

PAPER – 6 : AUDITING AND ASSURANCE

Question No.1 is compulsory.

Attempt any **four** questions from the remaining **five** questions.

Question 1

Examine with reasons whether the following statements are correct or incorrect. (Answer any seven out of eight)

- (a) *Even if law or regulation prescribes sufficient details of the terms of the audit engagement the auditor should record them in a written agreement.*
- (b) *It is not necessary for the auditor to periodically review the audit programme.*
- (c) *Dividends are recognized in the statement of profit and loss only when the amount of dividend can be measured reliably.*
- (d) *Every LLP is required to submit Statement of Account and Solvency in Form 8, which shall be filed within a period of sixty days from the end of three months of the financial year to which the Statement of Account and Solvency relates.*
- (e) *Classification as NPA should be based on the availability of security and asset classification would be facility wise and not borrower wise.*
- (f) *The audit plan is more detailed than the overall audit strategy.*
- (g) *Risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates.*
- (h) *External confirmation procedures are restricted to the items of addressing assertions associated with account balances & their elements only.* **(2 x 7 = 14 Marks)**

Answer

- (a) **Incorrect:** If law or regulation prescribes in sufficient detail the terms of the audit engagement, the auditor need not record them in a written agreement, except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities.
- (b) **Incorrect:** There should be periodic review of the audit programme to assess whether the same continues to be adequate for obtaining requisite knowledge and evidence about the transactions. Unless this is done, any change in the business policy of the client may not be adequately known, and consequently, audit work may be carried on, on the basis of an obsolete programme and for this negligence, the whole audit may be held as negligently conducted and the auditor may have to face legal consequences.
- (c) **Incorrect:** Dividends are recognised in the statement of profit and loss only when:
 - (i) the entity's right to receive payment of the dividend is established;

- (ii) it is probable that the economic benefits associated with the dividend will flow to the entity; and
- (iii) the amount of the dividend can be measured reliably.
- (d) **Incorrect:** Every LLP is required to submit Statement of Account and Solvency in Form 8 which shall be filed within a period of thirty days from the end of six months of the financial year to which the Statement of Account and Solvency relates.
- (e) **Incorrect:** Classification as NPA should be based on the record of recovery. Availability of security or net worth of borrower/guarantor is not to be taken into account for purpose of treating an advance as NPA or otherwise.
- Asset classification would be borrower-wise and not facility-wise. All facilities including investments in securities would be termed as NPA.
- (f) **Correct:** The audit plan is more detailed than the overall audit strategy that includes the nature, timing and extent of audit procedures to be performed by engagement team members. Once the overall audit strategy has been established, an audit plan can be developed to achieve the audit objectives through the efficient use of the auditor's resources.
- (g) **Correct:** Risks of material misstatement may be greater for significant judgmental matters that require the development of accounting estimates, arising from matters such as the following:
- ◆ Accounting principles for accounting estimates or revenue recognition may be subject to differing interpretation.
 - ◆ Required judgment may be subjective or complex, or require assumptions about the effects of future events, for example, judgment about fair value.
- (h) **Incorrect:** External confirmation procedures frequently are relevant when addressing assertions associated with certain account balances and their elements. However, external confirmation need not be restricted to account balances only.

Question 2

- (a) *Describe the guiding principles which the auditor should take into account which serves as the safeguards to eliminate the threats to independence.* **(4 Marks)**
- (b) *With Ref. to SA 320 "Materiality in planning and performing an audit" Indicate the factors which may effect the identification of an appropriate benchmark while determining materiality for the financial statements as a whole.* **(4 Marks)**
- (c) *It is imperative for the auditor to project misstatements for the population while performing audit procedures through sampling. Comment.* **(3 Marks)**
- (d) *With respect to SA 520 "Analytical procedures", explain the following factors to be considered by the auditor for substantive audit procedures.*

(i) Account type (ii) Predictability (iii) Nature of Assertion.

(3 Marks)

Answer

- (a) The Chartered Accountant has a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to eliminate the threats.

