



# Practical Intricacies in Internal Audit of Manufacturing Companies

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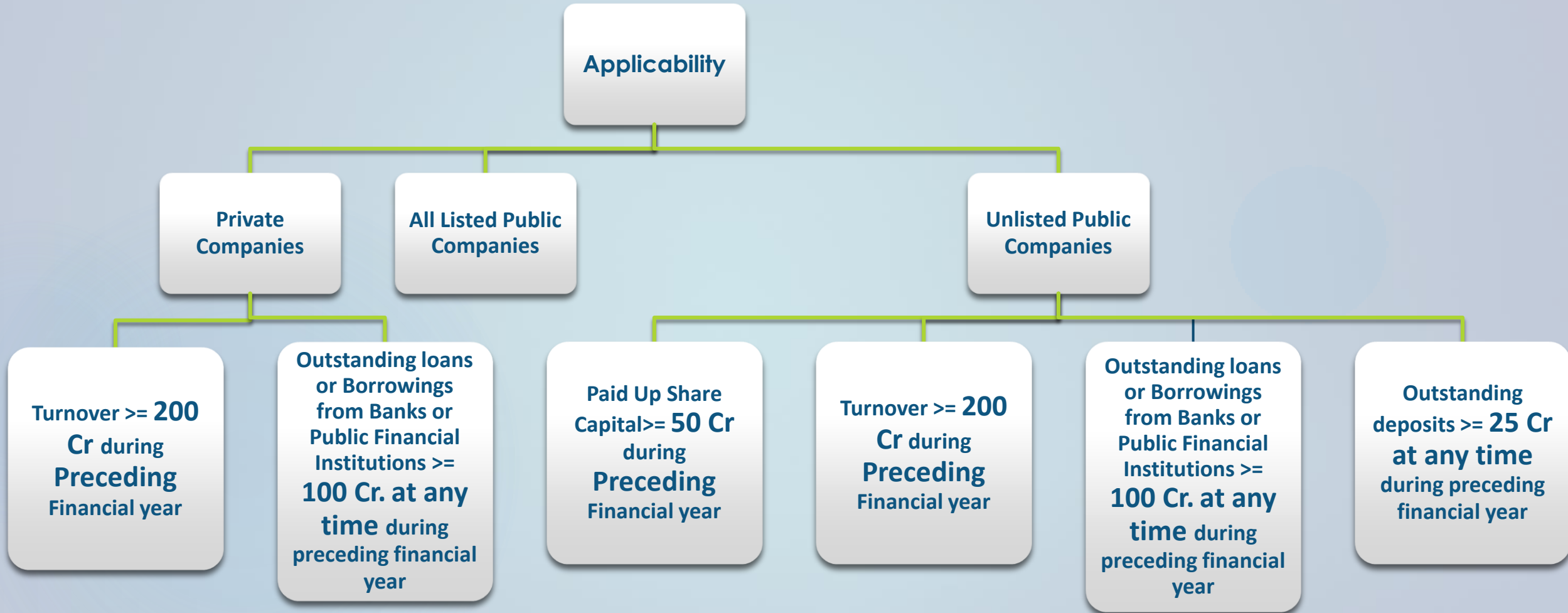
**CHARTERED ACCOUNTANTS**

# *What is Internal Audit*

Internal audit is –

- a. An **independent management function**, which involves
- b. A continuous and **critical appraisal** of the functioning of an entity with a view
- c. To suggest **improvements** thereto and **add value** to and strengthen the overall governance mechanism of the entity, including the entity's strategic risk management and internal control system.

# Internal Audit – Applicability – Sec 138 of Companies Act, 2013



# ***Internal Audit - Applicability of CARO, 2020***

Under Clause XIV of CARO, 2020 the statutory auditor needs to report in its report

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

## **Penalty for Non executing Internal Audit**

Company and every officer of the company who is in default or such other person shall be punishable with fine which may extend to ₹ 10,000/- and where the contravention is continuing one with a further fine which may extend to ₹ 1,000/- for every day after the first during which the contravention continues.

