PAPER – 6 : AUDITING AND ASSURANCE

*Question No.**1** is compulsory.*

*Attempt any **four** questions from the remaining **five** questions.*

Question 1

Examine with reasons (in short) whether the following statements are correct or incorrect:

(a) Judgemental matters are transactions that are unusual due to either its size or nature and that therefore occur infrequently.

(b) A well designed and drafted audit plan and audit strategy which takes care of all the uncertainties and conditions, need not be changed during the course of audit.

(c) An auditor is not concerned with consistency of accounting policies relating to opening balances.

(d) Audit evidence obtained from external confirmation is always reliable.

(e) Banks recognize income on Non-Performing Assets on accrual basis.

(f) Management of the organization is solely responsible for the compliance of auditing standards while preparing financial statements.

(g) The Board of Director of ABC Ltd., a listed company at Bombay Stock Exchange, is required to fill the casual vacancy of an auditor only after taking into account the recommendations of the audit committee.

(h) Any partner of an LLP, who is appointed as an auditor of a company, can sign the audit report.

(i) When auditing in an automated environment, inquiry is often the most efficient and effective audit testing method.

(j) An auditor should issue disclaimer of opinion when there is difference of opinion between him and the management on a particular point. ***(2 x 10 = 20 Marks)***

Answer

(a) ***Incorrect:*** Significant risks often relate to significant non-routine transactions or judgemental matters. Non-routine transactions are transactions that are unusual, due to either size or nature, and that therefore occur infrequently. Judgemental matters may include the development of accounting estimates for which there is significant measurement uncertainty. Thus judgemental matters are not always unusual due to their size or nature.

(b) **Incorrect:** The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit. As a result of unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures, the auditor may need to modify the overall audit strategy and audit plan and thereby the resulting planned nature, timing and extent of further audit procedures, based on the revised consideration of assessed risks.

(c) **Incorrect:** In conducting an initial audit engagement, one of the objective of the auditor with respect to opening balances is to obtain sufficient appropriate audit evidence about whether appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

(d) **Incorrect:** The reliability of information to be used as audit evidence, and therefore of the audit evidence itself, is influenced by its source and its nature, and the circumstances under which it is obtained, including the controls over its preparation and maintenance where relevant. Even when information to be used as audit evidence is obtained from sources external to the entity, circumstances may exist that could affect its reliability.

For example, information obtained from an independent external source may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity.

(e) **Incorrect:** Income from non-performing assets (NPA) is not recognised on accrual basis due to its uncertainty but is booked as income only when it is actually received.

(f) **Incorrect:** As per Section 143(9) of the Companies Act, 2013, every auditor shall comply with the auditing standards.

(g) **Correct:** Where a company is required to constitute an Audit Committee under section 177, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee.

(h) **Incorrect: Section 141(2)** of the Companies Act, 2013 states that where a firm including a limited liability partnership is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm.

(i) **Incorrect:** There are basically four types of audit tests that should be used in an automated environment. They are inquiry, observation, inspection and re-performance. Inquiry is the most efficient audit test but it also gives the least audit evidence. Hence, inquiry should always be used in combination with any one of the other audit testing methods. Inquiry alone is not sufficient. Applying inquiry in combination with inspection gives the most effective and efficient audit evidence.

(j) **Incorrect:** The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

In case of difference of opinion, either the auditor will issue qualified report or adverse report and not disclaimer of opinion.

Question 2

Discuss the following:

(a) Factors that should be considered for deciding upon the extent of checking on a sampling plan. ***(5 Marks)***

(b) "An adequate planning benefits the audit of financial statements." Discuss. ***(5 Marks)***

(c) "Professional judgment is essential to the proper conduct of an audit." Discuss. ***(5 Marks)***

(d) With respect to audit in an automated environment, explain the following:

(i) CAATs

(ii) Data Analytics

(iii) Database

(iv) Information Systems

(v) Privileged access ***(5 Marks)***

Answer

(a) The factors that should be considered for deciding upon the extent of checking on a sampling plan are following:

(i) Size of the organisation under audit.

(ii) State of the internal control.

(iii) Adequacy and reliability of books and records.

(iv) Tolerable error range.

(v) Degree of the desired confidence.

