

STOCK & BOOK DEBTS AUDIT



COVERAGE

- ✓ **Meaning - Stock and Book Debts Audit**
- ✓ **Need & Objective of Stock and Book Debts Audit & How to get empanelled for Stock Audit in Banks**
- ✓ **Frequency, Borrower eligibility & Fee for Stock Audit**
- ✓ **Procedure to be followed**
- ✓ **Scope and Coverage in Audit Report**
- ✓ **Drawing Power calculation**
- ✓ **Format of Stock Audit Report**
- ✓ **Common Irregularities observed**



MEANING OF STOCK AUDIT

- Stock audit in its general usage in the auditing world refers to the physical verification of the inventory. However it also includes many more aspects, which **depends on the terms of reference or the engagement letter of the assignment.**
- Audit with respect to the inventory and debtors against which cash credit facility is obtained from bank and other financial institutions by the borrower
- Inventories audit is about the authentication of quantity, quality, composition and valuation of the inventories and debtors.
- Arriving at the revised **drawing power** and any **other matter** connected with the **credit administration** by the banks.

NEED & OBJECTIVE OF STOCK AND BOOK DEBTS AUDIT

Bankers perspective:

- Whether stock is owned by Borrower and Finance is made available against value of paid stocks only.
- Compliance of terms & conditions of finance.
- Proper Preservation/storage of Stock.
- Whether obsolete & non-moving stock has been segregated.
- Whether stock is adequately insured against all major perils.
- Whether physical stock confirming with the stock statement submitted to the Banker.
- Age-wise & Party-wise Book-Debts analysis submitted to the Bankers tallies with the Books.



HOW TO PREPARE AND GET EMPANELLED FOR STOCK AUDIT IN BANKS

- Whether stock is owned by Borrower and Finance is made available against value of paid stocks only.
- Appointment is generally made by the Zonal or Regional office of the respective banks.
- Empanelment is generally valid for 3-4 years
- Build your Firm profile focusing experience related to Stock Audit of Banks, Stock audit of Big Corporate, Cost Audit, Revenue Audit & concurrent audit experience of banks
- No. Of partners with their details, Specifying the details of Staff(qualified and non qualified), Service Tax Registration No, RBI Unique Code ,PAN , registered address, Branch address ,etc

BORROWER

ELIGIBILITY & FREQUENCY FOR STOCK AUDIT

Eligibility of Borrower

- Where exposure (Working Capital Limit) exceeds the pre determined threshold limit (generally Rs 1 Crore)
- Stock & debtors being primary security
- To ascertaining correctness of stock statements- CA/ CWA firms are appointed to conduct stock audit
- NPA Accounts are not subjected to stock audit even if limit exceeds the threshold limit



Frequency

- Stock audit is generally conducted on yearly basis in case of Public sector Banks, however it may be on quarterly, half yearly or annual basis in case of private sector banks like Kotak Mahindra Bank & ICICI Bank

FEES

ORIENTAL BANK OF COMMERCE	
WORKING CAPITAL LIMIT	FEE PAYABLE
2 to 10	15000
>10 to 25	20000
>25 to 50	30000
>50	40000

UNION BANK	
WORKING CAPITAL LIMIT	FEE PAYABLE
upto 5 crore	10000
>5 crore to 15 crore	15000
>15 crore to 25 crore	20000
>25 crore to 40 crore	25000
>40 crore to 60 crore	35000
>60 crore to 75 crore	45000
>75 crore	50000

DENA BANK	
WORKING CAPITAL LIMIT	FEE PAYABLE
Rs.1 cr. And above upto rs.3 cr.	5000
>3 crore to 10 crore	7500
>10 crore	10000

INDIAN OVERSEAS BANK	
WORKING CAPITAL LIMIT	FEE PAYABLE
upto 1 crore	6000
>1 crore to 2 crore	8000
>2 crore to 5 crore	11000
>5 crore to 10 crore	15000
>10 crore	16000

