finance and Accounts of Uttarakhand, Rural Road Development Authority (UKRRDA)

PIU 01 & 02, Almora (UK)For the period from 2016-17 to 2018-19

सत्यमेव जयते

Internal Audit Wing

O/o the Chief Controller of Accounts,

Ministry of Rural Development

Rajendra Bhawan, Deen Dayal Upadhyay Marg, New Delhi

O/o the Chief Controller of Accounts

Ministry of Rural Development

Internal Audit Wing

Rajendra Bhawan, New Delhi

CERTIFICATE COURSE ON INTERNAL AUDIT - Volume - I

Internal Audit (Risk Based) Report on Finance and Accounts of ...., **Rural Road Development Authority, PIU-01 & 02, Almora.**

Name of Audit Party Team:

1. Sh. XYZ, Audit Consultant

2. Sh. XYZ, Audit Consultant

Auditee Office:

Duration of Audit: 24 02.2020 to 29.02.2020

Period of Audit: 2016-17 to 2018-19

Audit Domain: PMGSY Programme Fund, Administrative Expenditure Fund on random sample system

Incumbency

Name of the General Manager	Period	Name of the Accountant/ Cashier	E-mail ID	Mobile	Address
		Shri XYZ			
MR. XYZ	01.04.2016	Cashier			
	to	From 01.04.2016			
	31.12.2016	to Till date			
	31.12.2016				
	to				
	30.06.2018				
	04.08.2018				
	to				
	06.05.2019				
	07.05.2019				
	till-date				
Shr XYZ GM, PIU-02 **w.e.f.** **04.12.2017**		Shri XYZ (Account Clerk)			

The construction of roads under PMGSY has been carried out by four PIUs under Superintending Engineer, ... E-mail

PIU-1 is Executive Engineer, Irrigation Department of state Govt., ... and has the charge of ADB Division. PIU-II is Executive Engineer PWD of state Govt. ... and has the charge of other Division of State Govt.

Introduction

Pradhan Mantri Gram Sadak Yojana (PMGSY) was launched by Govt. of India in December 2000 with 100% central funding with the objective of providing all weather road connectivity in rural areas. However the funding pattern changed to 60:40 ratio sharing between the Centre and the State from 2015. This Program aims to provide a single all weather road connectivity to eligible unconnected habitations. These unconnected habitations should be on the core network (a network of routes to provide basic economic and social goods and services to habitations). The eligibility of these unconnected habitations is the populations size (Census 2001) 500 plus population in plain areas, 250 plus in Special category states, Desert areas, Schedule V areas and 88 selected tribal and backward districts and 100 to 249 in critical LWE affected blocks identified by the MHA. PMGSY-II, basically looks at the consolidation of rural road network through the up-gradation of "major link routes" and "through routes" based on District Rural Roads plans.

Organizational Setup

The PIU xyz 01 & 02 are the state Govt. Department Irrigation department and PWD and working under SRRDA …District. Receiving funds from Ministry of Rural Development, Government of India and for executing the Scheme PMGSY under the control of LSGD Department.

PROGRAMME IMPLEMENTATION UNIT (PIU)

The Programme Implementation Units (PIU) are the basic units for project planning, execution and accounting. A PIU may consist of one or more Engineering Divisions, appropriately headed by an Executive Engineer or Superintending Engineer. The PIU would be directly responsible for contracting implementation and Quality Management of PMGSY works. The PIU would also be the financial and accounting centre at the field level.

Audit Objective

Planning for program was as per the procedure prescribed in Operations Manual for preparation of District Rural Road Plan and Core Network for providing all weather road connectivity to unconnected habitations.

♦ Adequate funds were provided and utilized for effective implementation of program.

♦ Tendering and contract management, of the state in respect of program implementation ensuring canons of financial propriety and transparency.

♦ Construction of roads was taken up and completed within timeline specified in PMGSY guidelines and according to specifications of Indian Road Congress (IRC) without involving any cost overrun.

♦ Road maintenance contracts were implemented effectively and State Government took institutional measure to build capacity and devolve fund and functionaries to District Panchayat for sustainable maintenance of roads and

♦ The envisaged three tier quality control mechanism and monitoring system were effective

Scope of Audit:

a.   To track the flow of funds from the ministry to, PIU…….. -01&02) concerned.

b.   Checking of Bank authorization/expenditure & other related register and records maintained by SRRDA and PIU.

c.   Checking of the records such as Cash Book, Bank Statement, contract Ledger, Dr & CR Ledger, Security register.

d.   Checking of Contractor bills, MB, variation statement and other records related to work.

e.   To bring out recommendation for improving risk Management.

f.   To evaluate compliance with the provisions of various rules and regulations in incurring expenditure.

Audit Methodology:

a.   The Audit was conducted on the basis of objectives, provisions of the scheme, flow of funds; specific rules and laws governing the execution of programme.

b.   An entry conference was held with General Manager, SRRDA …..–PIU-01 & 02 at ……on the first day of Audit.

c.   On the basis of irregularities Paras have been raised.

d.   Site inspection of Project & Works of PMGSY.

e.   Internal Audit was conducted by scrutinizing the selected final bills of works and vouchers of Administrative Fund.

f.   Audit methodology involved examination of records of SRRDA Programme Implementation Unit

g.   Exit conference was held with Executive Engineer,PIU-01 and 02 on the last day of Audit.

Executive Summary

Para No.	Description of Para	Risk
1	Abnormal delay in final payment to contractors, irregularities regarding	High
2	Non recovery of Penalties amount of Rs.1,36,285 on account of liquidated damages from M/S K.B.M. Consultants.	High
3	Delay in preparation of PIU-Wise Annual Audited account for the year 2018-19	Moderate
4	Abnormal delay in construction of Road under Package No. UT-01-19 (PIU-02)	High
5	Non adjustment of advances to contractors for preparation of DPR including investigation /survey, etc.	High
6	Excess expenditure booked against cost of approved works without approval of competent authority.	High
7	Excess expenditure amounting to Rs. 8,49,700/- incurred under administration fund	High
8	Non Adjustment of Temporary Imprest with staff amounting to Rs. 1,19,826/- under Administration fund in PIU-II	High
9	Preparation of unrealistic Detailed Project Reports estimates	High
10	Non repayment of security Deposits to the contractors.	Moderate

Audit observation:

a.   Title of reference

b.   Rating

c.   Statements of facts

    i.   Criteria

    ii.   Condition

    iii.   Cause

    iv.   Consequence-Impact

    v.   Corrective Action-Recommendation

    vi.   Management's Action

Model Para

Para No.___: Excess expenditure amounting to Rs.8,49,700/- incurred under Administration fund.

High Risk Criteria: As per para No. 12.2 of PMGSY Programme Guidelines for implementing the scheme at District Level, all staff costs will be borne by the state Govt. However, the Administrative and Travel Expenses of PIUs and SRRDA costs will be met from PMGSY administrative fund to the following extent of the annual allocation of Programme fund.

a)   Admn. Expenses for PIUs   1% of Annual Allocation

b)   Travel Expenses of PIUs   0.50% of Annual allocation

c)   Admn. and Travel Expenses   0.25% (Rs. 75 lakh of annual of SRRD allocation max.)

d)   Independent Quality Monitoring   0.50% 2nd Tier

Conditions: A review of the cash book /Annual Audited Accounts of PIU-I for the year from 2016-17 & 2018-19 has revealed that PIU-I has incurred expenditure under Administration expenses and travel expenses in excess of the Administrative fund admissible to PIU-I as detailed below:

(Amount in Rs.)

Year	Programme fund allocated	Fund admissible under travel expenses	Expenditure incurred under travel expenses	Excess Expenditure
2016-17	15,78,23,461	7,89,112	9,15,131	1,6,019
2018-19	28,76,30616	14,38,153	21,61,834	7,23,681
Total		**22,27,265**	**30,76,965**	**8,49,700**

Consequences: If the fund is not monitored regularly, misappropriation of fund is possible.

Cause: Non –observance of scheme guidelines by the implementing agency

Recommendations: Executive Engineer PIU-I is advised to take up matter with the UKRRDA and amount incurred in excess of admissibility should be approved from the competent authority. In future, it may please be ensured that the PMGSY Guidelines are followed strictly and no excess expenditure is booked under Admin Fund. Compliance of the above may be furnished to O/o CCA, IAW, MoRD, New Delhi

WORKBOOK

1. What are the criteria for communication of assignment results?

  _____

  _____

  _____

2. Name the seven parameters that determine the quality of communication.

  _____

  _____

  _____

3. Name the 5Cs and their alternate statements

  _____

  _____

  _____

4. What are the three types of criteria?

  _____

  _____

  _____

5. Name the three types of recommendations

  _____

  _____

  _____

6. Expand S.M.A.R.T

  _____

  _____

  _____

Unit - 10

Certificate Programme on Internal Audit of
Rural Development Programmes

Case studies and exercises - Report writing – No.1

Attached is a report on audit in an office of a Central Government institution. The trainees may form themselves into 5-6 groups with 4-5 members each.

Each group is required to study the report carefully, and applying the knowledge gained from course on audit report writing, discuss the report and arrive at a list of review comments bringing out the weaknesses/flaws in the report if any, and suggestions on improving the report to conform better to the Standards. You have 30 minutes to complete this exercise.

Thereafter, one trainee from each group would present their findings. Time allotted for presentation is 5 minutes for each group.

Contents

REPORT ON INTERNAL AUDIT OF

1.	Name and Designation of the Head of the Department:	XXX, Chairman XXX, Chairman XXX, Chairman	01 Apr 06 to 18 Jan 07 19 Jan 07 to 06 Mar 07 08 Mar 07 to till date	**New Delhi for the period from 01 Apr 2006 to 31 Mar 2010**
2.	Name and Designation of Head of Office:	XXX, Pr. Registrar XXX, Pr. Registrar XXX, Pr.	01 Apr 06 to 05 Jun 06 01 Aug 06 to 29 Feb 08 03 Mar 08 to till date	
3.	Name and Designation of DDO	XXX, Account Officer	01 Apr 2006 to till date	
4.	Postal Address and Telephone No.			
5.	Name and Designation of			
6.	Period of accounts audited:			
7.	Month selected for detailed audit:	01 Apr 2006 to 31 Mar 2010		
8.	Date of Audit:	19 Jul 2010 to 28 Jul 2010 (08 Working days)		
9.	No. of Vehicles held by the Deptt	13 Vehicles (11 Four vehicle & 02 Three Wheelers) Nil		
10.	Any loss to Govt. property due to fire, theft, negligence or			

Introductory

The XXX was established in November 1985 by Parliament by an Act Bo. 13 of 1985 to deal with all cases relating to service matters which were previously dealt with by courts up to and including the High Court. There are now`11 17 regular Benches of the XXX functioning in various parts of the country, including its XXX at Delhi.

The XXX is a non-cheque drawing DDO submitting bills to the Pay and Accounts Office (XXX), New Delhi. The budget allotment and actual expenditure for the year 2006-07, 2007-08, 2008-09 & 2009-10 are given below.

Year	Allotment (")	Expenditure (")
2006-07	4,53,94,000	4,50,65,000
2007-08	5,18,38,000	5,15,31,000
2008-09	10,80,72,000	10,77,55,000
2009-10	11,56,37,000	11,56,01,000

The sanctioned strength and actual position as on 2006-07, 2007-08, 2008-09 & 2009- 10 are given below.

	GOs		NGOs	
Year	Sanctioned	Actual	Sanctioned	Actual
2006-07	38	32	186	167
2007-08	38	34	186	167
2008-09	38	34	186	172
2009-10	39	36	186	177

This office was subjected to Statutory Audit, which was conducted by the AGCR New Delhi for the period 2006 - 2009. They have raised paras, and are outstanding till date.

This report covers the Internal Audit of the accounts of XXX, New Delhi for the period 2006 – 2010, which was conducted by an Internal Audit party comprising XXX, Accountant of the office of the Controller of Accounts, Ministry of XXX, New Delhi. The Audit was conducted over 08 working days from 19 to 28 July, 2010. This is the 16th Audit of XXX by the Internal Audit Wing.

The objective of this internal audit was to inspect the financial and accounting records maintained in the XXX, with a view to ascertain how far the rules and regulations, systems and procedures in accounting and financial matters have been followed by them. This report contains the major observations of the Audit team based on the facts and figures gathered during the course of the audit on a sample test basis within the limited available time. This work is not primarily directed towards the detection of fraud or other irregularities and should not, therefore, be taken to assure that no other weaknesses exist. Accordingly, the comments refer only to those matters, which have come to our attention during the course of our audit work and do not attempt to indicate all possible improvements. These findings have been discussed with Pr. Registrar XXX.

