

**GUIDELINE ANSWERS  
JUNE 2024 EXAMINATION  
INTERNAL AND FORENSIC AUDIT  
GROUP 1 ELECTIVE PAPER 4.2  
PROFESSIONAL PROGRAMME (NEW SYLLABUS)**

<b>Question Paper Weblink</b>	<a href="https://www.icsi.edu/media/webmodules/examination/june2024/542.pdf">https://www.icsi.edu/media/webmodules/examination/june2024/542.pdf</a>
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**PART - I**

**Answer to Question No. 1(a) (i)**

**Clarity and understanding**

- As a preparer of audit documentation, step back and read your work objectively. Would it be clear to another auditor?
- Working papers should be clear and understandable without supplementary oral explanations.
- With the information the working papers reveal, a reviewer should be able to readily determine their purpose, the nature and scope of the work done and the preparer's conclusions.

**Completeness and Accuracy**

As a reviewer of documentation, if you have to ask the audit staff basic questions about the audit, the documentation probably does not really serve the purpose. Work papers should be complete, accurate, and support observations, testing, conclusions, and recommendations. They should also show the nature and scope of the work performed appropriately indexing and cross linking with the sample supporting documents obtained.

**Answer to Question No. 1(a) (ii)**

Classification of the documents collected
Purchase Invoices issued by ABC Ltd. - Documents which have their origin in the hands of the third party and held by the organization - <b>More reliable.</b>
Purchase Orders give to TAB Ltd. - Documents which have their origin in the hands of the organization and held by the third party - <b>Reliable.</b>

Transfer documents from store to production department and Transfer documents from production room to finished goods store - Documents which have the origin in the hands of the organization and held by the organization -**Reliable only if the internal control is effective and approved as per the delegation of authority.**

#### **Answer to Question No. 1(a) (iii)**

Where in exceptional circumstances, new or additional audit procedures are performed or new conclusions are reached, the following should be documented:

1. The circumstances encountered;
2. The new or additional audit procedures performed, audit evidence obtained, and conclusions reached, and their effect on the internal auditor's report; and
3. When and by whom the resulting changes to audit documentation were made and reviewed.

#### **Answer to Question No. 1(b)**

As per CARO 2020 Rule 3(xiv), the statutory auditor's report on the accounts of a company to which this Order applies shall include a statement on the following matters, namely:

- Whether the company has an internal audit system commensurate with the size and nature of its business.
- Whether the reports of the Internal Auditors for the period under audit were considered by the statutory auditor.

The aspects that a statutory auditor needs to consider while reporting whether the reports of the Internal Auditors for the period under audit were duly considered by him / her are given below:

- i. Internal audit is completed as per the plan and the reports are made available sufficiently in time. In case required, a meeting with internal auditor to discuss the observations to independently evaluate the impact of the observations on the financial statements has been done.
- ii. All internal audit observations having a financial impact are considered by the management and control deficiencies pointed out by the internal auditors are rectified.
- iii. Impact of the control deficiencies, if any, pointed by the internal auditors on internal financial controls over financial reporting (IFCoFR) have been assessed by auditor.
- iv. Since Statutory auditor is vested with the right to receive the full-fledged internal audit reports (including draft audit reports) together with annexures and not merely the executive summary / power point presentations, whether the same were made available when requested.

**Answer to Question No. 2(a)**

Organizations are required to establish and maintain a system of internal controls sufficient to assure that

- i. transactions are executed in accordance with management's authorization;
- ii. access to assets is permitted only with the proper authorization; and
- iii. the accounting records reflect the existing assets.

