

NAVACHETANA

INTERNAL
AUDIT

SHAISHAVI PROJECT
CONSULTANTS

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INTERNAL AUDIT POLICY

1. INTRODUCTION

Internal audit and control assists management to fulfil its responsibility of maintaining an adequate monitoring system incorporating various internal controls to the extent appropriate to the size and nature of the business. The internal auditor should reasonably assure himself that the existing systems are adequate.

Internal audit team is an independent body to ensure unbiased and independent opinions upon various functions and operations undertaken during the reporting period. The team should continuously review the operations and the conduct of all the employees of the organisation in their area of operations to ensure the maintenance of records and support the transaction with relevant facts, figures and other explanations.

Internal control system in an organisation can serve as an important tool to detect the inefficiencies existing and fractioning the system while achieving its targets. Internal control system consist of various rules brought together to achieve the robust way to find and curtail the inefficiencies existing in the system.

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

2. ROLE OF INTERNAL AUDIT

The role of internal audit is to provide independent assurance that an organization's risk management, governance and internal control processes are operating effectively. Internal auditors deal with issues that are fundamentally important to the survival and prosperity of any organization. Unlike external auditors, they look beyond financial risks and statements to consider wider issues such as the organization's reputation, growth, its impact on the environment and the way it treats its employees.

Independence and Objectivity

The internal audit activity will remain free from interference by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.

Internal auditors will have no direct operational responsibility or authority over any of the activities audited. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair internal auditor's judgment.

Internal auditors will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors will make a balanced assessment of all the relevant circumstances and not be unduly influenced by their own interests or by others in forming judgments.

3. ROLE OF AUDIT COMMITTEE

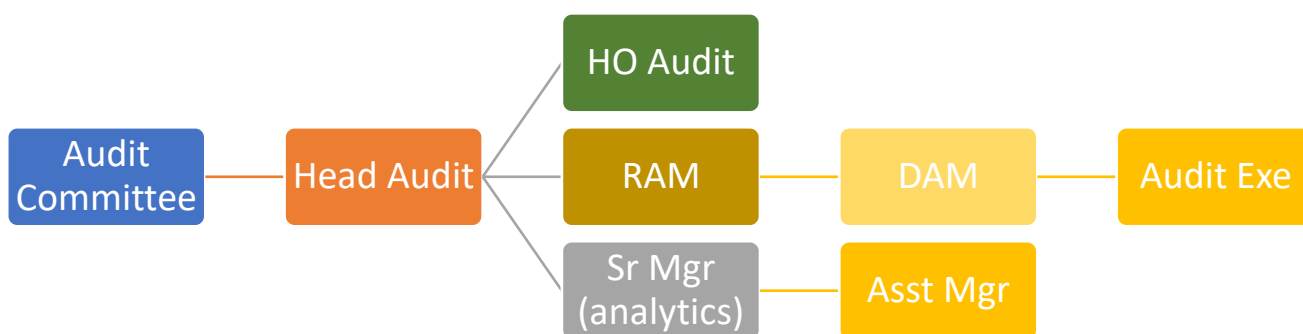
The audit committee's tasks include reviewing the company's internal controls and, company's governance and risk management systems. To do this, it utilizes the skills and expertise of the internal audit function, agreeing the scope of its work, its priorities and resources. It must also monitor and review the effectiveness of the organization's internal audit function.

The audit committee reviews and approves internal audit's remit, having regarded the complementary roles of the internal and external audit functions. It ensures that internal audit is free to work independently and objectively, i.e. free from the influence of those being audited. It ensures that internal audit has the necessary resources and access to information to enable it to fulfil its mandate and is equipped to perform in accordance with appropriate professional standards for internal auditors.

- Ensures that the Head of Internal Audit has direct access to the board chairman and to the audit committee and is accountable to the audit committee.
- Ensures that internal audit is appropriately tasked and resourced and has sufficient authority and standing to carry out its tasks effectively.
- Reviews and assesses the annual internal audit work plan.
- Receives a periodic report on the results of the internal auditors' work.
- Reviews and monitors management's responsiveness to the internal auditor's findings and recommendations.

- Meets Head of Internal Audit at least once a year without the presence of management.
- Monitors and assesses the quality and effectiveness of internal audit, and its role in the overall context of the company’s risk management system.
- Internal audit of branches is completely carried out through automation.