Review of Previous Reports

All the paras of the previous Internal Audit Report have either been dropped or taken afresh with latest facts and figures after verification of compliance except Para No 2, 9 (c), 10 (a) & 12 which have been taken in the current report.

Audit Findings

The following schedule set out details of the issues raised from the audit. The issues are color coded according to their priority ratings to enable major weaknesses to be easily identifiable. The key to the color ratings is listed below the table.

S. No.	Audit Findings	Rating	Issue raised in Prior Reports
1.	Deficient Procurement System		
2.	Irregularity in Procurement for Official Residence		
3.	Irregular use of Condemned Staff Car		
4.	Excess Consumption of petrol		
5.	Discrepancy in Pay Fixation		
6.	Non-adjustment of Advances		
7.	Improper maintenance of Log Book		
8.	Discrepancy in rounding off of amount of increment		
9.	Delayed Deposit of Govt. Money into Bank		
10.	Non-maintenance of register of grants and non watching of utilization certificates		
11.	Non-maintenance of Broadsheet of GPF (Group D)		
12.	Non-maintenance of Service Book in Duplicate		

Ratings

A major weakness that must be addressed soon.

An important matter that will significantly improve the control environment.

A minor weakness that should nevertheless be addressed to improve the control environment.

Para No. 1

Finding   **Deficient Procurement System**

Condition During the test check of procurement related files of, XXX, it was noticed that the procedure prescribed for procurement in the GFR is not being followed. For instance, the following procedural deficiencies were observed in a few cases:

1. There is no specific order for nomination of Local Purchase Committee. As per GFR, a Local Purchase Committee is to be constituted for making purchase of items costing more than Rs. 15,000.

2. Vendors are contacted directly for obtaining quotations. No reference enquiry has been given in the quotation. Quotations are received by hand instead of sealed envelope.

3. There is no mention of VAT/CST No, no seal of firm was found affixed on quotation.

4. Technical specifications were not prescribed in notice inviting quotations. Vendors seem to have quoted rates without proper specifications of items to be supplied.

5. Comparative statements are not signed/authenticated.

Effect   Rule 137 of GFR provides that every authority delegated with the financial powers of procuring goods in public interest shall have the responsibility and accountability to bring efficiency, economy, and transparency in matters relating to public procurement and for fair and equitable treatment of supplies and promotion of competition in public procurement.

Absence of specific order for nomination of Local Purchase Committee, receiving of quotation by hand instead of in sealed envelopes and other similar irregularities are detrimental to the objectives enumerated in Rule 137 of GFR.

Criteria   Chapter 6 of GFR 2005 provides guidelines for procurement of Goods and Services. These guidelines may be followed in total.

Recommendation Provisions of GFR regarding procurement of goods and services may be strictly followed. A Local Purchase Committee may be formed. Quotations be received in sealed envelopes and these quotation should contains a reference number of enquiry floated by department. All quotations should have a seal of firm and bear VAT/ CST No.

Rating

Para No 2

Finding   **Irregularity in Procurement for Official Residence**

Condition   A perusal of file No. 12(2)/Shahjahan Road/AE-2N/09-10 showed that an amount of Rs.1,49,686/- was spent on providing wooden tiles flooring at the official residence of Chairman XXX. In this regard, following observations are made:

1. Provision of flooring does not appear in the list of approved items contained in the XXX order dated 11.08.99.

2. The maintenance of official residence is carried out through CPWD. In this case, the CPWD is on record refusing to carry out the work on the grounds that they had already completed the upgradation work, including provision of Inviza tile flooring.

3. The expenditure of Rs.1,49,686/-, which was incurred through a private contractor, was not included by XXX in the overall ceiling of Rs.4,00,000/-.

4. The procedure adopted for carrying out the work does not appear to be fully transparent. Three quotations were obtained, apparently by hand, without giving much publicity. There were no enquiry references on the quotations.

Effect   Procurement of wooden tile flooring through private contractor resulted in double expenditure, which could have been avoided if the matter was taken up with CPWD in time. Further, non- inclusion of this item in the overall ceiling could result in expenditure in excess of the norms.

Criteria: The High Court Judges Rules, which lay down the entitlements in this case, provide for incurring expenditure up to the limit of Rupees 4 lakh towards free furnishing of the official residence of Chairman

XXX. XXX order no. 16/27/95-GA(Pt) dated 11.08.99 lays down the items to be provided for this purpose. GFR 137, 149, 151, 160, 161 detail the procurement procedure applicable to this case.

Recommendation: The extant case requires regularization. XXX need to setup a mechanism to ensure that expenditure is incurred only on approved items and within the permissible limits. XXX may also consider reviewing their order dated 11.08.99.

Rating   ████████

Para 3

Finding   **Irregular use of Condemned Staff Cars**

Condition: XXX, XXX, was accorded approval by the DoPT to purchase new cars in replacement of old cars, which were to be condemned and disposed off. The XXX purchased new car without getting the condemned car disposed off through auction. DoPT vide letter No. G-14012/10/2009-A7, dated 30.7.2009 conveyed approval for condemnation of vehicles DL-2CM-2868, DL-2CM-2869, DL- 2CM-7287. The XXX purchased new cars without disposing off the condemned vehicles, which are still in use. Expenditure on these vehicles during 2009-10 is as under:

Vehicle No.	POL Expenditure	Repair Expenditure
DL-2CH-7287	1,33,180	7,333
DL-2CM-2868	1,76,097	25,169
DL-2CM-2869	59,519	28,632
	3,68,796	**61,134**

Thus, an amount of Rs. 4,29,930/- has been expended on above mentioned three vehicles despite condemnation.

Effect: New car was purchased without getting the condemned car disposed off through auction. It was in contravention of guidelines laid down by DoPT and against fiscal procedure. Condemned vehicles are being used. These vehicles are not proving economical as they require frequent repairs and replacement of parts and consume more fuel.

Criteria: GFR and orders issued by Ministry of Finance provides that a new vehicle in replacement of an old and condemned vehicle can be purchased only after the disposal of condemned vehicle through auction. Rule 197 of GFR 2005 and orders of Ministry of Finance on the subject provide guidelines for mode of disposal.

Recommendation: The condemned vehicles may be auctioned at the earliest and in future it may be ensured that replacement vehicles purchased only after condemnation and disposal of old vehicles. The irregularity in the instant case may be got condoned from Ministry of Finance.

Rating

Para No 4

Finding	**Excess Consumption of petrol**

Condition   A test check of the fuel consumption on official vehicles revealed that the limits prescribed by the M/o Finance for monthly consumption of Petrol were not being adhered to. Excess consumption of petrol was noticed in the case of 04 vehicles during 2004-05, 02 vehicles during 2005-06 and 02 vehicles 2009-10 (Annex A).

Effect   Excess consumption of petrol shows lack of control of utilization of official vehicles. The expenditure on fuel will increase disproportionately if the limit of 200 Litre monthly is not observed and it would be in violation of order of Ministry of Finance issued on the subject.

Criteria   Min of Finance OM No.F-3(a) E-11(A) 95 dated 06.09.1995 provides that every official vehicle will be entitled to 200 litre of fuel per month or actual consumption of petrol whichever is less.

Recommendation   A column should be opened in the Log Book of every vehicle to record and monitor consumption of petrol. A responsible officer may be detailed by Head of Office / Department to watch and signed in bill / register to ascertain proper utilization of Petrol.

Rating

Para No.5

Finding	**Discrepancy in pay fixation**
Condition	Internal Audit conducted a test check of pay fixation done by the XXX, XXX on implementation of the 6th Pay Commission recommendations. In all 52 cases of pay fixation were checked. Out of these discrepancies in the form of higher pay fixation were noticed in 04 cases (Annex B). Wrong fixation of pay indicates lack of familiarity with the applicable rules/provisions. The test check results show discrepancies in about 8% of the sample tested, which is significant if the entire strength of 213 is to be considered.
Effect	Excess pay was given to official as compared to their actual entitlement. Although, the amounts involved are not significant at this stage, they will increase progressively, if not corrected in time.
Criteria	Pay fixation is to be done in accordance with central revised Pay Rules 2008 and as per Ministry of Finance / Department of Personnel, Public Grievances & Pension orders published day to day.
Recommendation	All pay fixations must be done in accordance with the applicable rules and got verified by the PAO before allowing the benefit to the employees. Recoveries may be effected in the cases pointed out.
Rating	

Para No. 6

Finding	Non-adjustment of advances
Condition	The XXX (XXX) had given advances to the tune of Rs. 3.77 crores in 2004 to NICSI for purchase of laptops, etc. These advances are still lying unadjusted. This was pointed out by the previous Internal Audit Party but even after a lapse of 4 years, these advances are still lying outstanding.
Effect	The long outstanding advances show the lack of control over utilization of Government money. Government money is lying with a private party and is causing loss of interest to Government.
Criteria	The Government advances should be adjusted as early as possible without undue delay. As per Rule 164(2) of the Receipt and Payment Rules, it is the duty of the departmental authorities to monitor the recovery and settlement of the advances given for the departmental expenditure. In terms of Rule 9 of GFR, it is the duty of the department of Central Government concerned to ensure that receipts and dues of Government are correctly and promptly assessed and credited to consolidated fund.
Recommendation	Grant of Advances for purchase of Computers, printers and laptops, etc., should be avoided. If under extreme necessity, the grants of advances become inevitable, every effort should be made for early settlement of advances. In any case, all advances for meeting departmental expenditure must get settled before the close of the financial year.
Ratings	

Para No. 7

Finding	Improper maintenance of Log Book

Condition   XXX, XXX has 13 vehicles - 11 Four wheelers and 02 Three wheelers. A test check of the Log Books of   Government vehicles revealed that the Log Books are not being maintained in the proper form. For instance, kilometer readings have not been found mentioned while filling petrol account in respect of Vehicle No. DL 2CQ-3441 (COROLLA).

Effect   The non-indication of kilometer reading while filling petrol account, result in lack of control over consumption of petrol and   is against orders of Ministry of Finance.

Criteria   Staff Car rules provide for maintenance of petrol account in proper form prescribed under Rule 31 of Staff Car. Officers   using Staff cars should note in the log book in their hand writing the mileage at the start and at the completion of their trips after verifying   the milometer. The entry regarding drawl of petrol is also to be attested.

Recommendation   Guidelines provided in Staff Car Rules for maintenance of Petrol.

Account should be followed in to and entry should be attested.

Rating

Para No. 8

Finding   Discrepancy in rounding off of amount of increment

Condition   A test check of the increments granted by XXX, XXX showed that the amount of increment in respect of some officials was wrongly rounded off to the higher side resulting in higher fixation of pay to these officials (Annex C).

Effect   Excess amount of increment was allowed which resulted in excess increase in pay, DA, HRA also, this increase will have recurring effect in future increases of pay.

Criteria   As per CCS (Revised Pay) Rules, 2008, the amount below `1 is to be ignored while rounding off the amount of increment to the next multiple of ten.

Recommendation   The pay fixation and amount of increment should be got verified from PAO before allowing benefit to the employees. Recoveries may be affected and correct procedure may be followed in rounding off the amount of increment.