The following are the guiding principles in this regard: -

1. For the public to have confidence in the quality of audit, it is essential that auditors should always be and appears to be independent of the entities that they are auditing.
 2. In the case of audit, the key fundamental principles are integrity, objectivity and professional skepticism, which necessarily require the auditor to be independent.
 3. Before taking on any work, an auditor must conscientiously consider whether it involves threats to his independence. When such threats exist, the auditor should either desist from the task or put in place safeguards that eliminate them.
 4. If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.
- (b) Determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:
- ◆ The elements of the financial statements (Example - Assets, liabilities, equity, revenue, expenses);
 - ◆ Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused (Example - For the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets)
 - ◆ The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates;
 - ◆ The entity's ownership structure and the way it is financed and (Example - If an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings;)
 - ◆ The relative volatility of the benchmark.
- (c) (i) The auditor is required to project misstatements for the population to obtain a broad view of the scale of misstatement but this projection may not be sufficient to determine an amount to be recorded.
- (ii) When a misstatement has been established as an anomaly, it may be excluded when projecting misstatements to the population. However, the effect of any such

misstatement, if uncorrected, still needs to be considered in addition to the projection of the non-anomalous misstatements.

- (iii) For tests of details, the auditor shall project misstatements found in the sample to the population whereas for tests of controls, no explicit projection of deviations is necessary since the sample deviation rate is also the projected deviation rate for the population as a whole.
- (d) The auditor should consider the following factors for Substantive Audit Procedures:

Account Type – Substantive analytical procedures are more useful for certain types of accounts than for others. Income statement accounts tend to be more predictable because they reflect accumulated transactions over a period, whereas balance sheet accounts represent the net effect of transactions at a point in time or are subject to greater management judgment.

Predictability – Substantive analytical procedures are more appropriate when an account balance or relationships between items of data are predictable (e.g., between sales and cost of sales or between trade receivables and cash receipts). A predictable relationship is one that may reasonably be expected to exist and continue over time.

Nature of Assertion – Substantive analytical procedures may be more effective in providing evidence for some assertions (e.g., completeness or valuation) than for others (e.g., rights and obligations). Predictive analytical procedures using data analytics can be used to address completeness, valuation/ measurement and occurrence.

Question 3

- (a) *The auditor shall obtain an understanding of major activities that the entity uses to monitor internal control over financial reporting. Discuss "Monitoring of control" as a component of Internal control.* **(4 Marks)**
- (b) *While it is true that companies can benefit immensely from the use of data analysis in terms of increased profitability, better customer service, etc., analyse various functions that can be performed even by the auditor also using Data Analytics tools and techniques in the audit process to obtain good results.* **(4 Marks)**
- (c) *What factors are to be considered by an auditor while making control risk assessments?* **(3 Marks)**
- (d) *Analyse how risks in the IT system if not mitigated could have an impact on the audit.* **(3 Marks)**

Answer

(a) **Monitoring of Controls: Component of Internal Control**

The auditor shall obtain an understanding of the major activities that the entity uses to monitor internal control over financial reporting.

Monitoring of controls Defined: Monitoring of controls is a process to assess the effective ness of internal control performance over time.

- (i) **Helps in assessing the effectiveness of controls on a timely basis:** It involves assessing the effectiveness of controls on a timely basis and taking necessary remedial actions.
 - (ii) **Management accomplishes through ongoing activities, separate evaluations etc.:** Management accomplishes monitoring of controls through ongoing activities, separate evaluations, or a combination of the two. Ongoing monitoring activities are often built into the normal recurring activities of an entity and include regular management and supervisory activities.
 - (iii) **Management’s monitoring activities include:** Management’s monitoring activities may include using information from communications from external parties such as customer complaints and regulator comments that may indicate problems or highlight areas in need of improvement.
 - (iv) **In case of Small Entities:** Management’s monitoring of control is often accomplished by management’s or the owner-manager’s close involvement in operations. This involvement often will identify significant variances from expectations and inaccuracies in financial data leading to remedial action to the control.
- (b) In today’s digital age when companies rely on more and more on IT systems and networks to operate business, the amount of data and information that exists in these systems is enormous. A famous businessman recently said, “Data is the new Oil”.

The combination of processes, tools and techniques that are used to tap vast amounts of electronic data to obtain meaningful information is called data analytics. While it is true that companies can benefit immensely from the use of data analytics in terms of increased profitability, better customer service, gaining competitive advantage, more efficient operations, etc., even auditors can make use of similar tools and techniques in the audit process and obtain good results. The tools and techniques that auditors use in applying the principles of data analytics are known as Computer Assisted Auditing Techniques or CAATs in short.