# *Commensurate With Size of Business – As per CARO, 2020*

The auditor needs to examine whether the internal audit system is commensurate with the size of the company and the nature of its business. In this regard, the auditor should evaluate the following:

- ▶ The size of the internal audit department
- ▶ Qualifications of the persons who undertake the internal audit work
- ▶ The audit committee of the company or the Board shall, in consultation with the internal auditor, formulate the scope, functioning, periodicity and methodology for conducting the internal audit.  
Technical assistance to the internal auditor
- ▶ There is an adequate follow-up system to ensure that the deficiencies pointed out are corrected and remedial action taken on the deficiencies reported upon.
- ▶ Examine the minutes of the meetings of the Board of Directors and audit committee
- ▶ The auditor would advise to make inquiries regarding the existence of internal audit system and to report the fact under this clause



# Role of Internal Auditor

compliance  
**Internal Audit**  
 risk  
 independent  
 add value  
 effective improve  
 efficient assurance  
 objective

# Internal Audit Reporting – Stake holders



# Difference Between Internal Audit vs Statutory Audit

Point	Internal Audit	Statutory Audit
1. Meaning	It refers to an ongoing audit function performed within an organization by a separate internal auditing Department.	It is an audit function performed by the independent body which is not a part of the organization
2. Appointment	By Management	By shareholder
3. Objective	To better understand the risks facing the business & asses whether it is meeting its strategical objective.	Ensure that P&L A/c and Balance Sheet of the organization shows true and fair view.
4. Period	Carried out continuously throughout the year	Carried out Periodically generally at the end of the accounting year
5. User of Report	Management	Shareholders, Bank, Government and any other external stake holders
6. Method	Internal audit is a complete audit. It is carried out in detail. The auditor checks each and every item and process of the accounts.	Generally, in Statutory audit the test checking system is adopted. It is a sampling audit
7. Internal Financial control	Express an opinion on the adequacy and operating effectiveness of the company's IFC	Auditor needs to report on its CARO, 2020 on adequacy of Internal Financial Control
8. Examination	Internal Auditor examines the operational efficiency of the organization.	External auditor examines the Accuracy and Validity of the Financial statements.
9. Status of Auditor	Internal auditor is employee of the company, thus , less independent.	External Auditor is an independent person