Rating

Para No. 8

Finding   Discrepancy in rounding off of amount of increment

Para No. 9

Finding	**Delayed Deposit of Government Money into Bank**
Condition	The Government receipts collected by XXX, XXX are not deposited in the Government Account in a timely manner. The test check revealed 11 instances of delays ranging from 3-18 days (Annex D).
Effect	Delayed remittance of Government receipts means that this money is lying idle in the cash chest and Govt. is losing interest on this money. Also money lying with cashier for undue long period may be lost or misused.
Criteria	Rule 8 of Receipt & Payment Rules provide for bringing Government money into account without undue delay.
Recommendation	It may be ensured that Government money is deposited into the accredited bank without undue delay. A periodical checking should be carried out by DOO / Head of Office.
Rating	▮▮▮▮▮

Para No. 10

Finding	Non-maintenance of register of grants and non-watching of submission of UC
Condition	As per rule 212 (4) of General Financial Rule 2005, a register of grants is to be maintained by the sanctioning authority in form GFR 39. It has been observed that XXX, XXX is not maintaining such register in respect of Grants given to Bar Councils of Benches of CTA situated in different states. In the absence of this register, it is very difficult to watch the release of periodic grants to various Bar Councils as well as receipt of utilization certificates from them. Moreover, utilization certificate are not being obtained in proper form i.e. GFR 19-A. A review of file of grants showed that UCs in respect of grants released during 2008-09 to Bar Councils of Lucknow, Jaipur and Allahabad benches are still pending.
Effect	The non-maintenance of register of grants is a lapse on the part of Pr Bench XXX. This register helps in watching to whom the grant was released and when. It also helps in watching whether utilization certificate against the grant has been received. It helps in preventing release of grants to those Bar Councils of XXX who have not furnished UC in respect of previous grants.
Criteria	Rule 212 of GFR provides for maintenance of a Register of Grants and timely submission of Utilization Certificates by the grantee bodies/institutions.
Recommendation	DDO should ensure that a register of grants is invariably maintained as per proforma prescribed in GFR and all the grants are noted in it under proper attestation before releasing the payment.
Rating	██████████

Para No. 11

Finding   Non-maintenance of Broadsheet of GPF (Group D)

Condition   The broadsheet of GPF (Group D) is not being maintained. Responsibility for maintenance of
                       Provident Fund Accounts of Group 'D' employees devolves   on   Head   of   Offices.   On
                       receipt of schedules and vouchers, of GPF from the accounts section the dealing assistant
                       posts the figures in the ledger folio "Form CAM 47". A Broadsheet in form CAM 48 is also
                       maintained. In order to verify the posting made in the Ledger with the monthly account, the
                       figure entered in the ledger   Folio   should   be   posted   in the Broadsheet against the
                       respective account number and final totals struck. The individual closing balances in the
                       Broadsheet should also be verified with those shown in the ledger folio before they are
                       carried over to the next year's ledger folio.

Effect   The correctness of posting in GPF ledger cannot be verified in the absence of monthly
                       closing of Broadsheet and tallying the figure of Broadsheet with monthly account.

Criteria   Para 6.8 of Civil Account Manual provides for maintenance of Broadsheet in Form CAM 48.

Recommendation   The Head of Office should arrange to start instruct the dealing assistant to start preparing
                       Broadsheet of GPF.

Rating   ██████████

Para No. 11

Finding   Non-maintenance of Broadsheet of GPF (Group D)

Para No. 12

Finding	Non-maintenance of Service Book in Duplicate Condition . Duplicate copies are not being supplied to officials
Effect	The right of Government servant to ascertain that all the entries have been correctly recorded in his service book is affected. Moreover it is a safeguard against hardship due to loss of service book in office under unfortunate circumstances.
Criteria	The provision of Rule 257 of GFR provides that every Government Servant shall be given a duplicate service book.
Recommendation	All the officials may be provided duplicate copy of service book or alternatively service book may be complied in electronic form and may be kept in safe custody. Periodic updates may be made every year.

Rating:

Annexure A

Excess Consumption of Petrol

(Refer Para No. 4)

(i)   Statement of Excess Consumption of petrol during 2004-05, in Litre

Vehicle No.	Period April, 04 to June, 04	July 2004 to Sept. 2004	Oct, 2004 to Dec 2004	Jan, 2005 to March 2005	Petrol drawn in excess of the prescribed ceiling of 600 ltr. Petrol per quarter.
DL-2CA 4354	740	960	815	850	965
DL 2CH 4355	-	-	880	610	290
DL 2CH 7287	680	695	695	820	490
DL 2CH4356	-	-	620	685	105
					1850*

Cost of excess consumption of 1850 litre of petrol, taking an average rate of petrol @ Rs 38 per litre 1850 X 38 = Rs. 70,300

(ii)   Statement of Excess Consumption of petrol during 2005-06 in Litre

Vehicle No.	Period April, 2005 to June, 2005	July 2005 to Sept. 2005	Oct, 2005 to Dec 2005	Jan, 2006 to March 2006	Petrol drawn in excess of the prescribed ceiling of 600 ltr. Petrol per quarter.
DL-2CH 4355	610	740	-	-	150
DL 2CM 6684	680	650	-	-	130
					280*

Cost of excess consumption of 280 litre of petrol taking an average rate of petrol @ Rs.40 per litre *280 X 40 = Rs. 11,200/-

(iii)   Statement of Excess Consumption of petrol during 2009-10 in Litre

Vehicle No.	Period April, 2009 to March, 2010	Petrol drawn in excess of the prescribed ceiling of 600 ltr. petrol per quarter.
DL 2CH 7287	2815	415
DL 2CM 2868	3812	1412
		1827*

Cost of excess consumption of 1827 litre of petrol taking an average rate of petrol @ Rs. 47/- per litre is Rs. 85,869.

Discrepancy in Pay fixation

(Refer Para No. 5)

<u>**DISCREPANCIES IN PAY FIXATIONS**</u>

i)   Sh. XXX, SCD was drawing Basic pay of Rs. 4875 as on 1.1.2006 in the pre-revised scale of 4500-125-7000. As such his pay as on 1.1.2006 in the revised scale should have been fixed at Rs. 9070 + Rs. 2800 but the office has fixed the pay at Rs. 9270 + 2800. The pay fixation may please be revised and over paid amount be recovered.

ii)   Sh. XXX, Dy. Registrar XXX was promoted as Jt. Registrar w. e. f. 29.2.2008. While fixing his pay as on 1.7.2008, he was allowed notional increment on Grade pay of Rs. 7600/- instead of Rs.6600/-. As such his pay as on 1.7.2008 was wrongly fixed at Rs. 34180/- instead of Rs. 34150/-. The pay fixation may be revised and over paid amount be recovered.

iii)   Sh. XXX LDC was granted 1st   MA.C.P. w. e. f. 1.9.2008. He was granted 2nd MACP, w .e .f. 5.6.2009 which is irregular as the official has not completed 20 years of service. Moreover, Sh. XXX is working as adhoc LDC. His pay was stepped up from 9200 to 9350 w. e. f. 3.9.2008, with reference to Sh. Anil Kumar Adhoc LDC. The stepping up is irregular as both Sh. Raje Singh LDC and Sh. Anil Kumar LDC are adhoc.

iv)   Smt. XXX, Steno Grade D was promoted steno Gr 'C' w. e. f. 30.4.2009, She opted to get her pay re-fixed w. e. f. 1.7.2009. The pay as on 1.7.2009 works out to Rs. 14750/- (Rs. 10550+4200= Rs.14750) but the office has fixed it at Rs. 14810/- (Rs.10610+ Rs.4200). The pay fixation may be corrected and over paid amount may please be recovered.

Discrepancy in rounding off of amount of increment to the multiple of ten

(Refer Para No. 8)

S.No.	Name of official & designation	Month of increment	Rounded off to Rs.	Amount of increment as it should be (Rs.)
1		July 2008	720	710
2		July 2007	300	290
3		July 2007	370	360
4		July 2008	850	840
5		July 2006	550	540

Delayed deposit of Govt. money into Bank (Refer Para No 9)

S. No.	Amount (Rs.)	Date of Receipt	Date of Deposit in the Bank	Days
1.	609	16.10.2008	5.11.2008	16 Days
2.	254	20.10.2008	5.11.2008	18 Days
3.	292	21.10.2008	5.11.2008	15 Days
4.	369	22.10.2008	5.11.2008	18 Days
5.	340	23.10.2008	5.11.2008	13 Days
6.	19173	24.10.2008	5.11.2008	12 Days
7.	2570	1.12.2008	17.12.2008	16 Days
8.	3500	4.12.2008	17.12.2008	13 Days
9.	178600	18.04.2009	21.4.2009	03 Days
10.	3500	08.05.2009	13.5.2009	05 Days
11.	31126	15.5.2009	19.5.2009	04 Days

Certificate Programme on Internal Audit of Rural Development Programmes

Case studies and exercises - Report writing – No.2

Attached is excerpts from the planning memorandum prepared in connection with the proposed audit of a project being implemented by an autonomous organization.

The trainees may form themselves into 5-6 groups with 4-5 members each and complete the following tasks.

1. Carry out a brief risk assessment of the office. Assess the most significant risks and assess them as High, Medium and Low (for simplicity you can take a combined view of likelihood an impact)

2. Prepare a brief ToR for the audit (bullet points would do)

3. Imagine that you have done the field work. Write a para each on two most significant issues identified.

Time allowed: 30 minutes

Thereafter, one trainee from each group would present their findings. Time allotted for presentation is 5 minutes for each group.

CASE STUDY - 2

Background

Indian Agricultural Institute (IAI) is an Agricultural Research Institute working on enhancing farm productivity for the small holder farmers in collaboration with international as well as national partners. IAI gets its funding from the Government of India and other international partners and bilateral and multilateral institutions. It has an annual budget of over Rs.250 crores and has done successful work in the field of agricultural research thereby improving the livelihood of about 10 crores small holder farmers.

Among the research projects being implemented by IAI, The Internal Audit Department (IAD) has selected a project funded by the Norwegian government through the Ministry of Agriculture under the Norway-India Strategic Research Fund (NISRF). The project runs for 3 years, from 1.1.2017 to 31.12.2019 and carries a grant of Rs.5 crores and is implemented by the project office in Rajasthan.

The objective of the project is "*to enhance and improve livelihoods of Indian small holder farmers of Rajasthan by doubling their household income in 3 years through increased productivity achieved by means of improved farming practices*".

The project has just completed one year of operations.

A preliminary survey carried out in preparation for the audit revealed the following information (as on 1-8-2018), among others:

1. There is a quarterly (first of January, April, July and October) reporting to be done to the donor as well as to the Ministry of Agriculture. This reporting is both financial and technical. According to the latest financial report submitted, following is the summarized position:

Project		31-12-2017		31-03-2018	
	31-12-2019	**Budget**	**Actuals**	**Budget**	**Actuals**
Personnel	2,50,00,000	80,00,000	50,00,000	80,22,500	65,00,000
Partners	1,00,00,000	30,00,000	28,00,000	35,00,000	33,00,000
Supplies & Services	75,00,000	20,00,000	24,00,000	30,00,000	32,00,000
Equipment	25,00,000	10,00,000	8,00,000	15,00,000	9,00,000
Admin & Operations	50,00,000	15,00,000	12,00,000	18,00,000	24,00,000
Total	**5,00,00,000**	**1,55,00,000**	**1,22,00,000**	**1,78,22,500**	**1,63,00,000**

	Entire Project	30-06-2018		30-09-2018		31-12-2018	
		Budget	Actuals	Budget	Actuals	Budget	Actuals
Personnel	2,50,00,000	80,45,000		80,67,500		1,70,00,000	
Partners	1,00,00,000	42,00,000		50,00,000		60,00,000	
Supplies & Services	75,00,000	40,00,000		45,00,000		50,00,000	
Equipment	25,00,000	20,00,000		25,00,000		30,00,000	
Admin & Operations	50,00,000	23,00,000		30,00,000		33,00,00	
Total	5,00,00,000	2,05, 45,000		2,30,67,500		3,43, 00,000	

2. The staff position is as follows:

a) Head of Office - 1

b) Technical Staff - 10

c) Admin & Operations staff

Admin Officer – 1 Cashier – 1

Secretary – 1

Office Asst. -1

Driver -2

Office helper - 1

Total – 18

3. The Head of Office is a senior technical staff and is primarily responsible for the successful implementation of the project in the project location. He also has responsibility for the overall oversight of the project office. The technical staff and Admin. Officer report to him. He is mostly on travel to various farm locations in the state where the project is being implemented.

4. The Admin staff report to the Admin Officer who is responsible for the day- to-day operations of the office.

5. The cashier handles cash which is handled on an imprest basis with a limit of Rs.1,00,000. The daily cash disbursements are of the order of Rs.10000-15,000 a day. The limit for petty cash disbursement is Rs.5,000 above which payments have to be made by cheque. The average balance in the bank is about Rs.5 lakhs. Bank accounts are reconciled monthly and statements sent to Headquarters.

6. Latest bank reconciliation statement available is as on 31/5/2018 according to which position is as follows:

7. The project office maintains a current account with a bank which is jointly operated by the Head of Office and Admin Officer.

8. Procurement is handled by the Office Asst. The average procurement value is about Rs.2.0-2.5 lakh per month.

9. Transaction processing is done by the cashier who posts the entries in the accounting system. He also has the responsibility of carrying out bank reconciliation.