(b) Benefits of Planning in the audit of financial statements: Planning an audit involves establishing the overall audit strategy for the engagement and developing an audit plan. Adequate planning benefits the audit of financial statements in several ways, including the following:

1. Helping the auditor to devote appropriate attention to important areas of the audit.
2. Helping the auditor identify and resolve potential problems on a timely basis.
3. Helping the auditor properly organize and manage the audit engagement so that it is performed in an effective and efficient manner.
4. Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks, and the proper assignment of work to them.
5. Facilitating the direction and supervision of engagement team members and the review of their work.

6. Assisting, where applicable, in coordination of work done by auditors of components and experts.

(c) **Professional judgment is essential to the proper conduct of an audit.** This is because interpretation of relevant ethical requirements and the SAs and the informed decisions required throughout the audit cannot be made without the application of relevant knowledge and experience to the facts and circumstances. Professional judgment is necessary in particular regarding decisions about:

(i) Materiality and audit risk.

(ii) The nature, timing, and extent of audit procedures used to meet the requirements of the SAs and gather audit evidence.

(iii) Evaluating whether sufficient appropriate audit evidence has been obtained, and whether more needs to be done to achieve the objectives of the SAs and thereby, the overall objectives of the auditor.

(iv) The evaluation of management's judgments in applying the entity's applicable financial reporting framework.

(v) The drawing of conclusions based on the audit evidence obtained, for example, assessing the reasonableness of the estimates made by management in preparing the financial statements.

(d) **(i)** **CAATs**: Short form for Computer Assisted Audit Techniques, are a collection of computer based tools and techniques that are used in an audit for analysing data in electronic form to obtain audit evidence.

(ii) **Data Analytics:** A combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information

(iii) **Database:** A logical subsystem within a larger information system where electronic data is stored in a predefined form and retrieved for use.

(iv) **Information Systems:** Refers to a collection of electronic hardware, software, networks and processes that are used in a business to carry out operations and transactions.

(v) **Privileged access:** A type of super user access to information systems that enforces less or no limits on using that system.

Question 3

(a) M/s Pankaj & Associates, Chartered Accountants, have been appointed as an auditor of ABC Limited. CA Pankaj did not apply any audit procedures regarding opening balances. He argued that since financial statements were audited by the predecessor auditor therefore he is not required to verify them. Is CA Pankaj correct in his approach?

(5 Marks)

(b) *"While the auditor may choose to analyse the monthly trends for expenses like rent, power and fuel but for other expenses, an auditor generally prefers to verify other attributes." Mention those attributes.* ***(5 Marks)***

(c) *Write the audit procedures to be performed as an auditor for valuation (assertion) of following:*

 (i) *Loans and Advances and other current assets.* ***(5 Marks)***

 (ii) *Finished goods and goods for resale.* ***(5 Marks)***

Answer

(a) Initial audit engagement is an engagement in which either :

 (i) The financial statements for the prior period were not audited; or

 (ii) The financial statements for the prior period were audited by a predecessor auditor.

From the above, it is quite clear that CA Pankaj is not correct *in* his approach and therefore would be required to follow the initial audit engagement and also apply audit procedures regarding opening balances.

Audit Procedures regarding Opening Balances; The auditor shall read the most recent financial statements, if any, and the predecessor auditor's report thereon, if any, for information relevant to opening balances, including disclosures.

The auditor shall obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements by:

(a) Determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, any adjustments have been disclosed as prior period items in the current year's Statement of Profit and Loss;

(b) Determining whether the opening balances reflect the application of appropriate accounting policies; and

(c) Performing one or more of the following:

 (i) Where the prior year financial statements were audited, perusing the copies of the audited financial statements including the other relevant documents relating to the prior period financial statements;

 (ii) Evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or

 (iii) Performing specific audit procedures to obtain evidence regarding the opening balances.

(b) While the auditor may choose to analyse the monthly trends for expenses like rent, power and fuel, an auditor generally prefers to vouch for other expenses to verify following attributes:

(i) Whether the expenditure pertained to current period under audit;

(ii) Whether the expenditure qualified as a revenue and not capital expenditure;

(iii) Whether the expenditure had a valid supporting like travel tickets, insurance policy, third party invoice etc.;

(iv) Whether the expenditure has been classified under the correct expense head;

(v) Whether the expenditure was authorised as per the delegation of authority matrix;

(vi) Whether the expenditure was in relation to the entity's business and not a personal expenditure

(c) (i) Audit procedure for valuation of Loans and Advances and other current assets