Correct Classification of Controls as below:

Sr. No.	Controls Implemented	Control Classification/Type
1	Segregation of duties, rotation of jobs, background verification, Prior approvals, Firewalls, Computer and server backups	Preventive
2	Internal audits, reconciliations, financial reporting, financial statements, physical verification	Detective
3	Data Validation, audit trail, Authorization procedure, data verification	Input
4	Review of exception reports, monitoring quality controls, obtaining feedback.	Output

**Answer to Question No. 2(b)****Audit Plan**

Area	Verification Needed
1. Dispatches from factory to branches	Reconcile delivery challans with inward store entries at branches.
2. Dispatches at branch	Verify store entries with e-way bills
3. Invoicing	<ol style="list-style-type: none"> <li>(i) Verify purchase order raised by customers</li> <li>(ii) Verify e-way bills with invoices raised along with consignment note for transportation of goods in case of domestic sales</li> <li>(iii) Verify the contents of bill of entry in case of exports</li> <li>(iv) Verify the custom clearance</li> <li>(v) Verify the adequate transit insurance in both domestic and export sales</li> </ol>
4. Receivables	<ol style="list-style-type: none"> <li>(i) Verify receipts with invoices.</li> <li>(ii) Verify bank entries with customer details.</li> <li>(iii) Verification of genuineness of Credit Notes for Sales returns</li> <li>(iv) Verify age of receivables.</li> <li>(v) Carry out Balance confirmation exercises.</li> </ol>

Possible control weaknesses:

1. Goods dispatched but not billed.
2. Goods dispatched more but invoice raised for less (both quantity and value)
3. Payment not received against bills.
4. Excess credit to customer.
5. Unauthorised Credit Notes reversing revenue and misappropriating money
6. Teeming and Lading
7. Payment received but not recorded in books
8. Receipts not recorded in account of correct customers

Control features:

1. Inventory should be properly controlled and physically verified.
2. Regular reconciliation of invoices with e-way bills, weightment slip and consignment notes.
3. Follow up on receivables and ensuring age of outstanding as well as amount in the credit limit.
4. Journal entries passed in the books should be scrutinised using Data Analytics

**Answer to Question No. 2(c)**

The internal audit should verify the following:

AREA	VERIFY
Copper issued from store in Kg	Check the amount of copper issued from store
No. of starter motors issued	Check the number of starter motors issued for winding.
Entry in job work register	Verify the entries in job work register for material unused.
Amount of copper required by Bill of Material	Note the requirement as per Bill of Material.
No. of starter motors returned with winding.	Verify with job work register and security register.
Normal Loss in the process of winding	Verify normal loss in the process of winding as per past trends
Reconcile total weight of copper issued with number of starter motors.	No. of starter motors X weight of copper per motor vs weight of copper issued.
Return of Scrap Copper	Verify the scrap (normal loss) of copper has been returned by job worker.

Report on variance of copper issued vs returned.

### **Answer to Question No. 3(a)**

Some areas that internal audit should focus on when auditing the use of latest technologies in systems:

- (i) **Security and Privacy:** With the use of latest technologies, there is an increased risk of cyber threats and data breaches. Internal audit should ensure that the systems are secure and that appropriate measures are in place to protect sensitive data. This includes an assessment of the security protocols, encryption, access controls, and other security measures.
- (ii) **Governance and Management:** Internal audit should review the governance structure in place to ensure that there are adequate controls and oversight of the technology initiatives. This should include an assessment of the roles and responsibilities of key stakeholders, including the board, senior management, and the IT team. Additionally, internal audit should review the policies and procedures.
- (iii) **System Development Life Cycle:** Internal audit should ensure that appropriate controls are in place throughout the system development life cycle, from design to implementation to maintenance. This includes an assessment of the testing and validation procedures, as well as the change management process.
- (iv) **Business Continuity and Disaster Recovery:** Internal audit should ensure that appropriate measures are in place to ensure business continuity in the event of a system outage or disaster. This includes an assessment of the backup and recovery procedures, as well as the disaster recovery plan.
- (v) **Compliance:** Internal audit should ensure that the use of latest technologies is compliant with applicable laws and regulations. This includes an assessment of the data protection laws, industry-specific regulations, and other compliance requirements.