4. STRUCTURE



5. RISK MATRIX

TYPE OF RISK	EXPLANATION
Operational Risk	Operational risk relates to those risks which are caused due to adverse use or non-compliance of stated policies (credit, operational, HR, accounts). <i>For example:</i> Issue regarding group quality not being reinforced in fields as stated during training.
Credit Risk	Risk that affects the quality of performing assets (mainly loan portfolio) <ul style="list-style-type: none"> ▪ Poor client selection & use of inefficient appraisal technique. ▪ Poor monitoring & follow up, which increases the credit risk.
Error Risk	Mistakes done whether intentionally or unintentionally are considered as error risk. <ul style="list-style-type: none"> ▪ Incomplete loan documentation ▪ Various kinds of omissions such as not posting entry in MIS or Accounts
Fraud Risk	Frauds are intentional acts done committed for gaining advantage or making profits over and above than what one is eligible to gain. These acts are done with due care and intelligence and often difficult to detect.

6. AUDIT PLANNING

Audit plan to be prepared and approved by the Audit committee at the beginning of the year. Audit plan should make sure that all branches are covered under the Regular audit once in a month/quarter. The audit plan covers the plan for branch and HO audit. Frequency of Branch audit is fixed at monthly/quarterly, and is based on the following factors:

- Grading of previous audit
- Frauds if any reported earlier
- Volume of transactions
- Volume of collections
- Number of JLG additions/ removal during the previous audit period
- Cash mishandling if any reported earlier
- Implementation progress of follow-up audit observations
- Risk Category

Audit Frequency

The frequency of the Internal audit is finalised in discussion with the audit committee. The following audit frequency is recommended (till further amended);

- High Risk category branches audit every month
- Moderate Risk branches audit once in 2 months
- Low risk branches audited once in the quarter.

Audit Duration

High Risk category branches audit every month	4-5 days
Moderate Risk branches audit once in 2 months	3-4 days
Low risk branches audited once in the quarter	2-3 days

Audit Sampling

Audit Sampling means the application of audit procedures to less than 100% of the items within a class of transactions to enable the auditor to obtain and evaluate audit evidence about some characteristic of the items selected to form or assist in forming a conclusion concerning the population.

The population is the entire set of data from which the auditor wishes to obtain a sample to reach a conclusion. The auditor will need to determine that the population from which the sample is drawn is appropriate for the specific audit objective.

The primary consideration in determining the sample size is the amount of assurance required. While determining the sample size, the auditor should consider sampling risk, the tolerable error and the expected error. When using either statistical or non-statistical sampling methods, the auditor should design and select an audit sample, perform audit procedures thereon, and evaluate sample results to provide sufficient audit evidence.

Use judgment to select the most appropriate sample size, considering the following:

- Control frequency
- The type of evidence produced by the control
- The potential impact of the risk that the control is designed to mitigate
- Effectiveness of the entity level internal controls

7. ROLE OF HEAD INTERNAL AUDIT

- Revisit and revise Audit checklist (if required)
- Recommend changes in audit frequency & duration to Audit committee & management.
- Design Audit report formats (quantitative & qualitative)
- Manage the internal audit at all branches
- Prepares audit plan for the branches depending upon the frequency and need.
- Ensure compliance and adherence to the processes while designing audit checklists
- Monitor the overall functioning of branches and procure necessary data from all branches and HO
- Training and conflict resolution if any arising out internal audit
- To report to the appropriate authority about the findings of internal audit
- Participation in policy formulation as related to risk management and controls
- Analysing, guiding and recommending improvements in internal control and risk management based on best practices on time-to-time basis.

8. AUDIT CHECKLIST

A comprehensive audit checklist is prepared by Navachetana and the same is attached as Annexure I in the document. Four major areas of Audit is mentioned below:

- Branch Administration
- Field Operations
- Operations, Credit Risk Management & Compliance
- Branch Documentation

9. AUDIT DOCUMENTATION

Documentation of information should be sufficient, competent, relevant, and useful to provide a sound basis for audit findings and recommendations. They help the auditors in convincing the auditee about the observations made and recommendations provided. All IA staff members of Audit team should ensure that proper work paper files are maintained to support findings. The auditors need to file only those papers that would be of use either to support a finding or better understand any point revealed during the audit.

Qualities of a good working paper:

- Completeness
- Conciseness
- Uniform
- Neat
- Documents for exceptions

Copies of various documents can be used as examples, for clarification, and as physical evidence to support a conclusion or prove the existence of a problem. These documents can be memos, reports, computer printouts, procedures, forms, invoices, flow charts, contracts, or any of numerous other items.