- Assess the allowance for doubtful accounts. Review the process followed by the Company to derive an allowance for doubtful accounts. This will include a consistency comparison with the method used in the last year, and a determination of whether the method is appropriate for the underlying business environment.
- Obtain the ageing report of loans and advances, split between not currently due, 30 days old, 30-60 days old, 60- 180 days old, 180- 365 days old and more than 365 days old. Also, obtain the list of loans and advances under litigation and compare with previous year.
- Scrutinize the analysis and identify those loans and advances that appear doubtful; Discuss with management their reasons, if any of these loans/ advances are not included in the provision for bad recoverable; Perform further testing where any disputes exist; Reach a final conclusion regarding the adequacy of the bad and doubtful loans/ advances provision.
- Assess bad loans/ advances write-offs. Prepare schedule of movements on Bad loans/ advances – Provision Accounts and loans/ advances written off.
- Check that write-offs or other reductions in the recoverable balances have been approved by an appropriate and authorised member of senior management, for example the financial controller or finance director.
- Check that the restatement of foreign currency loans and advances/ other current assets has been done properly.

(ii) Audit procedure for valuation of finished goods and goods for resale

- Enquire into what costs are included, how these have been established and ensure that the overheads included have been determined based on normal costs and appear reasonable in relation to the information disclosed in the draft financial statements.

- Ensure that inventories are valued at net realizable value if they are likely to fetch a value lower than their cost. For any such items, also verify if the relevant semi/ partly processed inventories (work in progress) and raw materials have also been written down.
- Follow up for items that are obsolete, damaged, slow moving and ascertain the possible realizable value of such items. For the purpose, request the client to provide inventory ageing split between less than 30 days, 30-60 days old, 60- 90 days old, 90- 180 days old, 180- 385 days old and more than 365 days old (refer screenshot below)
- Follow up any inventories which at time of observance of physical counting were noted as being damaged or obsolete.
- Compare recorded costs with replacement costs. Examine vendor price lists to determine if recorded cost is less than current prices.
- Calculate inventory turnover ratio. Obsolete inventory may be revealed if ratio is significantly lower.
- In manufacturing environments, test overhead allocation rates and ensure that only direct labor, direct material and overhead have been included.
- Verify the correct application of lower-of-cost-or-net realizable value principles.

Question 4

(a) "Planning is not a discrete phase of an audit, but rather a continual and iterative process." Discuss. ***(5 Marks)***

(b) "The company has raised funds by issuing fully convertible debentures. These funds were raised for the expansion and diversification of the business. However, the company utilized these funds for repayment of long term loans and advances." Advise the auditor regarding reporting requirements under CARO, 2016. ***(4 Marks)***

(c) "A multinational co. wants to appoint you to carry the statutory audit." Discuss with reference to SA 330 the substantive procedures to be performed to assess the risk of material misstatement. ***(6 Marks)***

(d) "MMJ Ltd., an unlisted public company, did not appoint any internal auditor for the financial year ending on 31st March, 2019. The company had paid up capital of ₹ 20 crores and reserves of ₹ 25 crores. Its turnover for the preceeding 3 years were ₹ 75 crores for the year ended 31st March, 2018, ₹ 150 crores for March, 2017 and ₹ 190 crores for March, 2016. The company had availed term loan from the bank of ₹130 crores. The outstanding balance of the term loan as on 31st March, 2018 is ₹ 90 crores."

As an auditor of the company, how would you deal with the above? ***(5 Marks)***

Answer

(a) Audit Planning- a Continuous Process

Planning is not a discrete phase of an audit, but rather a continual and iterative process that often begins shortly after (or in connection with) the completion of the previous audit and continues until the completion of the current audit engagement. Planning, however, includes consideration of the timing of certain activities and audit procedures that need to be completed prior to the performance of further audit procedures. For example, planning includes the need to consider, prior to the auditor's identification and assessment of the risks of material misstatement, such matters as:

(i) The analytical procedures to be applied as risk assessment procedures.

(ii) Obtaining a general understanding of the legal and regulatory framework applicable to the entity and how the entity is complying with that framework.

(iii) The determination of materiality.

(iv) The involvement of experts.

(v) The performance of other risk assessment procedures.