In summary, internal audit should focus on security and privacy, governance and management, system development life cycle, business continuity and disaster recovery, and compliance when auditing the use of latest technologies in systems. By doing so, internal audit can help to ensure that the risks associated with the use of these technologies are effectively managed and that the organization is able to leverage the benefits of these emerging technologies.

### **Answer to Question No. 3(b)**

One of the significant challenges of internal audit is managing the conflict of interest. In large business houses, Internal auditors are employees of the company, and they are expected to report on the operations of the business objectively. However, auditors may be hesitant to report negative findings if it could jeopardise their job security or relationship with their colleagues.

In this case also, one of the significant challenges of internal auditor is managing the conflict of interest. Mr. Raj was hesitant to accept the given role because of Conflict of interest.

Organizations can take the following precautions to avoid conflicts of interest in internal audit:

- (i) **Develop and communicate clear policies:** Organizations should establish clear policies and procedures to identify and address potential conflicts of interest. These policies should outline the steps to be taken when conflicts arise, including recusal, disclosure, or seeking a second opinion.
- (ii) **Ensure auditor independence:** Organizations should ensure that internal auditors have the necessary independence to conduct the audit objectively. This can be achieved by appointing auditors who are free from any conflicts of interest and establishing clear lines of reporting and accountability for auditors.
- (iii) **Rotate auditors:** One way to reduce conflicts of interest is to rotate auditors between different departments or functions. This can help to reduce the risk of auditors becoming too close to the business units they are auditing and enhance the objectivity of the audit process.
- (iv) **Encourage open communication:** Organizations should encourage open communication between auditors and management. This can help to ensure that any potential conflicts of interest are identified and addressed promptly.
- (v) **Foster a culture of transparency:** A culture of transparency can help to reduce conflicts of interest by promoting openness and accountability. Organizations should establish clear channels for reporting conflicts of interest and provide support to auditors who raise concerns.

### Answer to Question No. 3(c)

Classification	NPA Amount (Rs. in Lakhs)	Correct Provision Made (Rs. in Lakhs)
Standard (other than Comm. Real estate and SME) (0.40%)	10000.00	40.00
Standard (Comm. Real estate) (1%)	500.00	5.00
Sub-standard (15 %)	3500.00	525.00
Doubtful (Secured and 18 months category) (40%)	1000.00	400.00
Doubtful (Unsecured and 18 months category) (100%)	500.00	500.00

Features of Banking Operations that make internal audit of banks challenging

- Voluminous and complexity of transactions,
- Wide geographical spread of banking network,
- Diversified and large range of products and services offered,
- Extensive use of technology,
- Strict vigilance and compliance.

**Attempt all parts of either Q. No. 4 or Q. No. 4A**

**Answer to Question No. 4(a)**

The supplier should be asked for-

1. Copy of supply invoices, e-way bills, e-invoices and consignment notes and compared it with P.O or agreement
2. Statement of account to reconcile with the books of the company.
3. Copies of delivery challans, e-way bills

The accounts department will be asked to report on-

1. Payments made to supplier and entries for bill approved.
2. Reconciliation of statement of account as provided by supplier and as per our books
3. The internal auditor will also verify store inventory entries.

After this verification the internal auditor may recommend payment.

**Answer to Question No. 4(b)**

The following are to be brought out in the internal audit report.

1. The bifurcation of income of the Trust as exempt Rs. 2 Crores with respect to which no invoices have been raised.
2. Non-exempt income of Rs 3 Crores with respect to which GST invoices has been raised and GST paid.
3. Non-exempt income of Rs 4 Crores with respect to which No GST invoices has been raised and No GST paid.
4. The control systems are not working as no invoices are raised if income is not realized. The invoices should be raised as per the accounting policy of the Trust and due GST has to be paid on the basis of Time of Supply provisions.
5. There should be a complete revamp of the system so that all income is accounted for.
6. Invoices should be raised for all income whether exempt, received or taxable.
7. Also, the Trust needs to claim Income Tax exemption for which proper invoices and accounting documents are necessary.