Data analytics can be used in testing of electronic records and data residing in IT systems using spreadsheets and specialised audit tools viz., IDEA and ACL to perform the following:

- ◆ Check completeness of data and population that is used in either test of controls or substantive audit tests. Selection of audit samples – random sampling, systematic sampling.
- ◆ Re-computation of balances – reconstruction of trial balance from transaction data. Re performance of mathematical calculations – depreciation, bank interest calculation.

- ◆ Analysis of journal entries as required by SA240, Fraud investigation and Evaluating impact of control deficiencies.
- (c) Auditor assesses control risk as Rely or Not rely on Controls. When making control risk assessments, the factors an auditor would consider are:
- ◆ The control environment's influence over internal control. A control environment that supports the prevention, detection and correction of material misstatements allows greater confidence in the reliability of internal control and audit evidence generated within the entity.
 - ◆ Evaluations of the related IT processes that support application and IT-dependent manual controls.
 - ◆ Our testing approach over SCOTs and disclosure processes (i.e., controls reliance or substantive only strategy).
 - ◆ The expectation of the operating effectiveness of controls based on the understanding.
- (d) When risks in IT systems are not mitigated, the audit impact could be as follows:
- (i) First, we may not be able to rely on the reports, data obtained from systems where such risk exist. This means all forms of data, information or reports that we obtains from system for the purpose of audit has to be thoroughly tested and corroborated for completeness and accuracy.
 - (ii) Second, we will not be able to rely on automated controls, calculations and accounting procedures that are built into the application. Additional audit work may be required in this case.
 - (iii) Third, due to the regulatory requirement of auditors to report on internal financial controls of a company, the audit report also may have to be modified in some instances.

Question 4

- (a) *ABC limited appointed XYZ & Company, Chartered Accountants, as a Statutory Auditor of the Company for the year 2019-20. CA X, partner of XYZ & Company, was looking after the audit of other income of the company which consists of interest income on fixed deposits. As a Statutory Auditor how would CA X verify interest income on fixed deposits for the year 2019-20?* **(4 Marks)**
- (b) *While conducting the audit of Amrit Ltd. the auditor A of ABC and Associates, Chartered Accountants observes that there are a large number of trade receivables standing in the books of account as on 31st March. The auditor wanted to send confirmation request to a few large trade receivables but the management refused the auditor to send confirmation request. How would the auditor proceed?* **(4 Marks)**

- (c) *The auditor's requirement to report under clause (X) of paragraph 3 of the Companies (Auditor's Report) Order, 2016 is restricted to frauds noticed or reported during the year. Explain what auditors may consider for reporting under this clause? (3 Marks)*
- (d) *Discuss the audit procedures generally required to be undertaken by the auditor while auditing Goods sent out on Sale or Return Basis. (3 Marks)*

Answer

- (a) CA X, partner of XYZ & Company, would carry out the following audit procedure for verifying interest income on fixed deposits of ABC Limited:
1. Obtain a listing of fixed deposits opened during the period under audit along with the applicable interest rate and the number of days for which the deposit was outstanding during the period. Verify the arithmetical accuracy of the interest calculation made by the entity by recomputing i.e. multiplying the deposit amount with the applicable rate and number of days during the period under audit.
 2. For deposits still outstanding as at the period- end, trace the same to the direct confirmations obtained from the respective bank/ financial institution.
 3. Obtain a confirmation of interest income from the bank and verify that the interest income as per bank reconciles to the calculation shared by the entity.
 4. Also, obtain a copy of Form 26AS (TDS withholding by the bank/ financial institution) and reconcile the interest reflected therein to the calculation shared by client.
- (b) In the given case of Amrit Ltd, the auditor wanted to send confirmation request to a few large trade receivables but the management did not want the auditor to send confirmation request.

If the management refuses to allow the auditor to send a confirmation request , the auditor shall-

1. Inquire as to management's reasons for the refusal and seek audit evidence as to their validity and reasonableness.
2. Evaluate the implications of management's refusal on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures; and
3. Perform alternative audit procedures designed to obtain relevant and reliable evidences.
4. If the auditor concludes that management's refusal to allow the auditor to send a confirmation request is unreasonable, or the auditor is unable to obtain relevant and reliable audit evidences from alternative audit procedures, the auditor shall communicate with those charged with governance in accordance with SA 260.