Review of working paper

An important part of the Department's quality control program is a timely and thorough review of work papers by the team-in-charge assigned to each audit and the concerned IA personnel. The purpose/objective of work paper review is to evaluate the adequacy of audit work performed and to

determine if the predetermined audit objectives have been met. The term "audit work paper" in this context applies to both hard copy audit work papers and to files stored in computer readable form.

10.AUDIT REPORT

Audit report is a written document, which is used to formally communicate the audit findings to the Management. The report contains the following:

- **Detailed Observation** - Lists down process weakness / control gap identified and exceptions noted, during our review.

- **Root cause** - Explains the root cause of the process weakness / control gap or the exception noted and categorizes them into:
 - a) **Design Deficiency**: When the process weakness / control gap is because of inherent limitation of the business process
 - b) **Operational Inefficiency**: When the exception noted results from non-adherence to laid down procedures.
 - c) **System Deficiency**: When the process weakness / control gap is a result of inherent limitation of the information technology architecture supporting the business processes.

- **Business Impact** - Explains the possible impact of process weakness / control gap on the business Impact could be monetary or non-monetary Business impact has been classified as:
 - a) Low
 - b) Medium
 - c) High

- **Recommendation to the Management** - Explains what steps should be taken to reduce the impact created by the process weakness/ control gap or the exception noted.

- **Management Response** - Space provided for the Management to fill up the proposed action plan for the recommendation made.

Branch Audit Report

Branch Audit Report is report prepared by the Field Auditor for the observations noted during the Branch audit. Branch Audit is conducted on a quarterly basis across all branches & Monthly Audit based on the audit plan. Field Auditor performs the audit in a span of 3-5 days including JLG & customer visits.

Branch audit observations are captured by the Field auditor in the Branch audit template and finalize the audit report by end of third day of audit and shares the audit report to Corporate office along with the audit evidence collected during the audit. The Field auditor shall also report on the status of previous audit report.

The Branch/Corporate audit report is consolidated by the Senior Manager Audit – Corporate on a quarterly basis and reported to the Management and Audit Committee.

Alert Audit Report

In case of any fraud/ cash mishandling / any misappropriation/ lapse in critical process found during the Branch/ Corporate audit to be reported to the Management immediately.

HO Audit Report

HO Audit report is report prepared for the observations noted during the HO audit and the same is reported to the Internal audit and Compliance. HO audit is performed on a quarterly basis based on the Audit plan approved by the Audit Committee. The HO audit findings are reported in the HO Audit report format.

Follow-up of audit observations:

One of the primary responsibilities is determining that the auditee takes corrective action on recommendations and resolves the system inefficiency identified.

The follow up of audit issues shall be done at the time when the concerned area is audited again in case of HO and in case of Branch follow-up of previous quarter observations will be done during the current quarter audit. The team-in-charge therefore should ensure that a copy of the prior Audit report is carried when proceeding for the audit. On follow up of the issues, if it turns out that the management has not taken the corrective action that it should have then the observations should be highlighted in this section.

MIS Reporting

Management Information Systems reporting is the snapshot report presented to the Management and Internal Audit Head on a quarterly basis with the following details:

- **Branch** – Status of Branch audits, Grading Summary, Movement of Grading, Frauds if any reported and Key issues
- **HO** – Status of Corporate audits, Grading Summary, Frauds if any reported and Key issues

11.REPORTING TO AUDIT COMMITTEE

Audit Committee to be reported with the Key issues noted during the Branch audit and Corporate during the quarter. The Audit committee report to be prepared by the Manager – Corporate Audit consolidating the key observations from Branch audit and Corporate audit. Audit Committee report to be shared with the Audit Committee members five days before the Meeting date. Audit committee report comprises of the following:

- Status of Audit for the quarter
- Plan Vs Actual – Snapshot of delays in branch audit
- Branch audit - Grading across all branches for the quarter
- HO audit – Process wise grading
- Executive Summary – Corporate & Branch
- Detailed findings and recommendations

12.TIMELINES FOR REPORTING

Report	Timelines	Recipient of Report
Branch Audit Report	Last day of the audit+3 days	Division/Regional Manager Branch Manager/ Head Internal Audit/ Senior Manager – HO Audit.
Consolidated Branch Audit Report	Before 10 th of month succeeding the quarter	Head Internal Audit
HO Audit Report	Before 10 th of month succeeding the quarter	Head of Department / Internal audit & Compliance/ Business Head
MIS report	Before 10 th of month succeeding the quarter	CFO/CEO – Internal audit & Compliance/ Business Head/ MD
Audit Committee Report	5 days before the Audit Committee meeting date	Audit Committee Members/ Company Secretary
Alert Audit Report	As and when it is reported	Senior Manager/Head Internal Audit/ Internal Audit & Compliance