**Answer to Question No. 4(c)**

The draft internal audit report would be as follows:

The Board of Directors  
Tele Manufacturing Ltd.  
(Place)  
(Date)

Internal Audit Report on Material Consumption  
Period covered (Date ---- to ---- Date)

1. It was noted that the adverse material consumption variance of raw material was Rs. 3 Crores (Usage Variance Rs. 1 crore and Price Variance Rs. 2 crore) more than the budget.
2. The reasons for the same were an increase in usage due to:
  - Substandard material quality
  - Machine breakdown
  - Erratic power supply
  - Worker's not being very properly trained
  - Machines being old and absence of precision CNC equipment, added to the increased consumption.
3. The price of raw material was impacted by the war in the Middle East as well as Ukraine. The government imposed a countervailing duty on the material. All these factors led to an increase in the cost of raw materials.

Remedial Measures suggested;

- a. Proper procurement planning should be done so that material can be purchased at the best price in economic quantities.
- b. Workers should be properly trained.
- c. Effective power back-ups
- d. A machine maintenance schedule should be drawn.
- e. A phased program of purchase of new CNC machine may be drawn up.

Sd/-  
XT  
Internal auditor

## **OR [ALTERNATIVE TO Q. NO. 4]**

### **Answer to Question No. 4A(a)**

As per section 138 of the Companies Act, 2013, the internal auditor shall either be a Chartered Accountant or a Cost Accountant (whether engaged in the practice or not), or such other Professional as may be decided by the Board to conduct an internal audit of the functions and activities of the company.

As per Section 144 of the Companies Act, 2013 An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be, but which shall not include inter-alia Internal Audit (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company).

The internal auditor may or may not be an employee of the company. However, Statutory Auditor shall not be appointed as internal auditor of the company.

Therefore, the appointment of AAA and Co. (Chartered Accounting firm) as an internal auditor of ABC Private Limited is not valid as AAA and Co. is also a statutory auditor of ABC Private Limited.

### **Answer to Question No. 4A(b)**

Internal Audit has become an important management tool for the following reasons:

1. Internal audit (IA) examines and assesses organisation's records and financial information, workflows, systems, and processes. Through the internal audit function, IA team will identify issues like compliance concerns, complete risk assessments, investigate internal or external fraud, and sometimes identify data inaccuracies in financial reporting.
2. Internal Auditing is a specialized service to look into the standards of efficiency of business operation.
3. Internal Auditing can evaluate various problems independently in terms of overall management control and suggest improvement.
4. Internal Audit's independent appraisal and review can ensure the reliability and promptness of MIS and the management reporting on the basis of which the top management can take firm decisions.
5. Internal Audit system makes sure the internal control system including accounting control system in an organization is effective.
6. Internal Audit ensures the adequacy, reliability and accuracy of financial and operational data by conducting appraisal and review from an independent angle.
7. Internal Audit is an integral part of "Management by System".
8. Internal Audit can break through the power ego and personality factors and possible conflicts of interest within the organization.
9. It ensures compliance of accounting procedures and accounting policies.
10. Internal Auditor can be of valuable assistance to management in acquiring new business, in promoting new products and in launching new projects for expansion or diversification of business.

**Answer to Question No. 4A(c)**

Handling personal expenses on a corporate card can lead to complications, but it's important to have a clear policy and procedure in place to address such situations.