VIJAYA BANK	
WORKING CAPITAL LIMIT	FEE PAYABLE
upto 200 LAKHS	8000
>200 LAKS to 500 LAKHS	10000
>500 LAKHS	12000

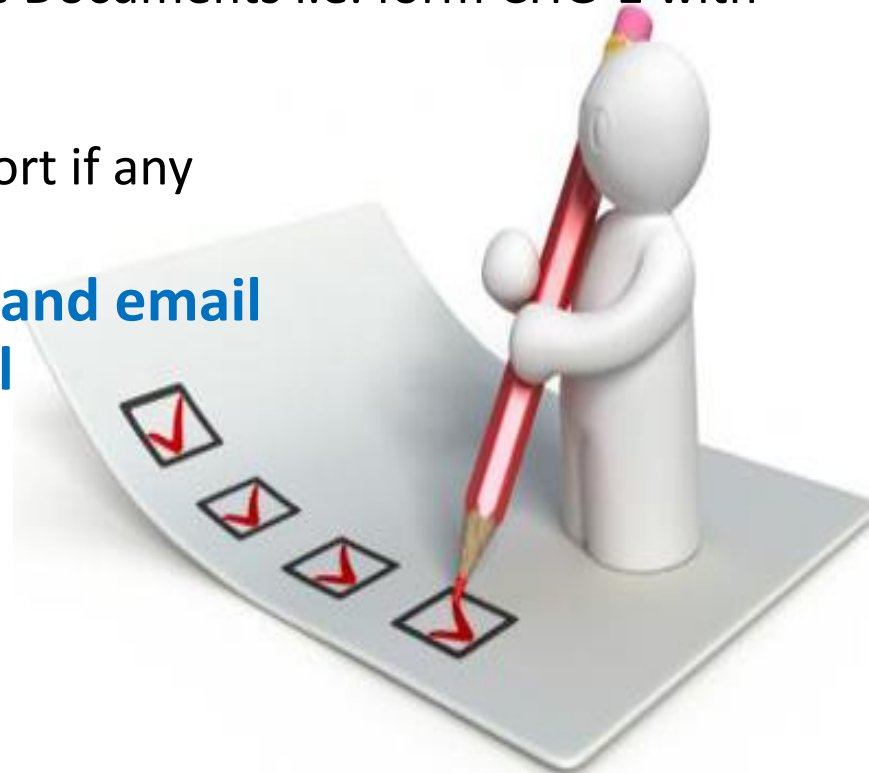
CORPORATION BANK	
WORKING CAPITAL LIMIT	FEE PAYABLE
Rs.1 cr. And above upto rs.2 cr.	12000
>2 crore to 5 crore	15000
>5 crore	20000

PROCEDURE TO BE FOLLOWED

Step 1: Visit branch and obtaining documents

- Sanction Letter
- Stock & Book Debt Statement for Last 3 Months and latest CA certified Statements (quarterly/half yearly basis)
- Bank Statement for the last 3 Months
- In case of Company, copy of ROC Charge Documents i.e. form CHG-1 with copy of Challan
- Insurance Policies
- Previous Stock Audit Report/Credit Report if any

Step 2: Take borrower Name, Mobile and email of borrower from branch- send e-mail for documents required and schedule visit date



PROCEDURE TO BE FOLLOWED....

Step 3: Visit the office of borrower

Documents to be collected

- Stock & Book Debt details from the books of accounts as on the date of Inspection and for the last three months
- Cash Book for last six months
- Audited Financial Statements and Tax Audit Reports
- Invoices of Purchases and Sales on random basis for last six months
- RG1 Registers, Excise Return, Sales Return, Stores & Spares Statement
- Details of other loans outstanding in the name of Promoters and related Parties

VERIFICATION OF STOCK

- Obtain knowledge about internal control & Management information System
- Verify whether stock as per Stock statement matches with the books of accounts
- Obtain Itemwise details of stock as on date of inspection from stock register /ERP system of the borrower
- Cross verify details of stock Register/ERP with RG1 register
- Calculate ageing of Stock from the ERP/Stock Register and identify slow moving stock
- Take sufficient sample from stock register and
- Physically verify inventory ,finished products and stores spares