Balance in the bank as on 31/5/2018   6,79,200

Add:

Cheques deposited, not credited

Deposited on 31/11/2017   2,45,000

Deposited on 1/2/2018   1,27,000   3,72,000

                                                  10,51,200

Less:

Cheques issued, not presented

Issued on 20/9/2017   45,000

Issued on 29/5/2018   1,345

Issued on 29/5/2018   14,000

Issued on 29/5/2018   24,000   84,345

Balance as per books as on 31/5/2018   11,35,545

You are required to form yourselves into 4 groups and do the following tasks:

4. Carry out a brief risk assessment of the office. Assess the most significant risks and assess them as High, Medium or Low (for simplicity you can take a combined view of likelihood and impact)

5. Prepare a brief ToR for the audit (bullet points would do)

6. Imagine that you have done the field work. Write a para each on two most significant issues identified.

Unit - 11

Post Audit Review Mechanism and Interaction with Audited Agencies

Learning Outcomes:

♦ Audit Planning design matrix

♦ Audit design matrix.

♦ Minutes of entry meeting

♦ Collection appropriate audit evidence.

♦ Major audit findings

♦ Departmental Appreciation Note

1.1 Post Audit Review Mechanism

The Aspect of Scrutiny of inspection reports by senior level authority at Head Quarters/Ministry is known as Post Audit Review Mechanism.

Total auditable units under the audit jurisdiction is known as Audit Universe and these units are to be updated with latest data relating to the units which enable for proper selection.

- Units are divided into 3 groups

- Apex units (policy makers)

- Auditable units (monitoring mechanism)

- Implementing units (who implement the programme)

1.2 Audit intended to communicate its finding to three types of people

- Firstly to Auditable Units (Monitoring Mechanism) through Inspection Reports (IRS) containing audit findings relating to implementing units.

- Secondly to apex units (policy makers) communicating important common findings noticed in implementing units. This is done through departmental appreciation note (DAN)

- Thirdly to stake holders (members of parliament or state legislatures) through audit report containing audit findings through audit paras in audit report.

1.3 Planning

Planning is done at two levels - macro level and micro level.

- Taking into consideration of man power available, macro level Annual Audit plan (AAP) is prepared and this is reviewed by expert committee and this will be guiding factor for conducting audits in that year.

- For conducting individual audit micro plan is prepared duly providing mandays and the period of audit.

- Audit planning is done by way of audit design matrix duly indicating audit objective, sub- objective, scope, criteria, documents to be seen, Questions to be asked, Evidence to be collected.

- This document is a guiding factor for audit team to conduct audit.

- Person who prepares this document depends upon the audit department needs and availability of Resource persons.

1.4   Execution

- Audit team selected for conduct of audit is issued with audit engagement letter addressed to the auditee unit.

- Audit team is headed by a team leader.

- Team leader meets Head of the Audit unit and conducts Entry meeting with him and minutes the same.

- Team leader then issues audit requisitions relating to production of records, information on theft, embezzlement, misappropriation and replies to old Audit paras .

- Audit team scrutinizes records, put questions and obtain answers as per audit design matrix.

- Collects evidence and forms audit conclusions.

- Communicates audit findings to auditee unit and obtain replies from them.

- He now prepares **Audit finding matrix** giving details audit conclusions and findings with reference to **audit design matrix**

- He then convert his findings into appropriate paras, duly incorporating replies and prepares a draft inspection report.

- This draft inspection report is discussed with head of the audit unit on the last working day and conducts Exit conference. He obtains signature of the head of the auditee unit as token of seeing it.

2.1   The inspection report has to be prepared in 5 parts –

a)   Introduction,

b)   Audit findings (major as well as other findings),

c)   Position of outstanding audit findings in respect of previous inspection reports,

d)   Success stories,

e)   Acknowledgement.

2.2   Team leader who conducts audit and prepares draft inspection report is not authorized to approve and issue it to Management.

- A senior level authority gets it scrutinized and approves the same.

- The aspect of scrutiny by senior level authority is called Post Audit Review Mechanism.

- This review is also done while preparing departmental appreciation note.

2.3   Team leader is expected to furnish statistical data relating to audit that was done duly giving details of

- Audit personnel,

- Dates of audit,

- Period of audit,

- Allocation of work among audit staff,

- Code of ethics,

- Title sheet in Annexure-II ,

- Information sheet in form IAM-8,

- Details of sanctioned files in respect of Grant-in-aid checked,

- List on Pay fixations verified,

- Certificate regarding losses due to Fire, Theft, Fraud, Embezzlement, etc.;

- He is also expected to furnish Audit design matrix, audit finding matrix, minutes of entry meeting and exit meeting.

2.4   The Inspection reports received from Audit party should be examined/vetted to see that:

- All the documents as listed above have been duly received and the report is complete in all respects.

- There are no blanks and omission of any data what so ever.

- Adequate reasons have been recorded for each objection settled.

- There are no anomalies, ambiguities or misconstruction of sentences.

- The objections are based on facts and not merely on presumptions and apprehensions and relevant rules or orders infringed have been reported.

- Inspection report has been discussed with the Head of the office in the exit conference and his signature obtained and this is checked with audit engagement letter

- All the files relating to previous inspection reports have been received back.

- Collection of appropriate audit evidence (documents in support of facts and figures contained in audit findings). In post review these documents are verified to ensure that findings are not heresy and supported by authorized evidence.

- The report is drafted in polite language and all points of financial significance are correctly brought out

- The tone and tenor in the audit para is carefully scrutinized under post audit review mechanism and it is ensured that language used is polite, clear and beyond ambiguity.

- It is also verified that findings are crisp and easy to understand and does not take much time to the reader.

- In post review, it is ensured that replies to the preliminary audit findings (audit enquiries/audit memos/audit observations/half margins) have been received and they are incorporated in the paras with proper rebuttal.

- This rebuttal should be supported by documents and should specify why the finding is to be retained with reference to reply furnished.

3.1   The audit findings in the Inspection reports are of two categories.

- Major audit findings which are likely to be converted as departmental appreciation notes

- Other audit findings.

3.2   Settlement of minor paras.

- Records not maintained- cash book, stock registers, log books based on reply may be settled on verification of records by the next Audit.

- Settlement of paras having financial implications /recoveries are to be settled after recoveries made and verified by the next Audit team only.

3.3   After scrutiny and vetting the draft report should be submitted to CCA for approval

- The report should be forwarded to Head of the Office inspected and a copy endorsed to next higher authority inviting his attention on major audit findings

- A copy of Inspection Report is also endorsed to PAO concerned

- The IR shall be issued within one month from the date of receipt and it should be entered/filled in the control register under attestation of the AAO

- The paras of the IRs shall be watched through objection book

- Since inspection reports are on working of implementing units and they are issued to auditable units, replies to these findings (both major findings and other findings) are obtained from auditable units.

- This enables them to process departmental appreciation notes.

- The departmental appreciation notes are prepared by the authority who approves the inspection report and put up for approval of the higher authority than the authority who approves the inspection report.

- The departmental appreciation notes are issued to ministries and replies to be obtained and processed to its logical conclusion.

3.4 Significant issues/important paras would be circulated to all other audit teams with the approval of Vice-Chairman of Audit Committee.

- Summary of Major Objections based on the basis of work done by the Internal Audit parties during the financial year would be brought out in the annual audit review for the Ministry/Department and would be submitted to the Chairperson of Audit Committee

- The Annual Audit Review should also be submitted to the office of Controller General of Accounts (CG A) in the prescribed format by 31st May

3.5 The programme division would be required to take follow up action on Audit report and significant non-compliance would be brought to the notice of Audit Committee for adequate action

- To peruse and settle the objections including test audit notes of Statutory Auditors a register will be maintained in the form (Annexure-II) to set apart separate folios for each DDO to keep watch the progress of settlement of paras.

- The progress made in settlement of objections will be reviewed monthly and appropriate further action taken to ensure their speedy settlement.

- Performance of Internal Audit would also be periodically reviewed by Pr. CCA/CCA/CA and results of this assessment will be shared by Chief Audit Executive with Audit Committee.

- In respect of other audit findings which are not included in the audit reports, are pursed through Inspection reports and replies are obtained from auditee units and upon obtaining satisfactory acceptable reply, the finding gets dropped by the authority who approved it.

WORKBOOK

1.   What is meant by Post Audit Mechanism and who do it?

2.   What are the types of people that audit findings are communicated and what are they?

3.   What are the elements found in audit planning design matrix?

4.   Inspection reports are prepared in how many parts and name them?

5.   What are the major points to be seen/vetted from the inspection reports received at headquarters a part review?

6.   What are the details of data relating to the audit that was done by Audit Team is supposed to furnish along the report?

7.   What are the elements found in Audit Design Matrix?

Unit - 12

Basic Concepts of Accounting & Book Keeping

Learning Outcomes

1. Meaning & Scope of Accounting

2. Objectives of Accounting

3. Functions of Accounting

4. Advantages of Accounting

5. Limitations of Accounting

6. Double Entry System

7. Mode of Accounting

8. Accounting Process

   • Journal

   • Ledger

   • Cash Book

   • Trial Balance

   • Profit and Loss A/c

   • Balance Sheet

9. Receipts and Payments & Income and Expenditure

10. Bank Reconciliation statement

1. Meaning and Scope of Accounting:

Definitions of Accounting

According to the "American Institute of Certified Public Account(AICPA)" Accounting is the art of recording , classifying , summarizing the data in a significant manner and in terms of money, transaction, and events which are, in part at least of a financial character and interpreting the results thereof."

The widely accepted definition of accounting, given by the American Accounting Association in 1966 which treated accounting as:

"The process of identifying, measuring and communicating economic information to permit informed judgment and decisions by the users of accounts."

In 1970, the Accounting Principles Board (APB) of American Institute of Certified Public Accountants (AICPA) enumerated the functions of accounting as follows:

"The function of accounting is to provide quantitative information, primarily of financial nature, about economic entities, that is needed to be useful in making economic decisions."

Thus, accounting may be defined as the process of recording, classifying, summarizing, analyzing and interpreting the financial transactions and communicating the result thereof to the persons interested in such information.

Components of Basic Accounting:

1.   Recording:

This is the basic function of accounting. All business transactions of a financial character, as evidenced by some documents such as sales bill, passbook, and salary slips etc are recorded in the books of account. Recording is done in a book called journal and this book may further be divided into several subsidiary books according to the nature and size of the business.

2.   Classifying:

Classification is concerned with the systematic analysis of the recorded data, with a view to group transactions or entries of one nature at one place so has to put information in compact and usable form. The book containing classified information is called ledger. This book contains on different pages, individual accounts heads under which, all financial transactions of similar nature are collected. For example, there may be separate account heads for salaries, rent, printing and stationery etc. All expenses under these heads, after being recorded in the journal, will be classified under separate heads in the ledger. This will help in finding out the total expenditure incurred under each of the above heads.

3.   Summarizing:

It is concerned with the preparation and presentation of the classified data in a manner useful to the internal as well as the external uses of financial statements. This process leads to the preparation of the financial statements like trial balance, profit and loss account, balance sheet, cash flow statement.

4.   Analyzing:

The term analysis means methodical classification of the data given in the financial statements. The figure given in the financial statements will not help anyone unless they are in a simplified form. For example all items relating to the fixed assets are put at one place while all items related to the current assets are put at another place. It is concerned with the establishment of relationship between the items of the profit and loss account and the balance sheet i.e., it provides the basis for interpretation.

5.   Interpreting:

This is the final function of accounting. It is concerned with explaining the meaning and significance of the relationship as established by the analysis of accounting data. The recorded financial data is analyzed and interpreted in a manner that will enable the end users to make a meaningful judgment about the financial condition and profitability of the business operations. The financial statements should explain not only what had happened but also why it happened and what is likely to happen under specified conditions.

6.   Communicating:

It is concerned with the transmission of summarized, analyzed and interpreted information to the end users to enable them to make rational decisions. This is done through preparation and distribution of accounting reports, which include besides the usual profit and loss account and balance sheet, additional information in the form of accounting ratios, graphs, diagrams, fund flow statements, etc.

2.   Objectives of Accounting:

1.   Systematic Record of Transactions

   •   E.g.: Book Keeping:-Journal, Ledger, Trial Balance

2.   Ascertainment of Results

   •   E.g.: Manufacturing, Trading and Profit& Loss A/c

3.   Ascertainment of Financial Position

   •   E.g.: Balance Sheet

4.   Communicating information to various Users

   •   E.g.: Financial Reports

3.   Functions of Accounting:

1.   **Maintaining systematic records:** Business transactions are properly recorded, classified under appropriate accounts and summarized into financial statements– income statement and the balance sheet.

2.   **Communicating the financial results:** Accounting is used to communicate financial information in respect of net profits (or loss), assets, liabilities etc., to the interested parties.

3.   **Meeting legal needs:** The provisions of various laws such as Companies Act, Income Tax and Sales Tax Acts require the submission of various statements, i.e., annual account, income tax returns, returns for sales tax purposes and so on.