(b) The auditor is required to report as per clause xiv of paragraph 3 of CARO 2016, whether the company has made any preferential allotment or private placement of shares or fully or partly convertible debentures during the year under review and if so, as to whether the requirement of section 42 of the Companies Act, 2013 have been complied with and the amount raised have been used for the purposes for which the funds were raised. If not, provide the details in respect of the amount involved and nature of non-compliance;

In view of the above clause, the auditor would report that funds raised by the company for expansion and diversification of business have not been used for the said purpose rather the company has utilised these funds for repayment of long term loans and advance.

(c) Substantive procedures to be performed to assess the risk of material misstatement:

Irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance, and disclosure.

1. This requirement reflects the facts that:

   (i) the auditor's assessment of risk is judgmental and so may not identify all risks of material misstatement; and

   (ii) there are inherent limitations to internal control, including management override.

2. Depending on the circumstances, the auditor may determine that:

   - Performing only substantive analytical procedures will be sufficient to reduce audit risk to an acceptably low level. For example, where the auditor's assessment of risk is supported by audit evidence from tests of controls.

- Only tests of details are appropriate.
- A combination of substantive analytical procedures and tests of details are most responsive to the assessed risks.

3. Substantive analytical procedures are generally more applicable to large volumes of transactions that tend to be predictable over time. SA 520, "Analytical Procedures" establishes requirements and provides guidance on the application of analytical procedures during an audit.
4. The nature of the risk and assertion is relevant to the design of tests of details. For example, tests of details related to the existence or occurrence assertion may involve selecting from items contained in a financial statement amount and obtaining the relevant audit evidence. On the other hand, tests of details related to the completeness assertion may involve selecting from items that are expected to be included in the relevant financial statement amount and investigating whether they are included.
5. Because the assessment of the risk of material misstatement takes account of internal control, the extent of substantive procedures may need to be increased when the results from tests of controls are unsatisfactory.
6. In designing tests of details, the extent of testing is ordinarily thought of in terms of the sample size. However, other matters are also relevant, including whether it is more effective to use other selective means of testing.

(d) Every unlisted public company having-

(i) paid up share capital of fifty crore rupees or more during the preceding financial year; or

(ii) turnover of two hundred crore rupees or more during the preceding financial year; or

(iii) outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year; or

(iv) outstanding deposits of twenty five crore rupees or more at any point of time during the preceding financial year;

In view of above provisions, MMJ Ltd would have to appoint internal auditor for the financial year 31-03-2019 because it had availed a term loan from the bank of ₹ 130 Crores. The outstanding balance of term loan as on 31-03-2018 ₹ 90 crores would not make any difference because section is contemplating outstanding at any point of time during the preceding financial year.

Question 5

(a) "An auditor is required to make specific evaluations while forming an opinion in an audit report." State them. ***(5 Marks)***

(b) "Mr. A is offered by ABC Ltd. for appointment as cost auditor and asked to certify certain requirements before such appointment." Discuss those requirements with reference to the provisions of the Companies Act, 2013. ***(5 Marks)***

(c) Briefly mention the matters that are relevant in planning attendance at physical inventory counting. ***(5 Marks)***

(d) Write any five circumstances of conflicting or missing evidence that indicate the possibility of fraud. ***(5 Marks)***

Answer

(a) Specific Evaluations by the auditor: In particular, the auditor shall evaluate whether :

(i) The financial statements adequately disclose the significant accounting policies selected and applied;

(ii) The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;

(iii) The accounting estimates made by management are reasonable;

(iv) The information presented in the financial statements is relevant, reliable, comparable, and understandable;

(v) The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and

(vi) The terminology used in the financial statements, including the title of each financial statement, is appropriate.

(b) Cost Auditor: Rule 6 of the Companies (Cost Records and audit) rules, 2014 required the companies prescribed under the said rules to appoint an auditor within 180days of the commencement of every financial year. However, before such appointment is made, the written consent of the cost auditor to such appointment and a certificate from him or it shall be obtained.

The certificate to be obtained from the cost auditor shall certify that the-

(1) the individual or the firm, as the case may be, is eligible for appointment and is not disqualified for appointment under the Companies Act, 2013, the Cost and Works Accountants Act, 1959 and the rules or regulations made thereunder;

(2) the individual or the firm, as the case may be, satisfies the criteria provided in section 141 of the Companies Act, 2013 so far as may be applicable;

(3) the proposed appointment is within the limits laid down by or under the authority of the Companies Act, 2013; and

(4) the list of proceedings against the cost auditor or audit firm or any partner of the audit firm pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.