VERIFICATION OF STOCK

- Analysis of Electricity Bills for the last 3 months with excise returns/RG1 Register
- Ensure whether stock received on job work basis is not included in stock value & are stored separately
- Reconcile value of stock submitted as per the statement as on the date of inspection with last stock statement submitted.
- Identify cut off date if multi-locations needs to be covered
- Stock Transfers should be supported with Form F
- Evaluate controls with regard to scrap and waste material
- Whether FIFO system is adopted so as to prevent obsolescence of old inventories
- Comment on quality of Stock
(method of storage, safety& security protection from rain ,moisture, dust & pilferage)



VALUATION OF INVENTORIES

Valuation of Inventory should be as per Accounting Standard -2, issued by The Institute of Chartered Accountants of India .

Inventory shall be valued at Cost or Net Realisable Value whichever is Lower.

Identify the valuation policy adopted (FIFO,LIFO, Weighted Average) from the Annual accounts

Identify obsolete stock and reduce it from the total value of stock



DEBTORS

- Ensure whether Sales have been timely booked
- Whether Debtors confirmation is obtained periodically.
- Identify related party transactions which may result into debtors/creditors
- Exclude related party debtors while calculating DP
- Compare the rate at which transactions are being transacted with related parties with unrelated parties



OPERATIONS IN ACCOUNT

- Whether A/C is regularly operated ?
- Whether Sales are being routed through the Account ?
- Cash Withdrawal Details/Cash Book
- Related Party Transactions – Normal Operations , Unsecured Loan
- Repayment of Loans and advances taken by Promoters

DRAWING POWER FORMULA

PARTICULARS	AMOUNT (RS)
Stock (Excluding Obsolete and slow moving stock)	XXX
Less : Trade Creditors	(XXX)
Paid up Value of Stock	XXX
Less : Margin as per Sanction Letter (Generally 25%)	(XXX)
Net Paid up Value of Stock (A)	XXXX
Trade Debtors (Not more than 90/180 Days , as per Sanction Letter)	XXX
Net Debtors	XXX
Less : Margin as per Sanction Letter	(XXX)
Net Debtors available for DP (B)	XXX
Total Drawing Power (A+B)	XXX

DRAWING POWER- EXAMPLES

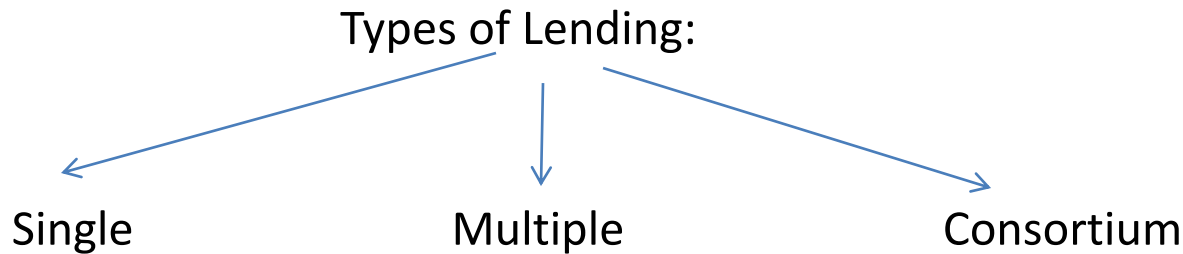
PARTICULARS	AMOUNT
Stock	1000
Less : Trade Creditors	(400)
Paid up Value of Stock	600
Less : Margin 10 %	(60)
Net Paid up Value of Stock (A)	540
Trade Debtors (Not more than 90/180 Days)	500
Net Debtors	500
Less : Margin 25%	(125)
Net Debtors available for DP (B)	375
Total Drawing Power (A+B)	915