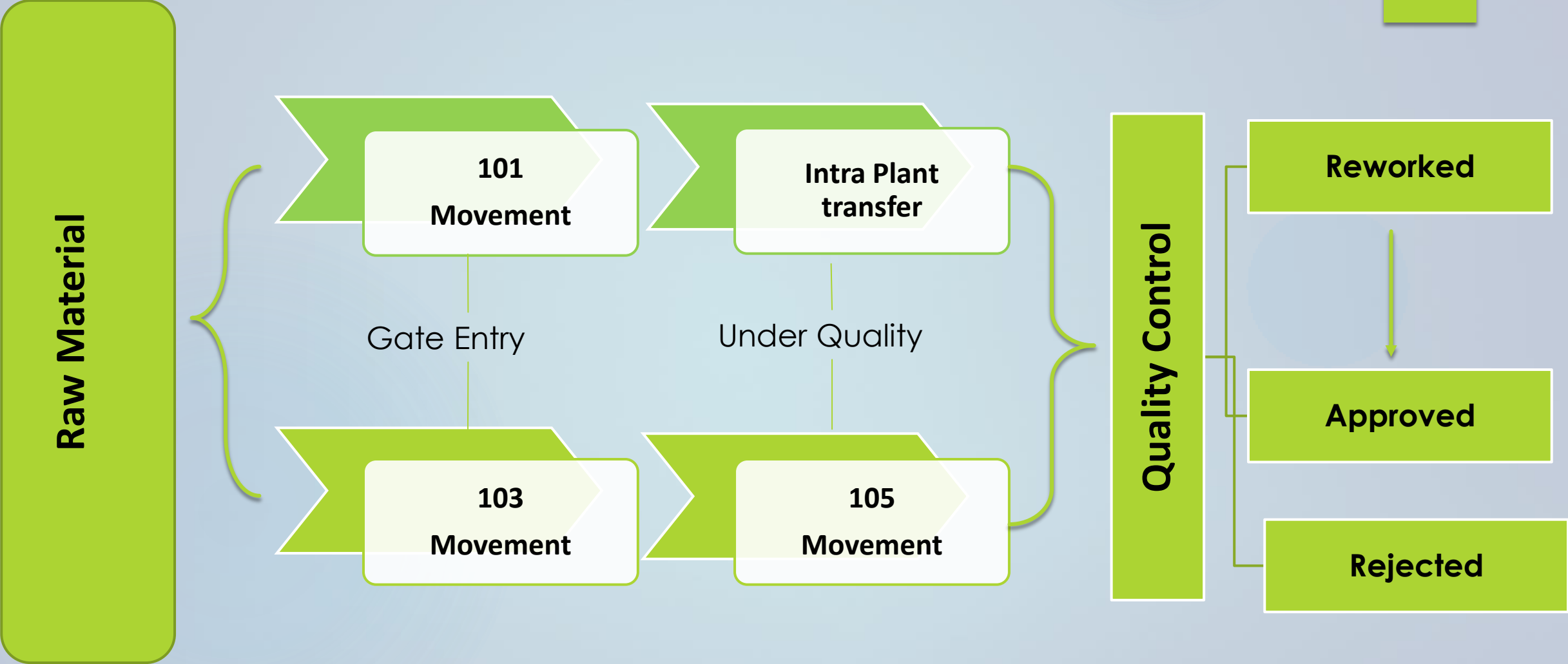
# Objectives of Internal Auditing



# *Objectives of Internal Auditing in Practical Scenario*

- Reduction in Production, operational Cost
- Identification of Income escaped
- Identification of fraud and unethical practices
- Increase in operational efficiencies
- Identification of Statutory non compliance
- Compliance of internal standard operating practices
- Tax Rationalization
- Identification of potential business or financial risks

# Raw Material Receipt Process in SAP



# MB 51 Extracts

Material Document	Plant	Material	Material Description	Movement Type	Batch	Order	Reservation	Base Unit of Measure	Quantity	Amount in LC	Storage Location	Movement Type Text	Co-Storage Item	Material Document Item	Posting Date	Time of Entry	Entry Date	Unit of Entry	Vendor	Purchase Order	Sales Order	Sales Order Item	User name	Qty in Un. of Entry
4904700285	1000	0804G040000SA00	RUBBER PIPE, ASSEMBLY	321	1GM00687		0	NOS	6,000	0.00	AS01	TF quality to unrest		2	13-04-2022	07:16:26	13-04-2022	NOS	20033	4810005108		0	CNQMEU01	6,000
4904700285	1000	0804G040000SA00	RUBBER PIPE, ASSEMBLY	321	1GM00687		0	NOS	-6,000	0.00	AS01	TF quality to unrest		1	13-04-2022	07:16:26	13-04-2022	NOS	20033	4810005108		0	CNQMEU01	-6,000
4904712848	1000	0804G040000SA00	RUBBER PIPE, ASSEMBLY	261	1GM00687	500000068950	1985589	NOS	-6,000	12,720.00	-MA01	GI for order		51	27-04-2022	16:44:05	27-04-2022	NOS				0	CNPPEU07	-6,000
5001762891	1000	0804G040000SA00	RUBBER PIPE, ASSEMBLY	101	1GM00687		0	NOS	6,000	12,720.00	AS01	GR goods receipt		1	12-04-2022	15:30:43	12-04-2022	NOS	20033	4810005108		0	CNMMEU07	6,000

# MB 51 Movements

Type	Movement Type Description
101	Goods Receipt For Purchase Order
102	Cancellation Or Reversal Of Movement Type 101
103	Goods Receipt For Purchase Order To Gr Blocked Stock
104	Blocked Stock Sending Back To Vendor
105	Release From The Gr Blocked Stock For The Purchase Order
261	Goods Issue For An Production Order
262	To Reverse The Material Document
501	Goods Receipt Without Purchase Order : Unrestricted-Use Stock
502	To Cancel 501 Document
541	Transfer Of Unrestricted-Use Stock To Subcontracting Stock
542	Trasfer From Subcontracting Stock To Unrestricted Stock
543	Consumption From Subcontracting Stock
544	Reversal Of 543 - Consumption Reversal At Vendor Place
551	Scrapping From Unrestricted-Use Stock
601	Goods Issue For Delivery
701	Inventory Difference In Unrestricted-Use Stock
702	Goods Issue Against Physical Inventory In Unrestricted.



***Internal Audit Point means ....***

**Internal Audit Point = Process Discrepancy + Solution**

## ***Qualities of Recommendation/Solution***

1. **Practical** - It should be Practical to implement in company
2. **Legal** - Recommendation should be adhered to laws and regulations. Spirit of law should not be defeated.
3. **Ethical** – It should be in line with the business and professional ethics.
4. **Effective** - Impact of recommendation should be Effective to strengthen internal controls of the company.
5. **Cost effective** - Recommendation should be such that the company should be able to execute and design at minimum cost.
6. **Precise** - it should be easy to read and understand, even to someone with little knowledge of the subject area.
7. **Understandable** – It should be understandable to non finance person from the committee or management as well.

