

Contents

Stock Audit:

Introduction

Objectives of stock audit

Steps involved in stock audit

Common irregularities/ observation

Finding of stock audit & its uses.

Revenue Audit:

Introduction

Documents to be asked for/read through

Indicative scope of Revenue audit



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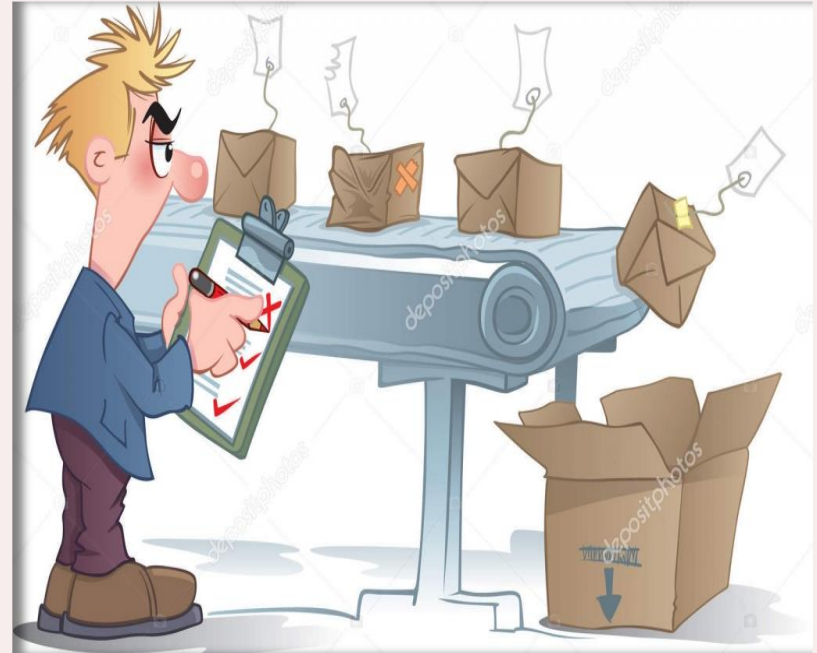
STOCK AUDIT



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INTRODUCTION

Inspection of asset charged to the lender at a regular interval is an important and desired activity of banks for monitoring and ensuring end use of funds. Besides carrying out unit inspection, banks study the borrower's books of accounts, conducting meaningful scrutiny of quarterly progress reports and also the no-lien accounts maintained with other banks at regular interval.



Further every bank has a '**stock audit policy**' under which all its branches shall arrange a "**stock audit**" of the accounts which are enjoying working capital facilities beyond certain limits. This is in addition to routine stock inspection carried out by the concerned branch.



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According to stock audit policy of the banks, the external auditors appointed by the bank shall conduct inspection of assets charged to the bank once or twice in a year as desired by the bank.



The purpose behind this check is to provide an audit or to know the position of existing stock. External auditors report is also a source of stock discrepancy information.



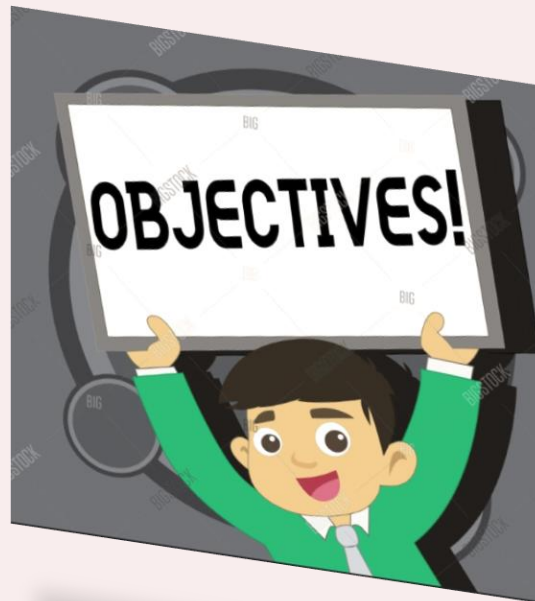
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OBJECTIVES OF STOCK AUDIT

The banker appointing the CA firm for conducting stock audit has main objective of ascertaining whether the security (borrower's stock) against which finance has been is safe and is valued correctly.

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

- a) To ensure proper **preservation/ storage** and handling of stock.
- b) To identify whether there exist any **obsolete stock**, if yes, whether it has been segregated & written off.



- c) To verify whether the stock is adequately **insured** against fire and other natural calamities (in appropriate cases against other risks like theft, burglary, marine , riots etc. As per sanction).



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Continuing...