The auditor shall also determine the implication for the audit and the auditor's opinion in accordance with SA 705.

- (c) The auditor is required to report under clause (x) of paragraph 3 of Companies (Auditor's Report) Order, 2016,

Where the auditor notices that any fraud by the company or on the company by its officers or employees has been noticed by or reported during the year, the auditor should, apart from reporting the existence of fraud, also required to report, the nature of fraud and amount involved. For reporting under this clause, the auditor may consider the following:

- (i) This clause requires all frauds noticed or reported during the year shall be reported indicating the nature and amount involved. As specified, the fraud by the company or on the company by its officers or employees are only covered.
 - (ii) Of the frauds covered under section 143(12) of the Act, only noticed frauds shall be included here and not the suspected frauds.
 - (iii) While reporting under this clause with regard to the nature and the amount involved of the frauds notice do reported, the auditor may also consider the principles of materiality outlined in Standards on Auditing.
- (d) The audit procedure generally required to be undertaken by the auditor while auditing Goods sent out on Sale or Return Basis is as under:
- (i) Check whether a separate memoranda record of goods sent out on sale or return basis is maintained. The party accounts are debited only after the goods have been sold and the sales account is credited.
 - (ii) Verify that price of such goods is unloaded from the sales account and the trade receivables record. Check the memoranda record to confirm that on the receipt of acceptance from each party, his account has been debited and the sales account correspondingly credited.
 - (iii) Ensure that the goods in respect of which the period of approval has expired at the end of the year, have either been received back or customers' accounts have been debited.
 - (iv) Confirm that the inventory of goods sent out on approval, the period of approval in respect of which had not expired till the end of the year lying with the party, has been included in the closing inventory.

Question 5

- (a) *As an auditor of PQR Ltd., you came across a misstatement resulting from fraud or suspected fraud which brings into question your ability to continue performing the audit. Explain the courses of actions available to you. (4 Marks)*
- (b) *Clue Ltd. is a Public unlisted company having paid-up share capital of ` 9 crores and public borrowings from the financial institutions of ` 51 crores. They appointed M/s Pray and Co., A Chartered Accountant firm as the statutory auditor in its annual general meeting for 11 years.*

- (i) *Is the manner of rotation of auditor applicable in case of Clue Ltd.?*
- (ii) *Whether the appointment of M/s Pray and Co. is valid?* **(4 Marks)**
- (c) *How would an auditor determine Key Audit Matters as per SA - 701, "Communicating Key Audit Matters in the Independent Auditor's Report"?* **(3 Marks)**
- (d) *RJ Limited is in the business of trading of cycles having Head Office at Delhi and branch at Mumbai. Statutory audit of Head Office was to be done by CA D and statutory audit of branch at Mumbai was to be done by CA M. During the course of audit by CA D at head office, CA D Wanted to visit branch at Mumbai and verify the inventory records at Mumbai. The management of RJ Limited did not allow CA D to visit Mumbai office and verify the inventory records as the branch audit of Mumbai was already being undertaken by another CA M.*
- In the above situation, discuss the rights available with CA D in terms of the Companies Act, 2013.* **(3 Marks)**

Answer

- (a) In the given case of PQR Ltd, the auditor came across a misstatement resulting from fraud or suspected fraud that brought into question the auditor's ability to continue performing the audit. In such a situation, the auditor shall :
- (a) Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities;
- (b) Consider whether it is appropriate to withdraw from the engagement, where withdrawal is possible under applicable law or regulation; and
- (c) If the auditor withdraws:
- (i) Discuss with the appropriate level of management and those charged with governance the auditor's withdrawal from the engagement and the reasons for the withdrawal.
- (ii) Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities, the auditor's withdrawal from the engagement and the reasons for the withdrawal.
- (b) (i) As per rules prescribed in Companies (Audit and Auditors) Rules, 2014, for applicability of section 139(2) the class of companies shall mean the following classes of companies excluding one person companies and small companies-
- (i) all unlisted public companies having paid up share capital of rupees ten crore or more;
- (ii) all private limited companies having paid up share capital of rupees fifty crore or more;

- (iii) all companies having paid up share capital of below threshold limit mentioned above, but having public borrowings from financial institutions, banks or public deposits of rupees fifty crores or more.