PARTICULARS	AMOUNT
Stock	1000
Less : Margin 10%	(100)
Net Paid up Value of Stock (A)	900
Trade Debtors (Not more than 90/180 Days)	500
Less : Creditors	(400)
Net Debtors	100
Less : Margin 25%	(25)
Net Debtors available for DP (B)	75
Total Drawing Power (A+B)	975

INSURANCE

- Ensure whether Stock hypothecated is adequately Insured
- Ensure whether policies are in force
- Ensure whether Bank clause is included in policy
- Ensure Whether Stock is covered against all major perils
- Ensure whether collateral security is insured adequately
- Ensure whether all location/godown is covered in Insurance
- Ensure whether transit insurance is obtained

CONSORTIUM LENDING



- Consortium Lending: This approach to lending also called the Single Window Lending was introduced by the RBI in 1974.
- Accordingly, **more than one bank finances** a single borrower requiring large credit limit.
 - (a) enables banks to spread risk of lending,
 - (b) broke the monopoly of big banks to have large accounts,
 - (c) enables banks to share experience and expertise,
 - (d) introduces uniformity in approaches to lending,
 - (e) enables banks to pool resources, and
 - (f) checks multiple financing of the same account.

FORMAT OF REPORT- MAJOR POINTS

- Borrowers Details
- Details related to sanctioned limit
- Physical maintenance and storage of stock- Quality and Quantity checks and controls
- Identify and exclude the slow and non-moving stock items
- Borrower's Management information system & Internal controls to safeguard stock.
- Plant and machinery details installed during the year
- Method of valuation of stock and tally with stock statement
- Insurance of stock and collateral
- Verification of Debtors- ageing, turnover, more than 5% etc
- Account operations – overdrawn, credit summation and cash withdrawals
- ROC Charge
- Statutory Dues
- Compliance with other terms and conditions of sanction.
- DP calculations by Banks vs Auditors- Discrepancies, if any along with reasons
- General Checklist

COMMON IRREGULARITIES

Stock related

- Stock book not maintained/ not updated at the store.
- Obsolete stock not excluded from stock figures submitted to bank.
- Stock figures submitted at the year end to bank and as per financial statement don't match.
- Confirmation for inventory with third party not obtained or physical verification of Inventory not done.
- Material received from third parties for job work not excluded while calculating drawing power.

Debtors related

- Age wise analysis of Debtors not given / done.
- Debtors over 90 days (or as per sanction) considered for drawing power.
- Existence of long pending debtors.
- Long pending debtors shown as below 90 days debts to bank.
- Stock debtors as per statements submitted and as per books not matching.
- Dispute with debtors and pending court cases.

COMMON IRREGULARITIES...

Stock Statement related

- Stock Book Debts statements not submitted / not submitted in time.
- Inadequate details viz.- rate, quantity and amount of different type of stock items not stated in the statement.
- Scrutiny of stock statements not done.

Insurance related

- Under insurance of stock Or Insurance expired and not renewed.
- Insurance Policy without Bank Clause.
- No coverage of all risks as per sanction.
- Location of goods wrongly stated.

Bank Account related

- Cash withdrawal during current period is abnormal.
- All sales as per financial statements not routed through account.
- Account not operated actively.
- Frequent overdrawing in the account.
- Diversion of funds and inter account transfers are not properly monitored.
- Borrower having operations with other bank for which permission of lender not obtained.

COMMON IRREGULARITIES...contd

Drawing Power related

- DP Register not written up to date.
- Drawing power not correctly calculated.
- Amount receivable from Sister concern considered for calculation of drawing power.
- Advances received from debtors not reported resulting into lower DP than calculated by bank.

General

- Latest visit report by branch official not on record.
- Operations in the accounts not scrutinized with reference to projections, QIS statements, audited accounts etc.
- Defects pointed out by the Internal Auditors/ Inspectors /Concurrent Auditors are not complied with.
- Bank name plate not displayed in the godown and locations where stock is kept
- ROC Charge (Borrower-Company) not filed with the Registrar of Company
- CERSAI (Central Registry of securitization asset Interest) Charge under SARFEASI Act 2008 not created over the property given as collateral to the Bank

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

THANK YOU

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