- d) To ascertain whether physical stock **tally** with the stock statement submitted to the banker.
- e) To ascertain whether **hypothecated stock** is realizable/ Marketable.
- f) To confirm that stock is **owned** by the borrower and finance is made against value of paid stock only.
- g) To examine the age wise **debtors outstanding** as per books and as per statement submitted by the bank, steps taken for recovery of long pending debtors and likely instances of debtors turning bad, if any.
- h) Any **other matters** of interest to the bank.



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STEPS INVOLVED IN STOCK AUDIT

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

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

The whole engagement of stock audit is divided in 3 parts :-



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Visit to Borrower's Branch

Banks generally has the system of maintaining two folders for each borrower of which one is used for keeping original documents executed by the borrower while other folder contains Application form, project report, Sanction letter etc.

Scrutiny of both the files with reference to terms of sanction helps stock auditor to gain insight about the borrowers affairs and conduct audit of the account.



Documents required from bank branch officials :-

- ✓ Sanction letter & latest renewal letter.
- ✓ Stock statement (last 6 months)
- ✓ Bank statement for the last 6 months.
- ✓ Turnover report last as well as current F.Y.
- ✓ In case of Co., Copy of form CHG 8.
- ✓ Balance o/s in all A/Cs with the bank.
- ✓ DP register.
- ✓ QMR/ QMS/ QIS/ QPR for last 2 quarters.
- ✓ Branch inspection report.
- ✓ Valuation report for collateral securities.
- ✓ half yearly/ quarterly book debt CA certified book debt statement.
- ✓ If the major transaction with same party reflects in a/c statement, then relation with such party & genuineness of such transaction should be verified.



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Visit to Borrower's Premises

Visit to borrower involves-
verification of stock & debtors,
inquire about internal controls,
and analysis of past results and bank operations.
Although audit is related to stock & debtors only,
understanding of overall financial scenario &
inquiry as to sister concerns & their businesses
may also help the stock auditor to finalize the report in a better manner.



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Documents required from the Borrower:-

- ✓ Stock position as on date of verification- Age wise, Class wise stock and Book Debts
- ✓ Trial balance or provisional balance sheet as on date of verification.
- ✓ Copy of latest audited balance sheet.
- ✓ Insurance policy (Incl.bank hypothecation clause for primary as well as secondary collateral security).
- ✓ Monthwise sales- Purchase data for the previous and current financial year
- ✓ Copy of GST/ Excise Returns of the Concerned periods
- ✓ Random Ledger Extracts of Major Debtors and Creditors
- ✓ Copy of all necessary licenses and renewal status of the same
- ✓ Method of valuation followed for inventory with detailed working.
- ✓ Products manufactured with details of licensed capacity, installed capacity & actual utilized capacity.
- ✓ Latest paid Challans of various Statutory Dues (viz. PF/ ESIC/ Property Tax/ Excise Duty/ Any other cess, levy)
- ✓ Other as per the nature and size of business of borrower



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Physical verification of stock involves:-

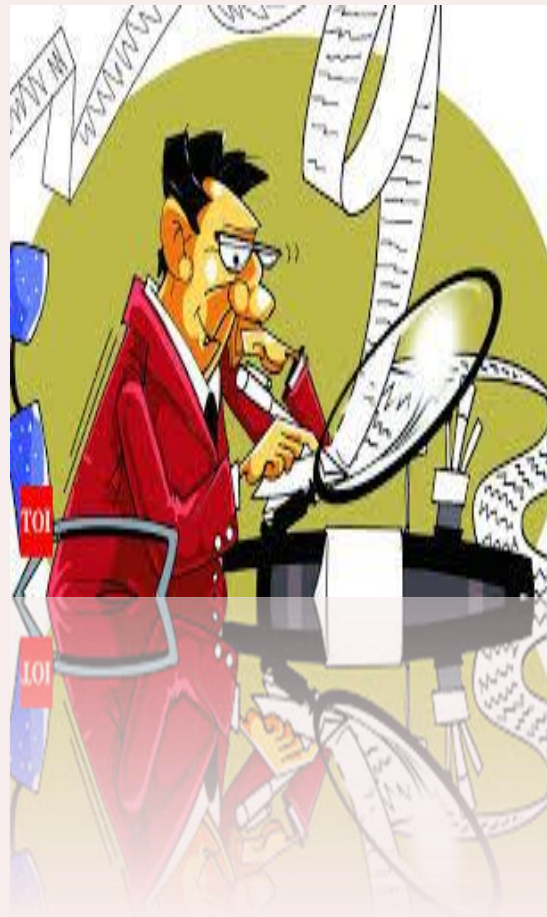
- ✓ Godown verification w.r.t. its location, condition, rent payments, maintenance etc.
- ✓ actual counting of stock & match it with book figures , reconciliation with the book figures, if there is any differences.
- ✓ Check on record- opening stock, purchase, production, sales & closing stock.
- ✓ Age wise analysis of stock & movement of stock.
- ✓ Check abnormal increase/ decrease in stock.
- ✓ Inspection of inward & outward register with the actual quantity billed & dispatched, lorry receipt etc.