(c) Matters relevant in planning attendance at physical inventory counting: Matters relevant in planning attendance at physical inventory counting include, for example:

(i) Nature of inventory.

(ii) Stages of completion of work in progress.

(iii) The risks of material misstatement related to inventory.

(iv) The nature of the internal control related to inventory.

(v) Whether adequate procedures are expected to be established and proper instructions issued for physical inventory counting.

(vi) The timing of physical inventory counting.

(vii) Whether the entity maintains a perpetual inventory system.

(viii) The locations at which inventory is held, including the materiality of the inventory and the risks of material misstatement at different locations, in deciding at which locations attendance is appropriate

(ix) Whether the assistance of an auditor's expert is needed.

(d) Conflicting or missing evidence, including:

(i) Missing documents.

(ii) Documents that appear to have been altered.

(iii) Significant unexplained items on reconciliations.

(iv) Unusual discrepancies between the entity's records and confirmation replies.

(v) Large numbers of credit entries and other adjustments made to accounts receivable records.

(vi) Missing or non-existent cancelled cheques in circumstances where cancelled cheques are ordinarily returned to the entity with the bank statement.

(vii) Missing inventory or physical assets of significant magnitude.

(viii) Unavailable or missing electronic evidence, inconsistent with the entity's record retention practices or policies.

Question 6

*Answer any **four**:*

(a) "CA. NM who is rendering management consultancy service to LA Ltd. wants to accept offer letter for appointment as an auditor of the LA Ltd. for the next financial year." Discuss with reference to the provision of the Companies Act, 2013. ***(5 Marks)***

(b) *Briefly explain the provisions for qualification and appointment of Auditors under the Multi-State Co-operative Societies Act, 2002.* ***(5 Marks)***

(c) *"The Auditor should examine the efficacy of various internal controls over advances, to determine the nature, timing and extent of his substantive procedures." Discuss briefly.*

(5 Marks)

(d) *Write basic standards set for Expenditure Audit of Government.* ***(5 Marks)***

(e) *"Ramjilal & Co. had been allotted the branch audit of a nationalized bank for the year ended 31st March, 2018. In the audit planning, the partner of Ramjilal & Co., observed that the allotted branches are predominantly based in rural areas and major portion of the advances were for agricultural purpose."*

Now he needs your assistance on the following points so as to incorporate them in the audit plan:

(i) for determination of NPA norms for agricultural advances

(ii) for accounts where there is erosion in the value of security/frauds committed by the borrowers. ***(5 Marks)***

Answer

(a) Section 141(3)(i) of the Companies Act, 2013 disqualifies a person for appointment as an auditor of a company who is engaged as on the date of appointment in management consultancy service as provided in section 144. Section 144 of the Companies Act, 2013 prescribes certain services not to be rendered by the auditor which are as under:

(i) Accounting and book keeping services

(ii) Internal audit.

(iii) Design and implementation of any financially information system.

(iv) Actuarial services

(v) Investment advisory services.

(vi) Investment banking services.

(vii) Rendering of outsourced financial services

(viii) Management services and

(ix) Any other kind of services as may be prescribed

Therefore, CA. NM is advised not to accept the assignment of auditing as the management consultancy service is specifically notified in the list of services not to be rendered by him as per section 141(3)(i) read with section 144 of the Companies Act, 2013.

(b) Qualification of Auditors -Section 72 of the Multi-State Co-operative Societies Act, 2002 states that a person who is a Chartered Accountant within the meaning of the Chartered

Accountants Act, 1949 can only be appointed as auditor of Multi-State co-operative society.

However, the following persons are not eligible for appointment as auditors of a Multi-State co-operative society-

(a) A body corporate.

(b) An officer or employee of the Multi-State co-operative society.

(c) A person who is a member or who is in the employment, of an officer or employee of the Multi-State co-operative society.

(d) A person who is indebted to the Multi-State co-operative society or who has given any guarantee or provided any security in connection with the indebtedness of any third person to the Multi-State co-operative society for an amount exceeding one thousand rupees.

If an auditor becomes subject, after his appointment, to any, of the disqualifications specified above, he shall be deemed to have vacated his office as such.

Appointment of Auditors - Section 70 of the Multi-State Co-operative Societies Act, 2002 provides that the first auditor or auditors of a Multi-State co-operative society shall be appointed by the board within one month of the date of registration of such society and the auditor or auditors so appointed shall hold office until the conclusion of the first annual general meeting. If the board fails to exercise its powers under this sub-section, the Multi-State co-operative society in the general meeting may appoint the first auditor or auditors.