CASH DISBURSEMENTS		YES	NO	NOT SURE	N/A
1.	Are the following duties performed by separate individuals? <ul style="list-style-type: none"> <li>• Preparing vouchers/checks</li> <li>• Approving vouchers/authorizing disbursements</li> <li>• Reconciling disbursement</li> <li>• Maintaining custody of cash</li> </ul>				
2.	Are disbursements made only from authorized expenditure accounts, trust funds, revolving funds or bank accounts and, except for petty cash payments, paid only through online vouchers, pre- numbered warrants/ checks, and/or journal entries?				
3.	Are controls in place to ensure that all disbursements are reasonable, necessary and made in accordance with state and federal regulations and County polices (as defined in the MAPP, MOUs, County Administrative Code, letter orders, OMB Circular A-87, etc.)?				
4.	Are cash advances prohibited except as authorized under special circumstances by the Board of Supervisors?				
5.	Are all disbursements supported by properly approved, original vendor invoices, employee claims, and/or contractor invoices and, if appropriate, contracts, purchase orders and receiving reports?				
6.	Are controls in place to ensure that only authorized personnel approve vouchers and sign warrants/checks?				
7.	Do voucher approvers or check/warrant signers review the supporting documentation before approving the voucher or signing the check?				
8.	Is periodically surprise physical cash verification conduct or not?				
9.	Are adequate controls maintained over unused, returned and voided checks/warrants and signature stamps, plates and files?				
10.	Are all disbursements properly recorded, classified and summarized in a cash disbursements journal?				

## **PART - B**

### **Answer to Question No. 5 (i)**

Main information in the case given is suspicion got confirmed by the whistle blower which is the starting point of any forensic audit. As per Association of Certified Fraud Examiners Report to the Nation 2024, 43% of Fraud were detected by Tip.

The forensic auditor will plan his investigation to achieve objectives such as:

- Obtain the whistleblower complaint and any supporting documentation, including emails, financial records, and other relevant evidence.
- Ensure the whistleblower's confidentiality and protection from retaliation, in accordance with company policies and relevant laws.
- Analyze the specific allegations outlined in the complaint to understand the nature and scope of the suspected misconduct.
- Identify what fraud, if any, is being carried out
- Determine the time period during which the fraud has occurred
- Discover how the fraud was concealed
- Identify the perpetrators of the fraud
- Quantify the loss suffered due to the fraud
- Gather relevant evidence that is admissible in the court
- Suggest measures that can prevent such frauds in the company in future.

Further after understanding the possible type of fraud that has been carried out and how it has been committed, the auditor is required to support the evidence collected with adequacy, enough to prove the identity of the fraudster(s) in court, reveal the details of the fraud scheme, and document the amount of financial loss suffered and the parties affected by the fraud.

### **Answer to Question No. 5 (ii)**

In order to find out collusive bidding, one need to undertake the following activities:

- Identify and interview all complainants and confidential sources to obtain further detail.
- Do due diligence background checks on the winning and losing bidders to identify, for example, undisclosed common ownership, employees or other affiliations, or prior involvement in other collusive bidding schemes.
- Obtain the bidding documents, including, if possible, bidding documents from similar prior projects (to identify bid rotation)
- Do a forensic analysis of the bids, looking for unusual bid patterns.
- Review bid securities submitted by the winning and losing bidders. Note such securities issued by the same bank on the same day to different bidders.
- Critical examine those securities that appear to be forged (this information can be used to induce the responsible party to cooperate in the investigation).
- Exercise audit rights on the winning bidder; look for evidence of collusion, for example emails between bidders setting bid prices, etc.
- Interview the winning bidder based on the evidence obtained in the investigation.

- Analyze the purchase contracts entered into in the last 5 years to comprehend since when contracts started getting awarded to related concerns.
- A disk imaging of the procurement/ committee head and his team members should be performed. The emails and other communications need to be reviewed to identify any red flags.
- Identify vendors who have been blacklisted or discontinued in the last 5 years and contact them to understand the reason for blacklisting or discontinuation.
- Are there any conflict-of-interest angle needs to be checked, i.e. any relationship exists between purchase committee members and the UBOs of the companies to whom contracts were awarded?