In the given case, Clue Ltd is an Unlisted Public company, any having paid up share capital of ₹ 9 crores and public borrowings from financial institutions of ₹ 51 crores. So, applying the above provisions to the given problem, although paid up share capital of Clue Ltd is below threshold limit of ₹ 10 crores yet the Company is having public borrowings from financial institutions worth ₹ 51 crores i.e above ₹ 50 crores.

Therefore, manner of rotation of auditors is applicable in case of Clue Ltd.

- (ii) Clue Ltd., an unlisted public company is covered by the rotational provisions, appointed M/s Pray and Co., a Chartered Accountant firm, as the statutory auditor in its AGM for 11 years. Here, the appointment of M/s Pray & Co. is not valid as the appointment can be made only for one term of five consecutive years and then another one more term of five consecutive years. It can't be appointed for two terms in one AGM only. Further, a cooling period of five years from the completion of term is required i.e. the firm can't be re-appointed for further 5 years after completion of two terms of five consecutive years.

Keeping in view above, the appointment of M/s Pray and Co. is not valid.

- (c) The auditor shall determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit.

In making this determination, the auditor shall take into account the following:

- (a) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA315.
- (b) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- (c) The effect on the audit of significant events or transactions that occurred during the period.

The auditor shall determine which of the matters determined in accordance with above stated para were of most significance in the audit of the financial statements of the current period and therefore are the key audit matters.

- (d) Section 143(1) of the Act provides that the auditor of a company, at all times, shall have a right of access to the books of account and vouchers of the company, whether kept at the registered office of the company or at any other place and he is entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor.

The right of access is not limited to those books and records maintained at the registered or head office so that in the case of a company with branches, the right also extends to the branch records, if the auditor considers it necessary to have access thereto as per Section 143(8).

In the given case where CA D was appointed as Statutory Auditor of Head office of RJ Ltd and CA M was appointed to conduct Statutory Audit of Branch office of RJ Ltd., CA D wanted to visit Mumbai Branch to verify the inventory records at Mumbai but management of RJ Ltd did not allow CA D to verify the inventory records at its Mumbai Branch on the ground that branch audit was already being undertaken by another CA M.

Keeping in view the above provisions of the Companies Act and facts of the case, it can be concluded that CA D has a right to visit the branch for verifying inventory records at Mumbai even if the branch accounts are audited by another auditor CA M, if he considers it necessary to do so for the performance of his duties as an auditor.

Question 6

- (a) *You are appointed as Statutory Auditor of DEF Bank Limited for the year 2019-20. As an Auditor how will you verify Provisions created by DEF Bank Limited?* **(4 Marks)**
- (b) (i) *You are appointed as an auditor of co-operative society. State the special features of the co-operative audit to be borne in mind by the auditor, concerning:*
- (1) *Audit classification of society.*
 - (2) *Discussion of draft audit report with the management committee.* **(4 Marks)**
- OR
- (ii) *The audit of receipts of government is not as old as audit of expenditure but with the rapid growth of public enterprises audit of receipts tax or non-tax has come to stay. Discuss audit of receipts with respect to Government Audit.*
- (c) *Explain the different types of revenue grants which local bodies may receive.* **(3 Marks)**
- (d) *What is the function of audit while examining various rules, regulations and orders with regard to Audit against Rules & Orders by C&AG?* **(3 Marks)**

Answer

- (a) For audit of Provisions, the auditor should ensure that the compliances for various regulatory requirements for provisioning as contained in the various circulars have been fulfilled. The auditor should obtain an understanding as to how the bank computes provision on standard assets and non-performing assets. It will primarily include checking the basis of classification of loans and receivables into standard, sub-standard, doubtful, loss and non-performing assets. The auditor may verify the loan classification on a sample basis.

The auditor should obtain the detailed break up of standard loans, non-performing loans and agree the outstanding balances with the general ledger. The auditor should obtain the tax provision computation from the bank's management and verify the nature of items debited and credited to profit and loss account to ascertain that the same are appropriately considered in the tax provision computation. The other provisions for expenses should be examined vis-à-vis the circumstances warranting the provisioning and the adequacy of the same by discussing and obtaining the explanations from the bank's management.

