LEARNING OUTCOMES

After studying this chapter, you will be able to:

- Understand the Regulations of Stock Exchange and legal frame of SEBI.
- Know the accounting for Stock Exchange, Rolling Settlement, Derivatives, types of markets, Margins, Circuit Filters or Circuit Breakers, role of auditor, etc.
- Gain the knowledge of Audit of Mutual Fund, Depositories, etc.
- Understand the concept of Energy Audit, Environmental Auditing and Audit of accounts of non-corporate borrower.
- Analyse the SEBI Checklist in respect of various aspects including Books of Accounts and other records, contract note, regulatory requirements, etc.
CHAPTER OVERVIEW

UNIT 1: Environmental Auditing
- Regulatory Framework
- Scope and Objective
- Features, Tools & Techniques of Environment Audit
- Environment Audit Process
- Audit Report
- Summary Flowchart

UNIT 2: Energy Audit
- Overview of Energy Audit
- Functions of Energy Auditor
- Preliminary Energy Audit
- Detailed Energy Audit and its steps
- Audit Report

UNIT 3: Audit of Accounts of Non-Corporate Borrowers
Overview
- Audit Procedures
- Special Audit Report

UNIT 4: Audit of Stock and Debtors/Unit Inspection
- Overview
- Purpose of Unit Inspection
- Audit Process
- Finding of Inspection
- Audit Report

UNIT 5: Audit of Members of Stock Exchange (SE)
- Functioning of SE
- Rolling Settlement
- Derivatives
- Circuit Filters/Breakers
- Accounting for SE
- Conduct of Audit
- Auditor's Report

UNIT 6: Audit of Mutual Fund
- Regulatory Framework
- Structure of Mutual Fund
- Risks involved in Mutual Fund Business
- Conduct of Audit
- Audit Report

UNIT 7: Audit of Depositories
- Regulatory Framework
- Inspection and Investigation
- Records and Documents to be maintained
- Inspection Report

SEBI Checklist for Auditors
UNIT 1: ENVIRONMENTAL AUDITING

1. OVERVIEW

Environmental audits are becoming increasingly common in certain industries. The term “environmental audit” has a wide variety of meanings. They can be performed by external or internal experts (sometimes including internal auditors), at the discretion of the entity’s management. In practice, persons from various disciplines can qualify to perform “environmental audits”. Often the work is performed by a multi-disciplinary team. Normally, “environmental audits” are performed at the request of management and are for internal use.

2. REGULATORY FRAMEWORK

In Indian scenario, the Regulatory Authorities like Ministry of Environment and Forest (MOEF), State Pollution Control Board (SPCB), State Department of Environment (SDOEn.) etc., have come into play to clear the projects from environmental viewpoint before it’s commissioning. The Environmental Impact Assessment (EAI) is a pre-requisite to start an industry. The EAI tries to forecast the expected damage to be caused by the development of the industries to the environmental and the means required to mitigate that damage, incorporating the same in the Project Report for compliance in due course, keeping in view the serious threat to all the living beings in the universe by the rapid industrialisation which is polluting the environmental on an irreparable extent. The Indian Govt. notified by GSR No.329E dated 13.02.1992 that “Every person carrying on an industry, operation or process requiring consent under Section 25 of the Water (Prevention and Control of Pollution) Act, 1974 (6 of 1974) or under Section 21 of the Air (Prevention and Control of Pollution) Act, 1981 (4 of 1981) or both or authorisation under the Hazardous Waste (Management and Handling) Rules, 1989 issued under Environment Protection Act, 1986 (29 of 1986) shall submit an environment audit report for the financial year ending the 31st march in form V to the concerned State Pollution Control Board on or before the 15th day of May every year, beginning 1993”.

3. SCOPE AND OBJECTIVE OF ENVIRONMENT AUDIT

With a view to define the Environmental Audit, it may be stressed that it is a critical analysis of (i) policies (ii) principles (iii) systems (iv) procedures (v) practices and (vi) performances of the aspect which relates the environment.
But a standard scope of Environmental Audit, as ought to be defined and adopted by standard companies, should be as follows:

“A management tool comprising a systematic, documented, periodic and objective evaluation of how well environmental organisation, management and equipment are performing with the aim of helping to safeguard the environment by:

(i) Facilitating management control of environmental Process.

(ii) Assessing compliance with company policies, which would include meeting regulatory requirements”.

The objective of the Environmental Audit are to evaluate the efficacy of the utilisation of resources of man, machines and materials, and to identify the areas of environmental risks and liabilities and weakness(es) of management system and problems in compliance of the directives of the regulatory agencies and control the generation of pollutants and/or waste.

As the Environmental Audit, especially in India, is still in its infancy the information usually gathered in the course of Environmental Audit is only what is required for the compliance of the statutory requirements, i.e., for Water Act, 1974, Air Act, 1981, etc., and for environmental clearance required before establishing an industry.