#### **Answer to Question No. 5 (iii)**

Following scope items are generally review by the forensic auditor and can consider reporting to management in case of procurement by non-PO route:

- Review to ensure that expenses are approved as per company policy or delegation of authority.
- Review of terms agreed with the vendors.
- Review of process to ensure desired receipt of goods/services and invoice accuracy.
- Review of process to ensure compliance to agreed terms and SLAs before processing the invoice and payment, and appropriateness of supporting evidence. This also includes review of levy of any interest, penalty or liquidated damages as per the agreed terms.
- Review of accounting controls with respect to the expense booking and payment processing.
- Review process of tracking due date for payments, and reconciliation of prepaid expenses (advance moneys paid).
- Review of segregation of duties with respect to the expense approval, receipt of goods/services, accounting and payment processing.

#### **Answer to Question No. 5 (iv)**

There are several ways in which a company can siphon off funds, including:

**Over-invoicing:** A company may inflate the cost of goods or services purchased to receive a higher amount of money from the purchaser. The excess amount paid is then siphoned off for personal gain.

**Under-invoicing:** A company may undervalue goods or services sold to reduce the amount of tax payable. The difference between the actual value and the undervalued amount is then siphoned off.

**Ghost employees:** A company may create fake employees and pay them a salary, but in reality, the money is siphoned off by the company's management.

**Round-tripping:** A company may create fictitious transactions with a third party to show an increase in revenue. The third party then returns the money, and the company's management siphons off the amount.

**Transfer pricing:** A company may manipulate prices when transferring goods or services between its subsidiaries to reduce tax payable. The difference in prices is then siphoned off.

**Misappropriation of funds:** A company's management may directly take money from the company's accounts for personal use, without any legitimate reason or business purpose.

**Offshore entities:** A company may transfer funds to an offshore entity to evade taxes or hide illegal activities. The money is then siphoned off by the company's management.

### **Attempt all parts of either Q. No. 6 or Q. No. 6A**

#### **Answer to Question No. 6 (i)**

Detection of shell companies involve examining the relationships between entities and identifying suspicious patterns.

- **Identify the Key Entities:** The first step is to identify the key entities that have to be analyzed. These could be companies, individuals, or any other relevant entities.
- **Collect Data:** Collect data on the identified entities from various sources, including public records, corporate filings, social media, and other online sources.
- **Build a Chart:** Build a chart representing the relationships between the entities.
- **Analyze the Chart:** Use link analysis techniques to identify suspicious patterns in the chart. Look for entities that are linked to multiple other entities or that have unusual patterns of connections.
- **Look for Red Flags:** Look for red flags that may indicate the presence of a shell company, such as a company with no employees or physical location, a company with a history of frequent name changes or ownership changes, or a company that is linked to other suspicious entities.
- **Investigate further:** If auditor identifies a suspicious entity, investigate further to gather more information and verify the findings. He may need to conduct additional research or consult with experts in the field to determine whether the entity is a shell company.
- **Risk Assessment:** Financial institutions should conduct a risk assessment of their customers and transactions to identify high-risk customers and transactions. This helps to allocate resources and prioritize investigations on high-risk transactions.
- **Watch list Screening:** Watch list screening involves comparing customer names against government and international watch lists of known criminals, terrorists, and politically exposed persons (PEPs). This helps to identify high-risk customers and transactions and prevent money laundering activities.
- **Data Analytics:** Financial institutions can use data analytics to identify patterns and trends in customer transactions, enabling them to identify potential money laundering activities.

Overall, fraud detection techniques in money laundering require a combination of technological solutions, human expertise, and regulatory frameworks to be effective in detecting and preventing criminal activities.