4.   **Protecting business assets:** Accounting maintains proper records of various assets and thus enables the management to exercise proper control over them with the help of following information regarding them:

   (a)   How much is balance of cash in hand and cash at bank?

   (b)   What is the position of the inventories?

   (c)   How much money is owed by the customers?

   (d)   How much money is owing to the creditors?

   (e)   What is the position of various fixed

5.   Accounting assists **the management in the task of** planning, control and coordination of business activities.

6.   **Fixing responsibility:** Accounting helps in the computation of the profits of different departments of an enterprise. This would help in **fixing the responsibility of departmental heads**.

4.   Advantages of Accounting :

1.   **Assistance to management:** The accounting information helps the management to plan its future activities by preparing budgets in respect of sales, production, expenses, cash, etc. Accounting helps in coordination of various activities in different departments by providing financial details of each department. The managerial control is achieved by analyzing in money terms the departures from the planned activities and by taking corrective measures to improve the situation in future.

2.   **Records rather than memory:** It is not possible at all to do any, business by just remembering the business transactions which have grown in size and complexity. Transactions, therefore, must be recorded early in the books of accounts so that necessary information about them is available in time and free from bias.

3.   **Intra-period comparisons:** Accounting information when recorded properly can be used to compare the results of one year with those of previous year(s).

4.   **Aid in legal matters:** Systematically recorded accounting information can be produced as evidence in a court of law.

5.   **Help in taxation matters:** Income Tax and Sales Tax authorities could be convinced about the taxable income or actual turnover (**sales**), as the case may be with the help of written records.

6.   **Sale of a business:** In case, a sole trader or a partnership firm or even a company wants to sell its business, the accounting information can be utilized to determine proper purchase price.

5.   Limitations of Accounting:

Financial Accounting is not absolutely exact

Financial accounting is not completely free from personal bias or judgment. Though transactions are recorded on actual basis, but there are many instances where estimates have to be made for calculating profits. Such estimates requires judgmental factor. For example provision for doubtful debt, depreciation of asset, etc.

Financial Accounting does not show what the business is worth

The assets are recorded in the balance sheet at cost less than depreciation because they meant for use not for sale. Hence the balance sheet should not to be taken to disclose the realized value of assets on sale.

Financial Accounting does not present the whole picture.

Financial Accounting information does not include the qualitative aspects of business such as good labor relation, quality of the goods, management efficiency, etc.

Accounting is considered only with those activities which can be expressed in monetary term.

Window Dressing in Balance Sheet

When accounts apply window dressing in balance sheet, the balance sheet can't exhibit the true and fair view of the state of affairs of the business.

*<u>**Worthless assets are also shown in Financial Statements.**</u>*

Certain Worthless assets are shown in balance sheet just to distort the factual position e.g. preliminary expenses, discount on issue of shares and debenture, underwriting commission, etc.

*<u>**No effects of inflationary trends.**</u> As money is not a stable unit of measurement of inflation makes most of figures out of date.*

Different Types of Accounts
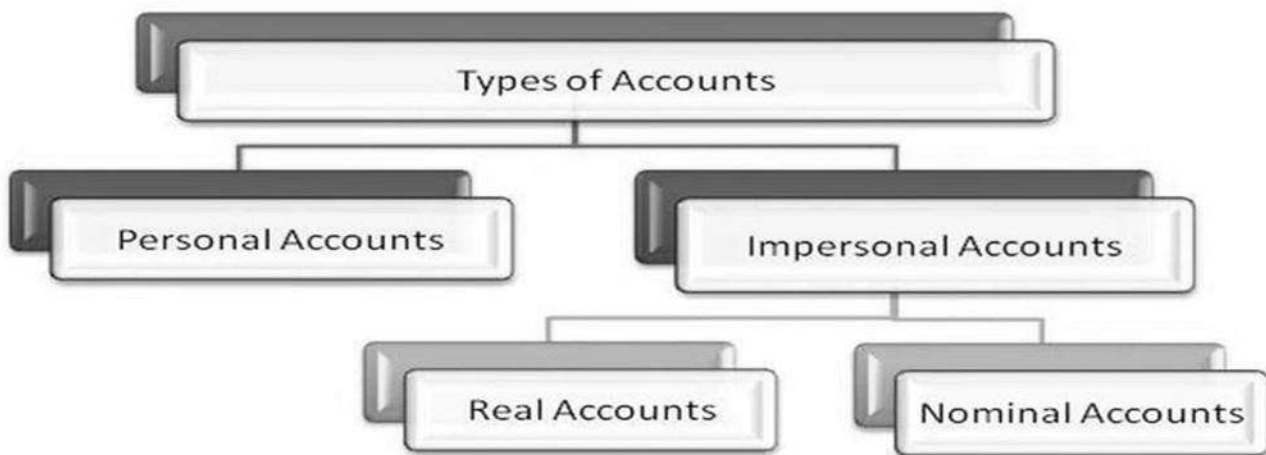
Personal Account:

As the name says, personal accounts are accounts of persons. They, therefore, bear the names of persons. Such persons can be credit customers or credit suppliers. Therefore, personal accounts are kept in either:

• *<u>**Sales ledger,**</u>*

or

• *<u>**Purchases ledger**</u>*

Note that in accounting, persons refer not only to individuals but also to companies, partnerships or any form of organization with whom there may be transactions.

Personal Accounts, in practices may be of following types:

• Natural Personal Account

• Artificial or Legal Persons Accounts

• Representative or Groups Personal Accounts.

Natural Personal Account

Such as the accounts of proprietor, supplier or receiver of goods or money, etc., in the name of natural persons such as Albert Account, James Account, etc.

Artificial or Legal Persons Accounts

Such as the accounts of legal entities in the nature of

limited companies accounts,

(Example : Hindustan Lever Limited , ITC Limited.)

Such as the accounts of legal entities in the nature of

Partnership Firms Accounts

(Example: Radhey Ram Nath Bros.)

Such as the accounts of legal entities in the nature of **Government agencies**

(Example: Sports Authority of India)

Such as the accounts of legal entities in the nature of **Institutional accounts**

(Example: Delhi Collage of Arts and Commerce);

Such as the accounts of legal entities in the nature of **Clubs Accounts**

(Example: Lions club)

Representative or Groups Personal Accounts

The group or representative personal accounts are the accounts of different persons of the same nature but more than one in numbers.

In the account books, the accounts are opened in the names of individual persons. But since they are of same nature, they are grouped into one account.

Example: *Sundry Debtors Account and Sundry Creditors Account.*

Impersonal Accounts

Accounts which are not personal such as Machinery Account, Cash Account, Rent Account, etc.

As seen in the previous slide, impersonal accounts are of two types:

1.   Real accounts

2.   Nominal accounts

All impersonal accounts are kept in the **General ledger**.

Real Accounts

Real account stands for the resources or properties of a business enterprise, which can be intangible and tangible.

Tangible accounts refer to properties having physical existence, like cash, building, stock of goods, furniture, etc.

Intangible refer to those which cannot be physically felt or touched but are capable of monetary measurement such as *Goodwill patent rights, trademarks, copyrights, etc.*

Nominal accounts

Nominal accounts relates to expenses, revenues, capital and drawing. Examples of accounts are:

- ⇒ Loan account
- ⇒ Sales account
- ⇒ Commission received account,
- ⇒ Salaries account,
- ⇒ Rent account,
- ⇒ Capital account,
- ⇒ Drawings account
- ⇒ Purchases Return Account
- ⇒ Sales Return Account

BASIC ACCOUNTING TERMS

ENTITY:

Entity means a thing that has a definite individual existence. When an accounting system is devised for a business entity, it is called an accounting entity. For example Big Bazaar, Bhargav Paints Pvt. Ltd., etc.

TRANSACTION:

An event involving some monetary value between two or more entities, and is capable of changing the financial position of the enterprise. We can also say that transaction is an activity of a financial nature having documentary evidence, capable of being presented in numerical, monetary term causing effect on assets, liabilities, capital, revenue and expenses. It can be in both forms cash or credit.

Transaction can be purchase of goods, collection of money, payment to creditors for goods and services, etc.

Assets

Assets are economic resources of an enterprise that can be useful expressed in monetary terms. They are those resources that the business owns. These are the items of value used for the operations of the business enterprise and also includes the Assets = Capital + Liabilities due to it from others. Some of the examples of assets are money owing by debtors, stock of goods, cash, furniture, machines, building, etc.

Assets = Capital + Liabilities

Assets can be broadly classified into two types :

- ⇒ Fixed Assets
- ⇒ Current Assets

FIXED ASSETS:

Fixed assets are those assets which are purchased for the purpose of operating the business and not for resale i.e., held by the business enterprise for long term purpose. Examples of fixed assets are building, machinery, furniture, etc.

CURRENT ASSETS:

Current assets are those which are held on the short term basis with the intention of converting them into cash during the normal business operations of the company. Examples of current assets are -unsold stock, debtors, bills receivables bank balance, cash in hand, etc.

Liquid Assets:

Liquid Assets liquid assets are those which yield cash in a very short period of time current assets excluding inventory and prepaid expenses are included in liquid assets.

Liquid Assets = Current assets - Prepaid expenses - Inventory

Intangible Assets

Intangible assets are those which can't be seen and touched but we can feel them for example goodwill, trademark, etc.

Tangible Assets

Tangible assets are those which can be seen and touched . For example furniture car building, etc.

Liabilities:

Liabilities are obligation or debt that an enterprise has to pay at some time in the future. They represent the creditors' claim on the firms' assets, or we can say that they are claims of those who are not owners. They can be expressed as :

Liabilities = Assets - Capital

Liabilities can be classified into following:

Long-term Liabilities *are those that are usually payable after the period of one year. They are also known as Fixed Liabilities.*

For example, long-term loan, debenture, public deposit, etc.

Short-term Liabilities *are those which are payable within a year from the date of balance sheet and paid out of current asset. For example, bank overdraft, bills payable, outstanding expenses.*

Capital:

Amount (in terms of money and asset having monetary value) invested by the owner in the firm is known as capital. For the firm, it is liability towards the owner, since owner is treated to be separate from the business. Capital is also known as owner's equity and is always equal to assets less liabilities. This can be expressed as:

Capital = Assets – Liabilities

Goods:

Goods refer to product and services in which the business unit is dealing i.e., in terms of which it is buying and selling or

producing or producing and selling. They are the physical item of trade. Here it should be noted that items which are purchased of stationery dealer, purchase of stationery will be goods for him but for others is just an item of expense.

Sales:

Sales are total revenue from goods or services sold or provided to customers when the goods are sold to cash, they are cash sales but if good are sold and payment is not received at the time of the sale, it is termed as credit sale. Some customers might return the goods, that returned portion is sale return which is deducted from the total sales but sales of fixed assets is not termed as sales.

Purchases:

Purchases are total, amount of goods procured by a business on credit and on cash, for use or sale. In manufacturing, raw material are purchased, processed further into finished goods and are then sold. In trading concern, purchases are made of merchandise for resale with or without processing.

Revenues

Revenues are the amount of the business earned by selling the goods or services to the customers, they are the inflow of asset which results in an increase owner capital sales of goods and services, earning from interest, dividends, rent, commission, etc., are some example of revenue.

Expenses

Costs incurred by the business in the process of earning revenue are known as expenses. They are the amount spend in order to produce the revenue. It decreases the capital. Expenses may include: Cost of sales, depreciation, general business expenses such as salary, advertisement, commission, rent, etc.

Expenses may classified into

Outstanding Expenses:

It refers to those Expenses which have become due during the accounting period but which yet not paid. They are liability of the firm.

Prepaid expenses:

It refers to those expenses which are not due yet but are paid well in advance. They are treated as an advances.

Expenditure:

Expenditure may be defined as money spends or liability incurred for some benefit, service or receiving property. Some of the example of expenditures are – Payment of rent, Salaries, Purchase of Goods, Purchase of Machinery, Purchase of Furniture, etc. Expenditure may be classified into:

Capital Expenditure:

Those Expenditure which are incurred for acquiring fixed assets like Building, machinery, furniture, etc., are referred to as a capital expenditure , and are shown in the balance sheet as assets

Revenue Expenditure:

Those expenditure which are incurred in the current year and benefit of which is also taken in the same accounting year. These expenditure do not result in income of the firm. All revenue expenditure is termed as expenses.

Profit

The excess of revenues of a period over its related expenses during any accounting year is profit.

⇒ ***Gross Profit***

Gross Profit is the difference between sales revenue or the proceeds of goods or services sold over its direct cost.