The subsequent auditor or auditors are appointed by Multi-State co-operative society, at each annual general meeting. The auditor or auditors so appointed shall hold office from the conclusion of that meeting until the conclusion of the next annual general meeting.

(c) Evaluation of Internal Controls over Advances: The auditor should examine the efficacy of various internal controls over advances to determine the nature, timing and extent of his substantive procedures. In general, the internal controls over advances should include*, inter alia,* the following:

(i) The bank should make an advance only after satisfying itself as to the credit worthiness of the borrower and after obtaining sanction from the appropriate authorities of the bank.

(ii) All the necessary documents (e.g., agreements, demand promissory notes, letters of hypothecation, etc.) should be executed by the parties before advances are made.

(iii) The compliance with the terms of sanction and end use of funds should be ensured.

(iv) Sufficient margin as specified in the sanction letter should be kept against securities taken so as to cover for any decline in the value thereof. The availability of sufficient margin needs to be ensured at regular intervals.

(v) If the securities taken are in the nature of shares, debentures, etc., the ownership of the same should be transferred in the name of the bank and the effective control of such securities be retained as a part of documentation.

(vi) All securities requiring registration should be registered in the name of the bank or otherwise accompanied by documents sufficient to give title to the bank.

(vii) In the case of goods in the possession of the bank, contents of the packages should be test checked at the time of receipt. The godowns should be frequently inspected by responsible officers of the branch concerned, in addition to the inspectors of the bank.

(viii) Drawing Power Register should be updated every month to record the value of securities hypothecated. These entries should be checked by an officer.

(ix) The accounts should be kept within both the drawing power and the sanctioned limit.

(x) All the accounts which exceed the sanctioned limit or drawing power or are otherwise irregular should be brought to the notice of the controlling authority regularly.

(xi) The operation of each advance account should be reviewed at least once a year, and at more frequent intervals in the case of large advances.

(d) The audit of government expenditure is one of the major components of government audit. The basic standards set for audit of expenditure are to ensure that there is provision funds authorised by competent authority fixing the limits within which expenditure can be incurred. These standards are—

(i) that the expenditure incurred conforms to the relevant provisions of the statutory enactment and in accordance with the Financial Rules and Regulations framed by the competent authority. Such an audit is called as the audit against 'rules and orders'.

(ii) that there is sanction, either special or general, accorded by competent authority authorising the expenditure. Such an audit is called as the audit of sanctions.

(iii) that there is a provision of funds out of which expenditure can be incurred and the same has been authorised by competent authority. Such an audit is called as audit against provision of funds.

(iv) that the expenditure is incurred with due regard to broad and general principles of financial propriety. Such an audit is also called as propriety audit.

(v) that the various programmes, schemes and projects where large financial expenditure has been incurred are being run economically and are yielding results expected of them. Such an audit is termed as the performance audit.

(e) (i) NPA norms for Agricultural Advances: As per the guidelines, Agricultural Advances are of two types, (1) Agricultural Advances for "long duration" crops and (2) Agricultural Advances for "short duration" crops

The "long duration" crops would be crops with crop season longer than one year and crops, which are not "long duration" crops would be treated as "short duration" crops.

The crop season for each crop, which means the period up to harvesting of the crops raised, would be as determined by the State Level Bankers' Committee in each State.

The following NPA norms would apply to agricultural advances (including Crop Term Loans):

- A loan granted for short duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for two crop seasons and,
- A loan granted for long duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season.

(ii) Accounts where there is erosion in the value of security / frauds committed by borrowers

Not prudent to follow stages of asset classification. It should be straightaway classified as doubtful or loss asset as appropriate.

(i) Erosion in the value of security can be reckoned as significant when the realisable value of the security is less than 50 per cent of the value assessed by the bank or accepted by RBI at the time of last inspection, as the case may be. Such NPAs may be straightaway classified under doubtful category and provisioning should be made as applicable to doubtful assets.

(ii) If the realisable value of the security, as assessed by the bank/ approved valuers/ RBI is less than 10 per cent of the outstanding in the borrowal accounts, the existence of security should be ignored and the asset should be straightaway classified as loss asset. It may be either written off or fully provided for by the bank.