13.CONFIDENTIALITY OF AUDIT INFORMATION

Auditors are required by this Code to respect the confidentiality of information acquired from the various audited departments. Auditors shall not disclose any official information or use it for personal reasons without authorization. Information collected during an audit may only be used for the purpose for which it was collected and may not be disclosed other than for audit purposes. The Audit has certain practices and procedures for reporting audit findings. Disclosure of such official information by auditors shall be only with the authorization of authorities. In addition, auditors must ensure the security and confidentiality of all files, whether in the offices of Audit Cell or on the location of the auditee department.

Auditee has an interest and a right to know audit findings and conclusions. It is necessary that all audit findings and conclusions be kept confidential until they have been completely substantiated, processed through an authorized clearance procedure with the audit entity, and approved for release by the authorities. Improper or premature external disclosure of audit findings can harm the audited entity and cause embarrassment to the Department.

Due Professional Care

In exercising due professional care auditors should,

Take reasonable steps to obtain information relevant to the audit. Auditors should consider information from the institution, any changes in legislation, and the results of previous audit work.

- Keep up to date with developments in professional matters
- Look out for and consider any unusual circumstances
- Consider audit objectives and plan work to adhere to them
- Document the conclusions arising from the planning process, and detail a budget for staff and time
- Discuss the main features of the audit with the institution

14.STANDARD OF CONDUCT

- Auditor shall exercise honesty, objectivity and diligence in the performance of their duties and responsibilities.
- Auditor shall exhibit loyalty in all matters pertaining to the affairs of the organization or to whomever they may be rendering the services. However, the members shall not knowingly be part of an illegal or improper activity.

- Auditor shall not knowingly engage in acts or activities which are discreditable to the profession of Audit or to their organization.
- Auditor should refrain from entering any activity which may be in conflict with the interest of their department, or which would prejudice their ability to carry out objectively their duties and responsibilities.
- Auditor shall not accept anything of value from an employee, client, customer, supplier, or business associate of their department, which would impair or be presumed to impair their professional judgment.

15. HEAD OFFICE INTERNAL AUDIT

Internal Audit of Accounts on monthly basis and HR, Admin & IT on quarterly basis will be conducted in Navachetana.

Type and Frequency of Audits

The following types of audits would be undertaken by internal audit department at the Head office.

1). Regular Audit

- The regular audits shall be conducted Head office on monthly as per audit plan. The audit coverage would be from the date of the closing of the previous audit.
- About 10 to 15 days would be spent for a Head office audit. Audit report will be providing to Managers and Head of Departments after completion of audit.

ACCOUNTS DEPARTMENT

Data Entry:

Verification data entries and ledgers such as Current Liabilities, Duties & Taxes or Statutory reports, Sundry Creditors, Provisions and Payables, Loans, Current Assets, Fixed Assets, Sundry Debtors, Investments, Deposits, Cash Book, Bank Accounts, Receivables & Advances

- In ledger entry verification for daily transaction.
- Monthly provisions ledger verification such as Salary, Travel, Incentive Rent, Commission, Loan interest & FD accrued interest with statements and working sheet.
- Payable ledger verification like payments made on monthly bases and monthly reconciliation.
- Cash book and cash ledger cross verification and physical cash checked with ledger and Cash book
- Bank ledgers checked with Bank statements and monthly reconciliation sheet verification.
- Advance and Receivables ledgers verification like Advance ledgers monthly reconciliation made and receivable amount received on time.
- Loan accounts and cross checked with Loan statements and Repayment schedules.
- Fixed deposit accounts and cross checked with FD statements and accrued interest posting verification.

- Fixed assets ledgers crossed checked with depreciation sheet.
- Incomes ledgers cross checked and income entry made proper ledgers.
- Expenditure ledgers cross checked and expenses entry made proper ledgers.

Statutory Reports:

Statutory reports such as PF, Professional tax, ESI, TDS and GST

- Statutory ledgers such as TDS amount deduct on related expenditures and payment made within due date.
- TDS quarterly return made and cross checked with ledgers.
- PF, ESI & Professional tax deduct on applicable employee salary slab and payment made within due date.
- GST return filling made on monthly and GST amount cross check with ledgers.
- Statutory ledgers return made on monthly, Quarterly and Yearly bases.