4. FEATURES OF ENVIRONMENTAL AUDIT

The following are features of environmental audit:

(i) Management tool – Environmental audit is generally considered as one of the management tool which is a part of internal control system and is mainly used to assess, evaluate and manage environmental performance of a company.

(ii) Aim of environmental audit – A green audit may be conducted for many purposes, for example, to comply with environmental laws or as a social responsibility measure or to meet some certification requirements. But the main and ultimate aim of any environmental audit is to evaluate and control the adverse impact of economic activities of an organization on the environment.

(iii) Environmental audit should be distinguished from Environmental Impact Assessment (EIA) – EIA is a tool used to predict, evaluate and analyze environmental impacts mostly before a project commences. It assesses the potential environmental effects of a proposed facility. The essential purpose of an environmental audit is the systematic scrutiny of environmental performance throughout a company’s existing operations.

(iv) Systematic – Environmental audit is a systematic process that must be carefully planned, structured and organized. As it is a part of a long-term process of evaluation and checking, it needs to be a repeatable process so that over time, it can be easily used by different teams of
people in such a way that the results are comparable and can reflect change in both quantitative and qualitative terms.

(v) **Documented** – Like any other audit, the base of any environmental auditing is that its findings are supported by documents and verifiable information. The audit process is designed in such a way that it seeks to verify on a sample basis past actions, activities, events and procedures with available evidences to ensure that they were carried out according to system’s requirements and in a correct manner.

(vi) **Periodic** – Environmental audit is generally conducted at pre-defined intervals. It is a long-term process.

(vii) **Objective Evaluation** – Though environmental auditing is conducted using pre-decided policies, procedures and a proper documented system, there is always an element of subjectivity in an audit, particularly if it is conducted internally. In addition to internal environmental audits, having independent audit teams that have specialized skills and who come back periodically (say annually) to repeat audits tends to increase objectivity in the system. Hence for the sake of objectivity, external environmental audits are preferable. This is also required under many certification guidelines (e.g. ISO 14001).

(viii) **Environmental Performance** – As mentioned before, the essence of any environmental audit is to find out how well the environmental organization, environmental management and environmental equipments are performing. The ultimate aim is to ensure that organization’s environmental performance meets the goals set in its environmental policy and also to ensure compliance with standards and regulatory requirements.

### 5. ENVIRONMENTAL AUDIT PROCESS

#### 5.1 Pre-audit or Planning Stage (Stage 1):

Audit planning is vital to the success of the audit undertaken. During this stage of audit, generally following steps are taken:

(i) **Collect background information about the entity** – Collect information about environmental policy and goals of the organization, relevant environmental laws, regulations and standards governing the entity, persons responsible for carrying environmental duties, environmental budget, significant environmental matters like, material costs, risk areas, etc.

(ii) **Define objectives of audit** – What are the goals of the environmental audit?

(iii) **Define scope** –

<table>
<thead>
<tr>
<th>What parts of a facility (operations) will be audited?</th>
</tr>
</thead>
<tbody>
<tr>
<td>What programmes will be audited?</td>
</tr>
<tr>
<td>How far back will the audit examine?</td>
</tr>
</tbody>
</table>
(iv) **Choose audit criteria** – Against what will the facility be audited (e.g., for regulatory compliance audits, against what regulations or standards will the facility be audited)?

(v) **Select the audit team members** – The audit team leader selects team members based on appropriate knowledge and experience. The team both. If internal staff is going to be involved, they should be chosen in a proper way so as to avoid conflict of interest. The facility environmental manager, for example, should not be on the audit team.

(vi) **Develop audit plan and protocols** – Protocols are written guides for the auditors that outline the activities to be undertaken in conducting a review of a given topic area during the environmental audit. They often contain detailed information about audit criteria, such as, applicable regulations. Computers are often used in creating audit protocols and in locating and sharing information between team members during the audit (e.g., regulatory databases are often utilized in creating audit protocols).

(vii) **Inform the facility** – Arrangements for on-site activities need to be made.

(viii) **Desktop review.**

### 5.2 On-site or Field Audit (Stage 2)

The following are steps involved in on-site or field audit:

(i) **Opening conference** – Communicate the objectives and methods of the audit of key facility personnel and schedule necessary meetings and interviews.

(ii) **Facility tour** – Identify areas of concern for more detailed inspection, get a feel for the site and modify the audit schedule accordingly.

(iii) **Site/ facility inspection** – Established protocols should guide the inspection. The team may also wish to inspect areas of concern or interest that they have been identified in the facility tour. It may not be possible to inspect the entire facility (comprehensive inspection), therefore, sampling techniques may be an important part of determining the parts of a site to be inspected.