- (b) (i) (1) **Audit classification of society** - After a judgement of an overall performance of the society, the auditor has to award a class to the society. This judgement is to be based on the criteria specified by the Registrar. It may be noted here that if the management of the society is not satisfied about the award of audit class, it can make an appeal to the Registrar, and the Registrar may direct to review the audit classification. The auditor should be very careful, while making a decision about the class of society.
- (2) **Discussion of draft audit report with managing committee** – On conclusion of the audit, the auditor should ask the Secretary of the society to convene the managing committee meeting to discuss the audit draft report. The audit report should never be finalised without discussion with the managing committee. Minor irregularities may be got settled and rectified. Matters of policy should be discussed in detail.

Or

- (b) (ii) Government auditing in India as elsewhere was primarily expenditure- oriented. Gradually, audit of receipts-tax and non-tax was taken up.

The audit of receipts is neither all pervasive nor as old as audit of expenditure but has come to stay in some countries. Such an audit provides for checking;

- (i) whether all revenues or other debts due to government have been correctly assessed, realised and credited to government account by the designated authorities;
- (ii) whether adequate regulations and procedures have been framed by the department/agency concerned to secure an effective check on assessment, collection and proper allocation of cases;
- (iii) whether such regulations and procedures are actually being carried out;
- (iv) whether adequate checks are imposed to ensure the prompt detection and investigation of irregularities, double refunds, fraudulent or forged refund vouchers or other loss of revenue through fraud or wilful omission or negligence to levy or collect taxes or to issue refunds; and
- (v) review of systems and procedures to see that the internal procedures adequately secure correct and regular accounting of demands collection and

refunds and pursuant of dues up to final settlement and to suggest improvement. The basic principle of audit of receipts is that it is more important to look at the general than on the particular, though individual cases of assessment, demand, collection, refund, etc. Are important within the area of test check. A review of the judicial decisions taken by tax authorities is done to judge the effectiveness of the assessment procedure.

- (vi) The extent and quantum of audit required to be done under each category of audit are determined by the C&AG. These are neither negotiable nor questioned. The prescribed extent and quantum of audit are structured in accordance with the design of test check, random sampling, general review ,in-depth study of specified areas, etc .as may be warranted by the nature of transactions, its importance in the scheme of activities of a department and the totality of its transactions, the frequency of check and total plan of audit to be executed during a period.
 - (vii) Institutional mechanism provides for primary check by the auditor, test check by the supervisor and control and direction by the group leader. Planning, executing and reporting of work is directed and monitored at middle and top levels of the audit hierarchy. There are built –in arrangements within the C&AG to ensure that the work assigned to each employee is carried out as prescribed.
 - (viii) The audit is conducted both centrally where accounts and original vouchers are kept and locally where the drawing and disbursing functions are performed depending on the organisational and institutional arrangements obtaining.
- (c) Local bodies may receive different types of grants from the state administration as well. Broadly, the revenue grants are of three categories:
- (a) *General purpose grants*: These are primarily intended to substantially bridge the gap between the needs and resources of the local bodies.
 - (b) *Specific purpose grants*: These grants which are tied to the provision of certain services or performance of certain tasks.
 - (c) *Statutory and compensatory grants*: These grants, under various enactments, are given to local bodies as compensation on account of loss of any revenue on taking over a tax by state government from local government.
- (d) Audit against Rules & Orders – Audit against rules and orders aims to ensure that the expenditure conforms to the relevant provisions of the Constitution and of the laws and rules made there under. It also seeks to satisfy that the expenditure is in accordance with the financial rules, regulations and orders issued by a competent authority.

It is the function of the executive government to frame rules, regulations and orders, which are to be observed by its subordinate authorities. The job of audit is to see that these rules, regulations and orders are applied properly by the subordinate authorities. It is, however, not the function of audit to prescribe what such rules, regulations and orders shall be. But,

it is the function of audit to carry out examination of the various rules, regulations and orders issued by the executive authorities to see that:

- (a) they are not inconsistent with any provisions of the Constitution or any laws made there under;
- (b) they are consistent with the essential requirements of audit and accounts as determined by the C&AG;
- (c) they do not come in conflict with the orders of, or rules made by, any higher authority; and
- (d) in case they have not been separately approved by competent authority, the issuing authority possesses the necessary rule-making power.