⇒ ***Net Profit***

It is the profit made after allowing for all expenses.

⇒ ***Gain***

Profit that arise from events or transactions which is incidental to business is termed as gain. Example for gain are: sale of fixed asset winning a court case, appreciation in value of fixed assets, etc.

Loss

The excess of expenses of a period over its related revenues is termed as loss. It decreases the owner's equity.

Loss = Expenses-Revenue

It is also referred to such activities of business which do not yield any benefit.

For example : Loss due to accident, theft etc. It also include loss on sale of fixed assets.

Income

Income is the profit earned during a period of time or we can say that the difference between revenue and expense is called income.

Income =Revenue – Expenses

Income can be classified into followings:

- **Income received in advance**

It refers to that part of income which has been received by business well in advance or before being actually earned. It is liability for the firm.

- **Accrued Income**

It refers to that part of income which has been earned by the business during the accounting year but yet not to become due, and therefore not yet received. It is treated as an asset for the firm.

Discount

Discount is the deduction in the price of the goods sold. Discount can be classified into two types:

1. Trade Discount

2. Cash Discount

♦ ***Trade Discount***

Offering any deduction at agreed percentage of sale price at the time of selling the goods, is termed as Trade Discount. It is

generally offered by manufacture to whole seller or whole seller to retailer.

It is always deducted from the sale price and no entry is made in the books of accounts.

♦ ***Cash Discount***

When the buyer is allowed some discount to induce them to make prompt payment, it is called cash discount. It is recorded in books of account.

Drawings

Any type of withdrawal i.e. in monetary terms of goods, by the owner from the business for personal use, is known as drawings. It is to be noted that drawings reduce the owner's equity in the business.

Debtors:

Those persons who owes money to the firm generally on account of credit sale of goods is called a Debtor. The total amount standing to the favor of such person and/or entity on the closing date , is shown in the balance sheet as Sundry Debtors on the asset side.

Creditor:

A person to whom the firm owes money is called a creditor. They are the persons and/or rather entities who have to be paid by an enterprise on amount for providing the goods on credit.

The total amount standing to the favor of such person and/or entity on the closing date is shown as Sundry Creditors on the liability side of balance sheet.

6.   Double Entry System:

In the present era double entry system of book keeping is considered to be the best, common and universal system. Because it modem, Scientific and complete. It fulfil the all the objectives of Businessman. Double entry system of book keeping has emerged in the process of evolution of various accounting techniques. According to it , Every transaction has Two Fold aspects debit and Credit and both aspects are to be recorded in the books of accounts. Therefore, in every transaction at least two accounts are effected.

The double entry system divides the page into two equal halves. The left hand side of each page is called the debit side, while the right hand side is called the credit side. There was no rational reason in the way in which the sides were chosen to represent different items, and the credit side could have easily been the left-hand side and the debit the right hand side. The Venation merchants who were the 'first known businessmen to use double entry just happened to select the left hand or debit side for the assets and opposite side to represent capital and liabilities, and so it has remained ever since.

7.   Mode of Accounting:

The business enterprises use accounting to calculate the profit from the business activities at the end of given period. There are two basis of calculating the profit, namely, the cash basis and accrual basis.

i)   **Cash basis of accounting:** In this basis of accounting, the income is calculated as the excess of actual cash receipts in respect of sale of goods, services, properties, etc., over actual cash payments regarding purchase of goods,

expenses on rent, electricity, salaries, etc. Credit transactions are not considered at all including adjustments for outstanding expenses and accrued income items. This method is useful for professional people like doctors, engineers, advocates, chartered accountants, brokers and small traders. It is simple to adopt because there are no adjustment entries. But this basis does not disclose the true profits because it does not consider the income and expense items which relate to the accounting period but not paid in cash. Moreover, this method is not applicable where the number of transactions is very large and expenditure on fixed assets is high. The income or profit is calculated with the help of receipts and payments account.

ii) **Accrual basis of accounting:** Under this method the items of income (revenue) are recognized when they are earned and not when the money is actually received later on. Similarly expense items are recognized when incurred and not when actual payments are made for them. It means revenue and expenses arc taken into consideration for the purpose of income determination on the basis of the accounting period to which they relate. The accrual basis makes a distinction between actual receipts of cash and the right to receive cash for revenues and the actual payments of cash and legal obligations to pay expenses. It means that income accrued in the current year becomes the income of current year whether the cash for that item of income is received in the current year or it was received in the previous year or it will be received in the next year. The same is true of expense items. Expense item is recorded if it becomes payable in the current year whether it is paid in the current year or it was paid in the previous year or it will be paid in the next year. The advantages of this system are:

8. Accounting Process:

Journal ⟶ Ledger ⟶ Trail Balance ⟶ P & L A/c

B/S Journal:

Transactions are first entered in this book to show which accounts should be debited and which credited. Journal is also called subsidiary book. Recording of transactions in journal is termed as journalizing the entries .It is the book of original entries in which transactions are entered on a day basis in chronological order. All transactions may be first recorded in the journal as and when they occur, the record is chronological, otherwise it would be difficult to maintain the records in an orderly manner. Debits and credits are listed along with the appropriate explanations. Performa is as follows:

Journal

Date	Particulars	LF	Debit Amount	Credit Amount

Ledger:

A ledger account has two sides-debit (left part of the account) and credit (right side of the part).Each of the debit and credit side has four columns. Performa as follows:

Dr   Ledger A/c   Cr

Date	Particulars	J.F	Amount	Date	Particulars	J.F	Amount

Rules Regarding Posting of entries in the Ledger:

1.   Separate Account is opened in ledger book for each account and entries from ledger posted to respective account accordingly.

2.   It is a practice to use words 'To' and 'By' while posting transactions in the ledger .The Word 'To' is used in the particular column with the accounts written on the debit side while 'By' is used with the accounts written in the particular column of the credit side.

Cash Book:

There are different types of cash books

1.   Single Column Cash Book

2.   Two Column Cash Book

3.   Three Column Cash Book

4.   Petty cash Book

Prepare simple cash book of Mr. Shiv Singh from the following transactions:

Date (Month June)	Particulars	Amount
1	Started with business with cash	10000
4	Paid for purchases	4000
7	Received from cash sales	3200
8	Paid to Raj Kumar	700
9	Received from K Kumar	900
16	Paid for stationary	137
25	Paid for office furniture	595
29	Receive from cash sales	1200
30	Paid salaries to staff	600
	Paid for office rent	350

Dr   **Simple Cash Book**   **Cr**

Date	Particulars	Lf	Amount	Date	Particulars	Lf	Amount
June1	To Capital		10000	June 4	By Purchases		4000
7	To Sales		3200	8	By Ra Kumar		700
9	To K Kumar		900	16	By Stationary		137
29	To Sales		1200	25	By Office Furniture		595
					By Office Rent		350
					By Salaries		600
					By Balance C/d		8918
			15300				**15300**
July1	To Balance B/d		8918				

Two column Cash Book:

Date	Receipts	LF	Discount	Amount	Date	Payment	LF	Discount	Amount
	To Bal b/d								

Three Column Cash Book:

Date	Receipts	LF	Discount	Cash	Bank	Date	Payments	LF	Discount	Cash	Bank

Petty Cash Book:

Receipts	Date	V.No	Particulars	Total	Conveyance	Cartage	Stationary	Postage

Trial Balance :

Name of the Account	LF	Debit	Credit
Building		XXX	-
Capital		-	XXX
Sales		-	XXX
Purchases		XXX	-
Total		**XXX**	**XXX**

Profit and Loss A/c for the year ended 31/03/20XX

Particulars	Amount	Particulars	Amount
To Opening Stock	XXX	By Sales	XXX
To Purchases	XXX	By Closing Stock	XXX
To Direct Expenses	XXX		
To Gross Profit	XXX		
Total	**XXX**	**Total**	**XXX**
To Indirect Expenses	XXX	By Gross Profit	XXX
To Net Profit	XXX	By Other Income	XXX
Total	**XXX**	**Total**	**XXX**

Balance Sheet for the year ended 31/03/20XX

Liabilities	Amount	Assets	Amount
Share Capital	XXX	Fixed Assets	XXX
Reserves & Surplus	XXX	Current Assets	XXX
Non Current Liabilities	XXX	Other Current Assets	XXX
Current Liabilities	XXX		
Total	XXX	Total	XXX

Accounting cycle is a step -by-step process of recording, Classifying and summarization of economic transactions of business. Its generates useful financial information in the form of financial statement including income statements, Balance sheet, cash flow statements and statement of change in equity.

Main steps in an accounting cycle:

1. *Collect & verify source data*

2. *Analyzing the transactions*

3. *Recording transaction via Journal Entries*

4. *Posting Journal Entries to Ledger Account*

5. *Preparing the trail balance*

6. *Preparing worksheet*

7. *Preparing Financial statements*

8. *Preparing adjusted entries at the end of the period.*

9. *Preparing post- closing trail balance*

9. Receipts and Payments & Income and Expenditure:

A Non-profit organization is a legal and accounting entity that is operated for the benefit of the society as a whole rather than for the benefit of a sole proprietor or a group of partners or shareholders. Non-profit making organization such as public hospitals, public educational institutions, clubs, temples, etc., conventionally prepare the Receipts & Payments A/c and Income and Expenditure A/c.

Financial Statement of Non-Profit Organization:

• Receipts & Payment Account equal to cash Book

• Income & Expenditure A/c Equal to Profit & Loss A/c

• Balance Sheet

Receipts & Payments A/c:

• Receipts & Payments account is a summary of the cash book without date column. It is an elementary form of account for presenting periodically the result of their working. It consists of a classified summary of Cash/Bank receipts and payments over a certain period together with the cash balances at the beginning and close of the period. The receipts are entered on the left hand side and payments on the right hand side i.e., same side as those on which they appear in cash book.

Receipts & Payment A/c for the year ended 31/03/20XX

Receipts	Amount	Payments	Amount
To Balance b/d		By Furniture	XXX
Cash Book	XXX	By Sales	XXX
Bank Book	XXX	By Balance C/d	XXX
Total	XXX	Total	XXX

Income & Expenditure A/c:

• The Income & Expenditure account is equivalent to the Profit & Loss A/c of a Business enterprise. It is an account which is widely adopted by not for profit making concern and is prepared by following accrual principle. Only items of revenue nature pertaining to the period of account are include therein. The preparation of the account, therefore, requires adjustment in relevant accounts of outstanding items of income and expenditure as also exclusion of amounts paid in advance before these are included in income and expenditure account. In so far as this, it resembles a profit and loss account and serve the same function .

Income & Expenditure A/c for the year ending 31/03/20XX

Expenditure	Amount	Income	Amount

Difference between Receipt and Payment Account and Income and Expenditure Account

Sl. No.	Particulars	Receipts & Payments Account	Income & Expenditure Account
1.	**Cash and Non cash transaction**	Only cash transactions are recorded here.	It is not confined to, cash transactions only, i.e. non-cash transactions are also included init.
2.	**Shows an items**	Receipts are shown on the debit side and payments on the credit side.	All revenue incomes appear on the credit side and expenditure on the debit side.
3.	**Capital and revenue items**	It includes both capital and revenue receipts & payment	It includes only income and expenditure of revenue nature
4.	**Balance sheet**	It includes both capital and revenue items, so it need not necessarily be accompanied by a Balance Sheet.	It includes only revenue items, so it must be accompanied by a balance sheet, the balance sheet contains the remaining balances.
5.	**Type of Account**	It is a Real Account	It is a Nominal Account
6.	**Transfer of Closing Balance**	Its balance is carried over to Receipts & Payments Account of the next year.	Its balance is transferred to Capital Fund.
7.	**Opening Balance**	This account shows opening balance except in the first year.	It has no opening balance.
8.	**Transactions**	Transactions relating to past, present and futures are recorded.	Transactions relating to currentyear only are recorded.
9.	**Adjustment**	Adjustments are not considered, because it is prepared on cash basis of accounting.	Adjustments are considered necessary because it is prepared on accrual basis of accounting.
10.	**Use of Double Entry System**	The double entry bookkeeping system is not followed while its preparation.	Double entry bookkeeping systemis followed strictly while its preparation.
11.	**Compulsory**	Its preparation is not compulsory.	It is compulsory. It must be prepared in order to ascertain the true result of a concern.
12.	**Closing Balance**	Closing balance of this account represents the closing cash inhand and at bank or overdraft at bank.	Closing balance of this account indicates either excess of income over expenditure or excess of expenditure over income.