(iv) **Evidence** – Collect sufficient, appropriate and reliable audit evidences to check the activities, performance impacts and reports.

(v) **Records/ document review** – The audit protocols should give instructions as to the types of records to request as well as what to look for when examining the documents.

(vi) **Staff interviews** – Interviews with key informants will yield the least reliable information, due to the fallibility of human memory, but are important in the identification of potential problems and in collecting information about facility operations.

(vii) **Initial review of findings** – Findings are the result of the evaluation of evidence collected against audit criteria. It is important at this stage to review where the facility does not meet the audit criteria.

(viii) **Closing/ exit conference** – This is a chance for auditees to identify misunderstandings and to be introduced to the findings of the audit team.
5.3 Post – Audit (Stage 3)

Steps involved in post – audit are as follows:

(i) Final evaluation of findings: Findings must be backed by evidence. It is important to note areas of deficiency that were present during the previous audit, but are not yet corrected. Often finding are labeled as major or minor depending on the level and types of risks posed and speed with which the audit team feels they should be addressed.

(ii) Draft preliminary audit report

(iii) Get approval of the management

(iv) Hold exit conference

(v) Discuss recommendations, if any

(vi) Prepare and submit final report.

5.4 Follow up or Review Stage (Stage 4)

This is also called corrective action follow-up phase. While not technically part of the audit, the audit manager or team leader may be involved in developing a corrective action plan for addressing audit findings with the facility and reporting to senior management as to the progress of this plan.

<table>
<thead>
<tr>
<th>Stage 1: Pre-audit or Planning Stage</th>
<th>Stage 2: On-site or Field Audit:</th>
<th>Stage 3: Post – Audit:</th>
<th>Stage 4: Follow up or Review Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Collect Background Information</td>
<td>Opening conference</td>
<td>Final evaluation of findings</td>
<td>Verify the actions taken on audit findings or recommendations</td>
</tr>
<tr>
<td>Define Objectives</td>
<td>Identify areas of concern</td>
<td>Submit preliminary report</td>
<td></td>
</tr>
<tr>
<td>Define Scope</td>
<td>Site/facility inspection</td>
<td>Get approval of management</td>
<td></td>
</tr>
<tr>
<td>Select audit criteria</td>
<td>Records/document review</td>
<td>Hold exit conference</td>
<td></td>
</tr>
<tr>
<td>Select audit team members</td>
<td>Staff interviews</td>
<td>Submit final report</td>
<td></td>
</tr>
<tr>
<td>Develop audit plan or use protocol</td>
<td>Initial review of findings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inform the facility</td>
<td>Closing/exit conference</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Review the background information</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

© The Institute of Chartered Accountants of India
6. TOOLS AND TECHNIQUES USED IN ENVIRONMENTAL AUDITING

Some of the tools which can be used in environmental audits are:

(i) **Checklists** – Checklists are very useful tools used to ensure that different tasks or topics are included during the audit. They are very useful in specialized cases where a complex range of issues and questions need to be asked to ensure that nothing is missed.

(ii) **Questionnaires** – Audit protocols or audit questionnaires provide the basis and structuring for most audits. They are based upon checklist questionnaires but are more complex and include more detail and sometimes logistical information and data relating to the audit and the site being audited.

(iii) **Questioning** – Questioning is one of the most crucial aspects of auditing yet from a training and awareness point of view, it is often given the least attention. The purpose is information gathering in nature and not an interrogation. The questioner must, therefore, be sensitive to the perspective of the auditee and avoid making the questions accusatory, judgmental or aggressive.

(iv) **Observation** – Observation is a vital component of an auditing exercise. Observation is a disciplined activity which must be carried out in a very deliberate and controlled manner. The idea of looking at something twice is important because it is part of the process that checks that the observation is accurately noted, analyzed and recorded.

(v) **Photographs** – These are a very valuable aid in the audit process. However, in order to use them, a number of important practical points must be borne in mind. The most important one is formal approval before using this technique.

(vi) **Research** – It is useful to try and undertake some background research and investigation into the site or company to be audited. Familiarization with the operations, products, raw materials reports, press material and newspaper articles etc. all provides useful background information to supplement questioning sessions and help understand the operational processes.

7. ENVIRONMENTAL AUDIT REPORT

The end product of environmental audit is environmental audit report (EA Report) which contains findings or results of environmental audit and recommendations for improvement, if any (mainly required in environmental performance audit where objective is to improve performance of the organization). EA report should be concise and informative with information displayed in a format that is easy to interpret and understand. The environmental auditor must ensure that EA report should provide an accurate record of soundly based observations and of logical deductions. The report must be signed by environmental auditor.
The Audit report should be complete, precise, accurate and balanced. It should contain constructive and precise recommendations. It must be persuasive and instrumental in inspiring the managements of entities to take corrective actions. The violations and omissions should also be effectively mentioned in the report. Last but not the least, the contents of green audit report should be easy to understand and free from vagueness or ambiguity, include information which is supported by complete and relevant audit evidence and be independent, objective fair and constructive.