### **Answer to Question No. 6 (ii)**

Comprehensive business analysis, however, calls for going beyond the conventional financial measures to consider qualitative factors relevant for evaluating the performance and prospects of a company. The American Association of Individual Investors (AAII) has summarized these factors as follows:

1. Are the company's revenues tied to one key customer? If so, the company's performance may decline dramatically if the customer goes elsewhere. On the other hand, if the relationship is firmly entrenched, this might actually stabilize sales.
2. To what extent are the company's revenues tied to one key product? Companies that rely on a single product may be more efficient and focused, but a lack of diversification increases risk. If revenues come from several different products, the overall bottom line will be less affected by a drop in the demand for any one product.
3. To what extent does the company rely on a single supplier? Depending on a single supplier may lead to unanticipated shortages, which investors and potential creditors should consider.
4. What percentage of the company's business is generated overseas? Companies with a large percentage of overseas business are often able to realize higher growth and larger profit margins. However, firms with large overseas operations find that the value of their operations depends in large part on the value of the local currency. Thus, fluctuations in currency markets create additional risks for firms with large overseas operations.
5. Competition. Generally, increased competition lowers prices and profit margins. In forecasting future performance, it is important to assess both the likely actions of the current competition and the likelihood of new competitors in the future.
6. Future prospects. Does the company invest heavily in research and development? If so, its future prospects may depend critically on the success of new products in the pipe line. For example, the market's assessment of a computer company depends on how next year's products are shaping up. Likewise, investors in pharmaceutical companies are interested in knowing whether the company has developed any potential blockbuster drugs that are doing well in the required tests.
7. Legal and regulatory environment. Changes in laws and regulations have important implications for many industries. For example, when forecasting the future of tobacco companies, it is crucial to factor in the effects of proposed regulations and pending or likely lawsuits. Likewise, when assessing banks, telecommunications firms, and electric utilities, analysts need to forecast both the extent to which these industries will be regulated in the years ahead, and the ability of individual firms to respond to changes in regulation.

### **Answer to Question No. 6 (iii)**

The under-mentioned ratios will show the trend as well as changes that have taken place in the financial position of the company:

It's essential to compare ratios with industry benchmarks, historical performance, and peer companies to evaluate performance effectively and identify areas for improvement.

- Sales to Average Inventories held.
- Sales to Fixed Assets.
- Equity to Fixed Assets.
- Current Assets to Current Liabilities.
- Quick Assets (the current assets that are readily realizable) to Quick Liabilities.
- Equity to Long Term Loans & Interest coverage ratio.
- Sales to Book Debts.
- Return on Capital Employed.

### **Answer to Question No. 6 (iv)**

The cash-flow statement shows the movement of cash in a business. The cash-flow statement has three components: cash flows from operating activities, from financing activities and from investing activities. The statement also mentions the current cash holding of the business.

What need to check in the data is whether flows from operating activities are positive or not. If they are positive, it means that the company is able to generate cash from its operations. If they are negative, it means that the company is losing money. While it may show profits in its P&L statement, negative flows from operations should ring an alarm.

Cash flows from financing activities show the money raised for the company's operations or the money paid towards debt repayment. The former will be a positive number on the statement, while the latter will be a negative number.

Cash flows from investing activities capture the cash used in investments. For instance, a business that has generated surplus cash may park it in a bank fixed deposit. Next year it may withdraw cash from that FD. The former will be a negative number on the statement, while the latter will be a positive number.

### **OR [ALTERNATIVE TO Q. NO. 6]**

#### **Answer to Question No. 6A (a)**

The following steps are to be undertaken for employee verification.

1. Temporarily suspend employees suspected of involvement in the collusion fraud to prevent further tampering with evidence and mitigate additional losses.
2. Secure and preserve all relevant documents, emails, financial records, and any other evidence related to the fraud to prevent destruction and tampering of evidence.
3. Limit access to sensitive systems and areas to prevent destruction or manipulation of evidence.
4. Verify academic records where possible check Digi locker details.
5. Do a search for professional qualifications.
6. Ask an external agency to verify previous employer details.
7. Verify social media posts of employee and living beyond means is also a reason for fraudulent earning.