10. Bank Reconciliation Statement:

To reconcile means to reason or find out the difference between two and eliminating that difference. Whenever we deposit or withdraw money from banks, it is always recorded in two places:

1.   Bank column of cash book and

2.   Bank Statement (Passbook)

The cash book is maintained by the person having the bank account whereas the bank statement is prepared by the bank. Therefore, the balance in both should be equal. But most of the times these two balances don't match.

Importance of Bank Reconciliation Statement:

Bank reconciliation statement is a very important tool for internal control of cash flows. It helps in detecting errors, frauds and irregularities occurred, if any , at the time of passing entries in the cash book or in the passbook , whether intentionally or unintentionally. Since frauds can be detected on the preparation of bank reconciliation statement therefore accountants are careful while preparing and maintaining the records of the business enterprises. Hence, it works as an important mechanism of internal control. Following are the silent features of BRS

1.   The reconciliation will bring out any errors that may have been committed either in the cash book or in the pass book.

2.   Any undue delay in the clearance of cheques will be shown up by the reconciliation

3.   A regular reconciliation discourages the accountant of the bank from embezzlement. There have been many cases when cashier merely made entries in the cash book but never deposited the cash in bank, they were able to get away with it only because of lack of reconciliation.

4.   It helps in finding out the actual position of the bank balance.

Causes of Difference:

The difference in the both balances (as per cash book and pass book) may be arise because of the following reasons:

⇒   **Timing:** Sometimes a transaction is recorded at two different times in cash book and the pass book. This may happen in the following cases:

- Mr. A has issued a cheque to PQR Ltd, Now, it will be recorded in his cash book immediately but the bank will recognize this transaction only when the same cheque will be presented to it by PQR Ltd.

⇒   **Transactions:** There are various transactions which the bank carries out by itself without intimating the customer.

- Interest received on a savings bank account, it will be credited by the bank immediately but the entry in the cash book will be made only when the customer comes to know about it.

⇒   **Errors:** Mistakes or errors made in preparing the accounts either by the bank or the customer can also result in disagreement of the two statements. For this reasons rectification of errors is required to be done in both the statement before preparing any bank reconciliation statement.

Some of the items that frequently cause the difference:

⇒   Cheques issued but not presented for payment

⇒   Cheques paid into the bank but not cleared

⇒   Interest allowed by the bank

⇒   Interest and expenses Charged by the bank

⇒   Interest and dividend collected by the bank

⇒   Direct payments by the bank like auto debit system.

WORKBOOK: Multiple Choice Questions

1. Scholarship granted to students out of specific funds provided by Government will be debited to

    (a)   Income and Expenditure Account

    (b)   Receipts and payments Account

    (c)   Funds

    (d)   None of the three

2. In case of NPO, excess of total assets over liabilities is known as

    (a)   Profits

    (b)   Surplus

    (c)   Capital Fund

    (d)   Accumulated Fund

3. General donations and legacies are credited to

    (a)   Receipts and Payments Account

    (b)   Income and Expenditure Account

    (c)   Capital Fund

    (d)   Fund Account

4. Interest on prize funds is

    (a)   Credited to Income and Expenditure Account

    (b)   Credited to Receipts and Payments Account

    (c)   Capital Fund

    (d)   Added to prize fund

5. Special aids are

    (a)   Treated as capital receipts

    (b)   Treated as revenue receipts

    (c)   Added to Capital Fund

    (d)   Both (a) and (c)

Unit-13:

Public Financial Management System (PFMS)

Introduction

The Public Financial Management System (PFMS) is a web-based online software application developed and implemented by the Controller General of Accounts (CGA), Department of Expenditure, Ministry of Finance, Government of India. PFMS started during 2009 with the objective of tracking funds released under all Plan schemes of Government of India, and real time reporting of expenditure at all levels of Programme implementation. Subsequently, the scope was enlarged to cover direct payment to beneficiaries under all Schemes. Gradually, it has been envisaged that digitization of accounts shall achieved through PFMS and beginning with Pay & Accounts Offices payments, the O/o CGA did further value addition by bringing in more financial activities of the Government of India in the ambit of PFMS. The outputs / deliverables for the various modes / functions of PFMS include (but are not limited to):

- Payment & Exchequer Control

- Accounting of Receipts (Tax & Non-Tax)

- Compilation of Accounts and Preparation of Fiscal Reports

- Integration with Financial Management Systems of States

The primary function of PFMS today is to facilitate sound Public Financial Management System for Government of India by establishing an efficient fund flow system as well as a payment cum accounting network. PFMS provides various stakeholders with a real time, reliable and meaningful management information system and an effective decision support system, as part of the Digital India initiative of Government of India.

PFMS is the channel for payment, accounting and reporting under Direct Benefit Transfer. As such, every Department/ Ministry of Government of India transfers funds electronically to beneficiary (individual or institution) through PFMS. Further, State Governments and the Implementing Agencies transfer the cash components to beneficiaries through PFMS. To facilitate the above, PFMS has interface with over fifty beneficiary management applications/systems of different Ministries and Departments.

PFMS was developed using an architecture which was envisaged in 2009, and as more functionalities have been added over the last few years, along with the ever-increasing depth and width of its operations, PFMS faces challenges of scalability and performance.

In this background, the O/o CGA intends to transform the current PFMS system into PFMS 2.0 with dedicated focus on process and user experience improvements, adding more functionality in core functional areas and drive end to end digital experience on the platform to serve all the stakeholders scale to tomorrows needs and perform better for peak and non-peak loads. It is envisaged to address the following major technical areas:

- Hyper-stability and scalability and Hybrid Cloud

- Sharing based database architecture

- A comprehensive data warehouse and Data cleansing

- AI, ML, Deep learning and Predictability framework

- Fraud Analytics

- High Latency, low bandwidth area operations with offline filing tools and App virtualization

- Mobility platform, bots and block chain

- Single Sign On (SSO) between applications

- An open API framework for integration

- Comprehensive PKI infrastructure & digital signing solution. Hardware Security Module (HSM) integration for management of cryptographic keys and data privacy and protection

- Comprehensive content management framework to enable paperless office (to store PDF, XML, JPG type content) with ability to digitize content store in "digitized content"

- Comprehensive DR and BCP strategy and drills parts of process

- Comprehensive data classification and privacy framework

- Comprehensive cyber security framework

- Comprehensive testing framework (unit, black box, white box, load and performance)

PFMS 2.0 is envisaged to be an effective, engaging, productive and efficient platform developed through techniques such as Design Thinking & Persona based user journeys.

1.1. Background

Public Financial Management System (PFMS) initially started as a plan scheme named CPSMS of the Planning Commission in 2008-09 as a pilot in four States of Madhya Pradesh, Bihar, Punjab and Mizoram for four Flagship schemes e.g. MGNREGS, NRHM, SSA and PMGSY. After the initial phase of establishing a network across Ministries/Departments, it has been decided to undertake National roll out of CPSMS (PFMS) to link the financial networks of Central, State Governments and the agencies of State Governments. The scheme was included in 12th Plan initiative of Planning Commission and Ministry of Finance.

The schemes sponsored by Government of India for Central Sector Scheme (CS) and Centrally Sponsored Scheme (CSS) a sanctioned order, followed by credit to the organizations for receiving funds.

Before, the process has been dependent on the physical orders. Due to computerization at Central Ministry level and also at State/Organization level. It is feasible now to implement various processes under e-Governance. The link between the two can be established by exchanging the data electronically by means of Public Financial Management System (PFMS).

1.2. Mandate

The mandate given to PFMS by Cabinet decision is to provide:

1.2.1.   A financial management platform for all plan schemes. A database of all recipient agencies, integration with core banking solution of banks handling plan funds, integration with State Treasuries. Efficient and effective tracking of fund flow to the lowest level of implementation for plan scheme of the Government.

1.2.2.   To provide information across all plan schemes/ implementation agencies in the country on fund utilization leading to better monitoring.

1.2.3.   Real-time information on resource availability and utilization across schemes.

1.2.4.   PFMS, a web based online management application is an information and decision support system for the plan schemes of the Government of India.

1.2.5.   The purpose of this system is to track and monitor fund disbursement and utilization under Plan Schemes on real time monitoring basis. PFMS is being implemented by the Office of the Controller General of Accounts (CGA), Ministry of Finance in technical collaboration with National Informatics Centre (NIC). The Portal provides a platform to enter all the transactions of expenditure, advances and transfers and also keeps track of real time monitoring of the funds allocated to various schemes and organizations.

1.3. Features of PFMS

1.3.1.   It's a web-based application/online management information and decision support system.

1.3.2.   Just in time- Release of funds.

1.3.3.   Complete tracking of funds and monitoring of its usage including information on its ultimate utilization.

1.4. Objectives of the PFMS

1.4.1.   To provide a financial management platform for all schemes, a database of all recipient agencies and integration with core banking solution of banks handling plan funds, integration with State Treasuries and efficient and effective tracking of fund flow to the lowest level of implementation for the schemes of the government.

1.4.2.   To provide information across all schemes/implementation agencies in the country on fund utilization leading to better monitoring review and decision support system to enhance public accountability in the implementation of the schemes

1.4.3.   To provide effectiveness and economy in Public Finance Management through better cash management for Government transparency in public expenditure and real-time information on resources availability and utilization across schemes. The rollout will also result in improved programme administration and management, reduction of float in the system, direct payment to beneficiaries and greater transparency and accountability in the use of public funds. PFMS will be an important tool for improving governance.

1.4.4.   To provide digitization of Government Accounts.

1.5. Benefits of PFMS in General

1.5.1. Improved programme administration and management

1.5.2. Reduction of float in the system

1.5.3. Direct payment to beneficiaries

1.5.4. Greater transparency and accountability in the use of public funds

1.5.5. State Government receives details of funds devolved from GoI immediately

1.5.6. Copies of sanction orders will be available in PDF for the users.

1.5.7. As the data will be available in xml format, the same could be consumed in their system for reporting purposes.

1.6 Benefits of PFMS to Various Stakeholders
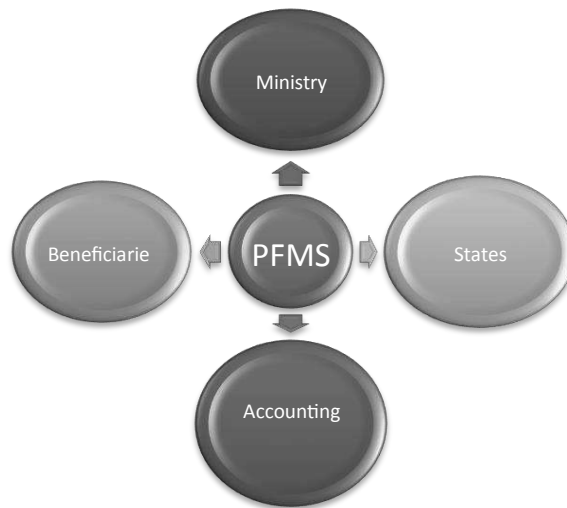
1.6.1. The information on releases can be used to communicate to the respective departments in the State for further release.

1.6.2. Efficient and effective tracking of fund flow to the lowest level of implementation for the scheme of the Government

1.6.3. To provide information across all scheme's implementation agencies in the country on fund utilization leading to better monitoring review.

1.6.4. Decision support system to enhance public accountability in the implementation of plan schemes.

1.6.5. Validation of Bank Accounts of Beneficiaries

1.6.6. Reducing failed transactions

1.6.7. Removal of Ghost beneficiaries

1.6.8. Online Status of success and failure from banks

1.6.9. Transparency and Accountability

1.6.10. Automatic Bank Validation

1.6.11.   Capturing component wise expenditure – on real time basis

1.6.12.   Tracking of flow of funds to the lowest level of implementation

1.6.13.   Online information of bank balances to facilities "just-in-time" provision of funds to implementing agencies

1.6.14.   E-Payment to ultimate beneficiaries

1.7. Bank Interface

- 1.8.1. Total 250 banks integrated with PFMS

- 1.8.2. All Nationalized Banks and SBI as well as its associate Banks

- 1.8.3. Major scheduled commercial banks including Private Sector Banks

- 1.8.4. Regional rural Banks/Cooperative banks

- 1.8.5. Indian Post

1.8. Detailed GFR Provision for PFMS

1.8.1.   **Rule 86**: PFMS, an integrated Financial Management System of Controller General of Accounts, Government of India shall be used for sanction preparation, bill processing, payment, receipt management, Direct Benefit Transfer, fund flow management and financial reporting.

1.8.2.   All the ministries sanctioning grant-in-aid shall register all implementing agencies till last level of implementation on PFMs to track fund flow and unspent balances.