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Common Irregularities / Observations in stock audit

- i. Inadequate details viz. rate, quantity and amount of different types of stock items not stated in the statement.
- ii. Debtors above 90 days (or as per sanction) considered for drawing power.
- iii. Stock, debtors & creditors figures submitted at year end in stock statement and financial statement are not matching.
- iv. Confirmation of inventory with third party not obtained.
- v. Material received from third party for job work not excluded while calculating drawing power.



- vi. Balance over drawing power although within sanctioned limit.
- vii. Under insurance of stock.
- viii. Insurance policy without bank clause.
- ix. No coverage of all risks as per sanction.
- x. Obsolete stock not excluded from stock figures submitted to bank.
- xi. Operations in the accounts not scrutinized w.r.t projections.
- xii. Defects pointed out by the Internal/ concurrent auditors are not complied.
- xiii. Cash withdrawal during current period is abnormal.



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Finding of stock audit & its uses:

Stock audit by external CA firm is one of the important tools of credit monitoring for the bank.

Apart from ensuring safety of realizable security, it also helps the bank to discipline the borrower or may act as a warning signal against probable future NPA.

It may aid the bank to take timely remedial measures to avoid substantial future losses.

It also highlights the weaknesses, if any in the existing monitoring system of the branch through comments about maintenance of DP register, scrutiny of statements and review of accounts and compliance of audit findings.

Over & above, stock audit also has the utility for the borrower. Comments about insurance inadequacies, wrong product description and location stated in the policies, if rectified timely, may save the borrower from avoidable future losses.



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REVENUE AUDIT



INTRODUCTION

Revenue Audit is the audit of items governing income and expenditure. It is conducted with a view to verify the accuracy, relevance of expenditure incurred and income earned according to applicable circulars, notifications, etc.



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DOCUMENTS TO BE ASKED FOR / TO BE READ THROUGH

- I. **Profit and Loss Account** for the audit period. (It may not be available as a single statement due to system issues so collect it as Jan. to Mar., April to Sept. and Oct. to Dec. – “Comparative Statement).

Note: scope of audit is restricted to items of revenue and expenditure only i.e. Banks major operations of Accepting Deposits and Lending.

- II. **Balance sheet** of previous year.



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III. Concurrent Audit Report Obtain copies of all concurrent audit reports pertaining to your Audit Period

Note: The concurrent audit reports give a lot of data regarding the banks operations. So do read it well before proceeding .

For e.g.: I) It gives details of accounts where limits or drawing powers have been exceeded therefore such accounts are required to be charged with overdue interest .

II) Whether Godown inspections are undertaken, if yes, whether revenue from this source is being collected.

IV. Last year's Revenue audit report/ Inspection Report



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INDICATIVE SCOPE OF REVENUE AUDIT

- a) Verification of all **Income heads** and **Expenses heads** w.r.t. income recognized and expenses charged.
- b) Correct **recovery of charges** as per the Bank's schedule of charges.
- c) Application of **Interest on Advances**.
- d) Application of **Penal Interest** on Advances.
- e) **NPA** Accounts.
- f) **Loan Processing Charges** as per sanction terms and charter of service charges.
- g) **Advances Related Charges**- Inspection charges, commitment charges, review charges, Solvency certificate issue charges etc.
- h) **Commission Charges** related to bank guarantee, foreign remittances, LC/BC, General and Life Insurance.



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- i) **Locker Rent** recovery as per the applicable charges and position of outstanding Locker Rent.
- j) Any **Other Income**.
- k) All other **Service Charges** as per latest service charges circular.
- l) **Reversal of Interests** paid or interest on premature deposits.
- m) **Interest paid** on savings account, Fixed deposits, NRE Accounts at the correct rate of interest.
- n) **System parameters** are in place for recovery of charges and there is no revenue leakage.
- o) **No debits in income** accounts without sanctions from the appropriate authority.
- p) **Reconciliations of Income and Expenditure** within the bank as well as external organizations are done on a timely basis to ensure no revenue leakage.
- q) **Revenue leakage** also in expenses incurred for operational and administrative purposes.
- r) **Recovery of charges** for services rendered for ATM / IMPS / POS (ecommerce transactions).



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E-mail: vinod@bnmca.com



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