Vouchers:

Vouchers verification such as Payment, Receipt, Journal & Contra vouchers.

- Vouchers cross check with data entry and vouchers filling date wise.
- Voucher are prepared properly observations like Debit & Credit heads mentioned and Narrations are update as per data entry.
- Payment vouchers proper expenditure bills and invoices.
- Vouchers cross checked signatures such as Scrutinized, Supervisor & Authorized.

HUMAN RESOURCE MANAGEMENT DEPT. (HR)

HR Audit will be conducted on quarterly basis and observation of Attendance Register, Leave register, Leave cards, payroll, PF, PT, ESI, Staff personal file and Travel & incentive provision and payment details.

- **Attendance Register:** We verify attendance register with employee signatures and cross verification with HR software.
- **Leave register and leave card:** We verify the leave register & leave card with attendance registers and HR software. Leave trackers cross checked with register and HR software.
- **Payroll (Salary Sheet):** We cross check the payroll with accounts provision entry and HR Salary payment details verify with Salary payable ledgers.

- **Statutory reports:** We verify the statutory reports of PF, PT, & ESI with Payroll deduction sheet and cross checked with return and payment sheet same as to be accounts ledgers.
- **Labour licence:** We verify Branch wise labour licence and renewal date checked.
- **Staff personal file:** We verify staff personal file such as Application form, Resume, KYC, Photos, Driving licence, Vehicle insurance, Employee background reports, Family details, Statutory records and Official documents.
- **Travel & Incentive:** We verify the employee travel & incentive sheet and cross checked with accounts provision and payment entry.

ADMIN DEPARTMENT

Admin Audit will be conduct on quarterly basis and observation of fixed asset register, Admin assets & expenditures invoice, Assets insurance, Rent agreement file, inward register, outward register, stationary stock and register, office documents and Vendor advance and payable.

- **Fixed Asset Register:** We verify the fixed asset register with physical assets along with serial & assets number and assets value.
- **Admin invoice and quotation:** We verify the assets quotation and invoice file and assets purchase details. Admin expenditures details cross check with accounts entry.
- **Rent agreement:** We verify the Branch wise rent agreements and we checked rent renewal date, Advance & Rent amount same as to be accounts entry. Rent payment made within agreement date.
- **Assets insurance:** We verify the fixed assets insurance cross checked accounts Fixed assets value and insurance renewal date.
- **Inward & Outward register:** We verify the inward & outward register and proper maintain and signature.
- **Stationary stock and register:** We verify the stationary stock register with physical stock and stationary purchase details & invoice verification.
- **Office Documents:** We checked office original documents properly stored and safely.
- **Vendor Advance & Payable:** Vendor advance & payment pending details verify with accounts data and month end ledger will be nil.

IT DEPARTMENT

IT Audit will be conducted on a quarterly basis and observation of IT assets, Assets agreements, IT Invoice and quotation, IT assets insurance, Server registers, Standby equipment and Vendor Advance & Payable.

- **IT assets tracker:** We verify IT assets tracker with invoice and Branch audit reports and Laptop & Tab assets check with employee wise serial and IMEI numbers wise.
- **IT assets agreement:** We checked IT assets agreement copy with IT assets tracker and Tab & Laptop agreement should be accessories details, provider and receiver signature
- **IT invoice and quotation:** We verify IT assets purchase invoice and same as to be accounts entry.
- **IT assets insurance:** IT assets insurance renewal and insurance value check.
- **Server register:** We verify server register for users and remote control.
- **Standby equipment:** We check standby equipment for intended to maintain continuous operation of a particular function.
- **Vendor Advance & Payable:** IT assets vendor advance & payment pending details verify with accounts data and month end ledger will be nil.

REPORTING, FOLLOW UP & COMPLIANCE

The Head office should ensure that the lapses observed by internal auditors are corrected during the course of audit. However, the rectifications made after being noted by the auditors.

The audit observations made during the audit would be discussed with the Head office staff and after obtaining necessary clarification and explanations if satisfied will be dropped and if not satisfied will be reported.

Manager's compliance submission within 10 days of working day after Audit reports publication. The compliance reply should be accurate and depict the correct reply to the deviations reported. Failure to send compliance report within the time limit allotted will be reported to the management for taking appropriate action in the matter.

ANNEXURE I
AUDIT CHECKLIST