1.8.3.   All the payment, to the extent possible shall be released "just-in-time" by the Ministries through PFMs.

1.8.4.   **Rule 232**: General Principles for award of Grants-in-aid for Centrally Sponsored Schemes. The following principles should be kept in view by Ministries/Department of the Central Government at the time of designing centrally sponsored schemes for implementation in State Governments or Union Territories and approving and releasing assistance to State Governments or Union Territories for such schemes.

1.8.5.   The release of funds to State Governments and monitoring further utilization should be undertaken through PFMS. The Ministries or Departments should establish a mechanism to ensure that the funds earlier released have been effectively utilized and that the data and facts reported by the State Governments or Union Territories relating to physical and financial performance are correct. Before releasing further funds, it should also be ensured that the State Governments or Union Territories have the capacity to actually spend the balance from the previous years and the releases during the current year.

2.   Enhanced Mandate of Ministry of Finance

Ministry of Finance, Dept. of Expenditure OM No 49 (7) /PF- I/ 2014 dated 02.12.2014 directed CGA to proceed with Digitization of Govt. Accounts through PFMS.

2.1. Modules to implement the Mandate:

Modules developed /under development by PFMS for stakeholders as per the Union Cabinet above mandate are as under:

2.1.1. Fund Flow Monitoring

(a)   Agency registration

(b)   Expenditure management and fund utilization through PFMS EAT module

(c)   Accounting Module for registered agencies

(d)   Treasury Interface

(e)   PFMS-PRI fund flow and utilization interface

(f)   Mechanism for State Governments towards fund tracking for State schemes

(g)   Monitoring of Externally Aided Projects (EAP):

2.1.2 Direct Benefit Transfer DBT modules

(a)   PAO to beneficiaries

(b)   Agency to beneficiaries

(c)   State treasuries to beneficiaries

2.1.3. Modules to implement the Mandate

(a)   CBS

(b)   India Post

(c)   RBI

(d)   NABARD & Cooperative Banks

2.2. Modules to implement Enhanced mandate:

2.2.1. PAO Computerization

(a)   Programme Division module

(b)   DDO module

(c)   PAO module

(d)   Pension module

(e)   GPF & HR module

(f)   Receipts including GSTN

(g) Annual Financial Statements

(h) Cash Flow Management

(i) Interface with non-civil ministries

2.2.2. Non – Tax Receipt Portal

2.3. Implementation Strategy

Action Plan has been prepared and approved by Ministry of Finance for phased implementation of Public Financial Management System.

* Improved Financial Management through

* Just in Time (JIT)

* Monitoring of use of funds including ultimate utilization strategy

* Universal rollout of PFMS which inter alia includes

* Mandatory Registration of all Implementing Agencies (IA) on PFMS and

* Mandatory use of Expenditure Advance & Transfer (EAT) Module of PFMS by all IAs

2.3.1. Implementation strategy for Central Sector (CS) Schemes/transactions

Activities to be completed

* Mandatory registration and use of EAT module by IAs

* Mapping of all relevant information of Scheme

* Uploading of budget of each scheme on PFMS

* Identify implementation hierarchy of each Scheme

* Integration of Systems Interface of specific Schemes with PFMS e.g. NREGASoft, AwasSoft

* Deployment and Training of Trainers

2.3.2. Implementation Strategy for Central Assistance to State Plan (CASP)

Activities to be completed

* State Treasury Integration with PFMS

* Registration of all SIAs on PFMS (1st level & below

* Mapping of State Schemes with corresponding central schemes

* Configuration of State Schemes on PFMS

* Configuring State Scheme Components

* Identify and configure hierarchy of each state scheme

* Integration of PFMS with Scheme specific software application

* Deployment and training of Trainers

* Continuous support for implementation

3. SOP to enter opening balance and fund received from different sources (Receipts)

Under centrally sponsored schemes, agencies are registered in PFMS under the respective schemes. All agencies must be mapped to the correct scheme and all details shall be checked. It is noticed that some agencies have been registered with multiple bank accounts for the same scheme. All such agencies shall be reviewed to ensure that there is only one account linked to the agency for the scheme under consideration.

Agency will use REAT module of PFMS to handle transactions of scheme concerned. First transaction is that of receipt received from the State treasury. This may have two components namely central share and State share. There may be receipt from other sources as well. The procedure to be followed by the All States/UTs to enter the receipt in PFMS has been explained in this SOP.

3.1. Process for implementation of PFMS to be followed by States

i. All the Project Implementing Agencies (PIA) to be registered in PFMS.

ii. Every State should have one State Nodal Agency with single State Nodal Account (SNA) for each scheme.

iii. SNA to be mapped to the particular scheme and all the funds to be transferred to PIAs through this SNA.

iv. REAT module to be used for Receipt, Expenditure, Advance and Transfer of the funds wherever applicable.

v. Needed manual entry by the States/UTs for Opening Balance and other Receipt under PFMS.

vi. Opening balance is the closing balance of the last year's audited balance sheet. Receipt from GOI and State, as received through treasury and directly for EBR. Expenditure Advance and Transfer as per books of SNA.

3.1.1. Funding Authority

i. Central Level PD (If funding level will be central govt.)

ii. State-level PD/Approval/Approval level-2 (If Funding level is State govt.)

iii. Parent Agency (If funding level is another Agency that is applicable for district, Block and GP level Agency).

3.2. Transfer of funds to State Nodal Account [SNA]

i. MoRD approves the release of funds for different components of the scheme including administrative expenditure

and IEC expenditure incurred at State, District and even Block level of the States/UTs after requisite financial concurrence.

ii.   A sanction is issued for release of funds to the State/UT using Scheme code of Centre.

iii.   The office of CCA releases fund transfer advice to RBI or other approved instrument as the case may be State treasury / UT receives the funds in its treasury.

iv.   State transfers funds from the treasury to the State Nodal Agency's bank account. This may include Central + State share.

v.   State nodal agency to have only one bank account (Called State Nodal Account) to receive this fund.

vi.   Payments of program components are directly released from the above State Nodal Account.

Source: https://pfms.nic.in

Annexure-I

ABREVATIONS

1.	MoRD	-	Ministry of Rural Development
2.	IAW	-	Internal Audit Wing
3.	RD	-	Rural Development
4.	CCA	-	Chief Controller of Accounts
5.	GFR	-	General Financial Rules
6.	CA	-	Controller of Accounts
7.	SS & FA	-	Special Secretary and Financial Advisor
8.	IAM	-	Internal Audit Manual
9.	IA	-	Internal Audit
10.	PAO	-	Pay and Accounts Office
11.	DDO	-	Drawing and Disbursing Officer
12.	NPS	-	New Pension Scheme
13.	GPF	-	General Provident Fund
14.	ICAI	-	Institute of Chartered Accounts of India.
15.	SIA	-	Standards of Internal Audit.
16.	GRIP	-	GRameen Internal Audit
17.	ATRs	-	Action Taken Reports
18.	CGA	-	Controller General of Accounts.
19.	DWS	-	Department of Watershed
20.	LR	-	Land Revenue.
21.	MoPR	-	Ministry of Panchayat Raj

1.	GOI	-	Government of India.
2.	ICT	-	Information and Communication Technology
3.	OTP	-	One Time Password
4.	CMS	-	Content Management System
5.	PDF	-	Portable Document Format
6.	JPG	-	Joint Photographic Group
7.	ACA	-	Assistant Controller of Accounts.

1.	C&AG	-	Comptroller and Auditor General of India Institute of Internal Auditors.
2.	IIA	-	Institute of Internal Auditors Chief Audit Executive
3.	CAE	-	Chief Audit Executive
4.	ISPIA	-	International Standards for Professional Practice of Internal Audit.
5.	QAIP	-	Quality Assurance and Empowerment.
6.	IPPF	-	International Professional Practices Framework.
7.	IAG	-	Internal Audit Guidelines.
8.	CoE	-	Centre of Excellence
9.	INTOSAI	-	International Organization of Supreme Audit Institutions.
10.	COSO	-	Committee of Sponsoring Organizations.
11.	DAN	-	Departmental Appreciation Note.
12.	ToR	-	Terms of Reference
13.	AAP	-	Annual Audit Plan.

Grameen Internal Audit Portal: Upgraded version

GRIP is a portal developed in consultation with O/o CCA, MoRD for digitalization of internal audit of MoRD progammes. It is developed by NIC, Ministry of Panchayati Raj, modifying the audit online portal of MoPR. The portal was inaugurated on 19th June, 2017. The portal has some basic features for audit process and some advance reporting features. Over a period of time, to harness its capacity in full capacity, a necessity has been felt to upgrade the portal with the additional features. The functionality was reviewed by DoRD. A few demonstrations were made by NIC, MoPR in the month of March, 2020. Based on the inputs during demonstration and inputs of users (members of IAW) it was found that the portal has certain limitation, it needs to be more user friendly and requires end to end solution for each process. The purpose is to make the reports at portal available to the senior officers of the State Government and also to make the portal user-friendly. The specific requirements have been identified in a series of meetings.

Activities desired to put end to end Internal Audit process on a MoRD Internal Audit portal are as under:

S. No.	Activities desired	Functionality available on GRIP
1	Provision for a Root user who creates the schemes and master users on Portal	Presently everything is with NIC, MoPR. Only limited users can be managed by the root users. No provision for master users or root users.
2	Provision for master users at each level like PD user, IAW user state level users	Not available
3	Provision for creation of users and sub users by master users	Not available
4	Provision for editing and accepting the edit in user details by reporting authority	Not available
5	Provision for master users and sub master users for configuration of scheme related information, risk matrix, etc.	Not available
6	Provision for adding auditee units and sub units up to panchayat level	Not available
7	Preparation of Audit plan on Portal, necessary changes as and when required. Putting remarks for reason for changes.	Not available for IAW
8	Formation of audit teams, assigning a unit, changes/ addition deletion, changes in dates. Putting remarks for reason for changes	Not available for IAW
9	Preparation of draft report in the field.	Not available for IAW
10	Provision for serving audit memos to auditee	Not available for IAW
11	Provision for reply of audit memos	Not available for IAW
12	Entry and exit meetings and showing draft report to Auditee.	Not available for IAW

S. No.	Activities desired	Functionality available on GRIP
13	Provision for sharing draft audit report among the audit party.	Not available for IAW
14	Provision for put up the report for approval to the reporting officer in the form of a single report.	Presently it is in individual paras and partly available in two windows.
15	Provision to mark comments and return to head of the audit party or concerned Supervisory officer or any one whom reporting officer wants to give for further improvement / necessary changes	Not available. There is provision to return only and it's rigid. It can be returned to the sender only. There is no flexibility/ choice.
16	Provision for adding additional remarks, viewing the details of auditee and correction in the details mentioned by approving	No such provision for approving authority
17	Provision for issuing digitally signed report to auditee	Partially available
18	Provision for marking copy of the report to other stake holders like PD, State nodal officer	Not available
19	Provision for head for the auditee unit to forward the report to concern for preparing draft reply.	Not available
20	Provision for sharing the draft report among the sub users of auditee	Not available
21	Provision of approving the draft Action taken report by the head of the auditee	Not available
22	Provision to submit the ATR to IAW	Not user friendly and inadequately designed. Managed by the DEOs of the IAW, MoRD. Auditee units didn't use this provision ever.
23	Provision for comments of IAW on ATR and then approval of acceptance/rejection by CCA through proper channel.	Not used
24	Reply to auditee on ATR	Not used
25	Progress of ATR and closing of the reports	Not used
26	Provision for editing draft report and ATR / attaching/ removing and supporting documents like e-office	Complex and limited.
27	Documentation on the requirement of hardware, managing the users maintaining the services on GRIP.	Not available
28	Assessment for the data recovery servers, demo server.	Not defined
29	Ownership of the portal	Not defined
30	Documentation on the role of users, access to reports, limitations, etc.	Not available
31	Miscellaneous activities to monitor the performance of certified auditors at Centre and states/ UTs.	Not available

Road map for restructuring of GRIP has been taken up under overall supervision of DDG, NIC, MoRD and necessary support is being provided by O/o CCA, DoRD, CIARD (Hyd.) and NIC, MoPR.

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National Institute of Rural Development and Panchayati Raj
Ministry of Rural Development, Government of India
Rajendranagar, Hyderabad - 500 030

TRAINING & CAPACITY BUILDING

RESEARCH & CONSULTANCY

POLICY FORMULATION & ADVOCACY

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INNOVATIVE SKILLING & LIVELIHOOD