Contents of Report: It is to be noted that length and detail of environmental audit report may vary according to nature and type of organization audited and also on the basis of scope and object of audit. However, usually it is expected that the report should include following contents:

I Executive summary

II. Table of contents
   (i) Background:
       - nature and type of auditee organization, main business, facility description, EMS, etc.
   (ii) Audit objective:
       - to review compliance status of the organization, to check reporting of non-compliance or to verify the mechanisms for rectifying non-compliance.
   (iii) Audit scope: whether it is initial audit, audit of only one site, facility or process or audit of whole organization, etc.
   (v) Audit team
   (vi) Audit schedule
   (vii) Audit methodology:
       - Document review
       - Checklist
       - Interviews, etc.
   (viii) Audit findings:
       - Compliance status: compliance with environmental laws, specific regulation, certification requirement or company’s own environmental policy.
       - Violation information: e.g. failure to have required clearance, permit or approval, failure to have required plan or failure to report to authorities.
Mention the relevant law or regulation to which the violation relates like, air, water or hazardous waste Acts.

- Significant consequences of non-compliance. e.g., penalty

- Areas where non-compliance was found and corrected during audit period and areas where it is yet to be corrected.

(ii) Audit conclusions and recommendations

- If audit findings indicate commendable level of compliance and no non-compliance was identified, still some opportunities for improvement can be identified and listed.
- If non-compliance was found, recommendations can be made for developing some mechanism so that in future, it is not repeated. Indicate the time until the correction is to be completed and person responsible for making corrections.

(x) Annexes

- Environment policy and action plan of organization
- List of applicable laws and regulations
- Checklists

(xi) Signature of auditor with date and place

8. EMERGING OPPORTUNITIES FOR CHARTERED ACCOUNTANTS IN ENVIRONMENT AUDIT

CA’s Role in Compliance and Certification Audits: Compliance audits are conducted to verify an entity’s compliance with environmental laws, regulations, standards, industry guidelines or company’s own policy. It is felt that CAs can very efficiently conduct compliance audits if they gain knowledge of relevant environmental laws and regulations. They can also conduct certification audits. Such arguments, generally, centre on the requirements outlined in ISO 14012 Guidelines for environmental auditing issued in 1996. CAs already have first set of required skills. After obtaining knowledge about environmental laws, EMS and relevant terms, they can very efficiently conduct environmental audits, particularly certifications audits. These audits may include monitoring of environmental management system of the unit, checking the status of consent orders, compliance of consent orders, water cess, other legal requirements, industrial data collection regarding product process, electric consumption, water consumption, raw materials and energy balance, etc.

In the same way, CAs can play important role in non-financial auditing or carbon audits.

CA and Environmental Information Audit: The main role of financial auditor is to express opinion on truth and fairness of assertions made in financial statements. This role can be very well extended to include environmental information audit where all types of environmental information reported by a concern through various mediums is verified with the help of all available evidences.
What is an environmental audit?

A systematic, objective, and documented evaluation of the impact of your business activities on the environment.

Why do so many companies are using the environmental audit as a management tool?

To prepare themselves for:
- New and tougher legislation
- Increasing corporate and personal liability
- Rising energy and materials costs
- Rapidly rising waste disposal costs
- Competitive pressure as other companies clean up their act
- Growing public pressure

What does an audit involve?

A rigorous environmental audit will do more than simply ensure legislative compliance; it will aim to identify the Best Practicable Environmental Option (BPEO) for your company. A good audit will help you run a tighter, more efficient company.

What can an audit do for you?

Ensure that your company is staying within the bounds of the law

Cut effluent and waste disposal costs

Reduce material and energy bills

Improve your corporate image

Assist in formulation of an environmental policy.

Who should carry out the audit?

If you have relevant expertise in-house, set up an internal audit team or you may wish to bring in external audit team.

And after the initial audit?

Define a set of corporate objectives based on the audit results and set them out in a formal environmental policy.

Evaluating your operational practices to determine whether they can be made more efficient in terms of resource use and waste production, or altered to minimize risk of pollution.

Examine the way in which your company deals with the waste it produces to see if more effective waste management options could be deployed.

Taking a good look at the material and energy resources your company uses to see whether more environmentally sound alternatives could be substituted.

Developing contingency plans for environmental mishaps

Like a financial audit, an environmental audit is not a one-off event. Regular monitoring will be necessary to check that your company is moving satisfactorily towards its objectives.

Incorporate an environmental component into both your training programme and communication strategy.