8. Scrutinize financial records, including bank statements, transaction logs, and accounting ledgers, to trace unauthorized transactions and identify patterns of fraud.
9. Conduct a comprehensive audit of stock to determine the extent of the discrepancy and identify the specific items involved.
10. Verify from police records

**Answer to Question No. 6A (b)**

1. Internal auditors play a crucial role in ensuring the integrity of financial records, compliance with regulations, and the effectiveness of internal controls. Trust and integrity are fundamental to this role.
2. Stakeholders, including investors, clients, and employees, may perceive the appointment negatively, questioning the company's judgment and commitment to ethical practices.
3. A person convicted of fraud would be liable to commit the same offence again.
4. The moral fibre of such a person is suspect.
5. Mr. A may be assumed to have contact with other criminals and reduce the likelihood of proper business control.
6. Everyone deserves a second chance, the role of an internal auditor is critical and requires the highest standards of trust and integrity.
7. Appointing a person previously convicted of fraud as IA is fraught with risks and can significantly undermine the effectiveness of the company's internal controls and stakeholder trust.
8. It is advisable to seek candidates with unblemished records who can uphold the ethical standards and responsibilities of the position.

**Answer to Question No. 6A (c)(i)**

The following steps are taken for verification of membership.

1. Define the audit scope, set objectives of audit and identify key stakeholders who will provide the information and obtain ABC Club's top management's support to assist the forensic audit.
2. Understand and document the policy and procedures of the club for accepting the membership application with supporting documents.
3. Creating a hypothesis based on available data, testing the hypothesis.
4. For the period under review verify Aadhaar Card, DOB proof and address proof of all children applicants and match it with Parent's membership.
5. Verify whether children are actually belongs to member or child purported to relative of member.
6. Verify the Children's membership records is in line with the eligibility criteria for membership.
7. Review all correspondence relating to children's membership approval or rejection and disputes if any.
8. Speak with club officials, accountants, and program coordinators to clarify any ambiguities and gather insights into potential issues.
9. Interview a sample of club members and, if appropriate, their children to validate records.

### **Answer to Question No. 6A (c)(ii)**

1. 100% verification of all applications with supporting original documents during period under review.
2. Evidence to be obtained regarding relationship of children and member.
3. All signatures of parents to be verified with the dates when they became members and also verify from photographs and signature verify with authorized government documents. More emphasis to be given on rejected application/ death of the member. A list to be maintained.
4. Check and verify from CCTV camera or functions video and photographs.
5. Laboratory analysis of physical and electronic evidence.
6. Creating a hypothesis based on available data, testing the hypothesis, Identifying the fraudsters involved. Interviewing and interrogation.

### **Answer to Question No. 6A (c)(iii)**

#### **Limitations of the Report**

1. Data is dependent on authenticity of documents and absence of digital records led to significant time in verification.
2. If there was lack of support to forensic audit from the concerned persons in charge of maintenance of membership records.
3. If the club's records are incomplete, missing, or not properly maintained, it can hinder the verification process.
4. Where photocopies of original documents are relied upon, the report will have a disclaimer.
5. All documents including electronic records are to be seen and verify with evidence.
6. Digital forensics that auditor focuses on identifying, acquiring, processing, analyzing, and reporting on data stored electronically.
7. Establish and maintain the chain of custody.

### **Answer to Question No. 6A (c)(iv)**

1. Employees involved in fraudulent activities will be subject to legal action under Indian Penal Code.
2. Temporary suspension of employees suspected of involvement in fraud pending further investigation.
3. Ensure that all relevant documents, emails, financial records, and other data are secured and preserved to prevent alteration or destruction.
4. Launch a thorough internal investigation to gather all relevant facts and evidence. This should include reviewing records, conducting interviews, and analysing data.
5. Standing orders of the club will be used to deny promotions and if possible, dismissal from service.
6. An employee may be held personally responsible, without any limitation of liability, for all or any of the liability if he or she was knowingly party to the fraudulent carrying on of business.
7. Discussion and interviews with employees.