# How to prepare the Audit Program ?

## Sales

Quantity

$$\text{Sales Quantity} * \text{Selling Price} = \text{Sales Value}$$

Rate

## Payroll

Man days  
Consumed

$$\text{Total Man-days} * \text{daily wage rate} = \text{Total payroll cost}$$

Per day  
rate

## Purchase

Quantity  
Inward

$$\text{Inward Quantity} * \text{Purchase Rate} = \text{Purchase Cost}$$

Purchase  
Price



# Key Audit Procedures

## Sales

1. Cost rationalization with sales
2. Comparing 601 report of SAP with Sales
3. Sales Pricing with BOM
4. Gross margin Analysis
5. Comparison of 601 with production (101)

## Purchase


1. Internal Benchmarking
2. Quotation comparison
3. Checking of rates as per Purchase order
4. Open Purchase order Analysis

## Treasury

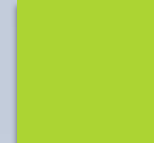
1. Opportunity cost of idle funds
2. Utilization of credit Period vs discount on prompt payment
3. Investment in mutual funds to mitigate the business risk

## Payroll

1. Salary breakup checking with master earnings
2. Employee composition as per business requirements
3. Comparison with Budgeted employee headcount
4. Increments , Gratuity & Bonus Analysis
5. Biometric attendance vs actual attendance



***Few Internal Audit Points  
appreciated by the Board***



# 1. Gross loss on sale in case of one spare part

## Observation

We obtained the list of FG codes and analysed the gross profits margins of all the FG items. Wherever the standard deviation was more, we checked the back up of pricing with the BOM appearing in the system.

In case of FG item 100066M0005 (Spare part item), the company is selling the product at a gross loss of 15%-20%. On further analysis, we observed that item no. K102028BH9900 – Throttle Valve is not being considered for the purpose of pricing.

We have been explained that this is a manual error and there is no reason for specifically excluding this item for the purpose of the pricing

We estimate a gross loss of at least **Rs. 7 lakhs** on the sale of this item for the period of Jan 15 to May 15

Root cause;  
Manual process for arriving at the pricing

## Recommendations

We suggest the company to compare the details considered for pricing for all the FG codes and compare it with the BOM appearing in the system.

This will ensure that the company does not lose money due to manual errors

## Management Comments

We have already started this process. This one item was exceptional and due to manual error.

**Responsibility:** Finance

**Date of implementation:** 1<sup>st</sup> April 2015

## 2. Same bank account number acceptance by SAP R3

### Observation

We observed that, for separate two separate Vendor codes in SAP, there can be same bank account number. Practically this will not happen that two different businesses has a same bank account number as bank does not accept the same.

According to us, this can be a loophole for the payment to vendors process.

During Understanding the process of Vendor development, we have been informed that creation of vendor in SAP and amendments in such vendor are done through senior finance manager only. No other employee has an authority to change the master details.

But, as part of vendor development, system should not allow to enter one bank account number twice in its database. It creates an inherent risk in vendor payment process.

### Root Cause

Acceptance of same bank account number for two different vendors

### Implications

Same bank account number can be entered for different vendors. We feel that the facility can be used in a incorrect way.

### Recommendations

We recommend to configure the SAP so that same bank account number will not be accepted for different vendor codes in the database.

### Management Comments

**We will escalate the matter to software consultant and get it resolved.**

**Responsibility : SAP Department**  
**Implementation Date: immediate**

### 3. Savings of GST charged over Package Food provided by Canteen Vendor

#### Observation

Company avails transport facilities for its employees for which it has contracted M/s Shree Sai Foods, Harayana based canteen service Provider. On review of the agreement and its subsequent amendment we observed the following -

**Double Taxation of GST on Package MRP Food:-**Contractor has agreed to provide Meal, Packed snacks and biscuits, Tea as per agreement. We observed that the contractor is also billing for MRP based products such as Biscuit and Namkeen on which GST 18% is charged to the company.

As per section 17(5)(b)(i) of CGST Act, GST paid on foods and beverages and outdoor catering not available to the company as input tax credit in the GST return. Hence, for the company GST on canteen Service is a cost.

This is amounting to tax on tax which has a cascading impact. Moreover, company can implement the tax structuring which would save reasonable amount of money.

#### Implication

The total expense for Namkeen and biscuits is 9 lakhs for the year approximately. As it is purchases at MRP price, the said price will be same for company also.

It is resulting in excess cost to company to the extent of 1.61 per year.

#### Recommendations

We recommend that -

Both the MRP products should be billed on the company name directly so that GST on MRP products **Rs. 1.61 lakhs** can be saved directly.

Also, company can avoid the cascading effect of GST.

#### Management Comments

**The audit point is accepted and well appreciated. We will implement on an urgent basis.**

**Responsibility:** HR department

**Date of implementation :** immediate

## 4. No co relation between crude oil prices and freight rates

### Observation

In the previous year, the crude oil prices nose-dived resulting in crash in the Baltic dry index ('BDI'). BDI provides an assessments of the price of moving materials by sea. Normally, the trends in freight rates coincide with the movement in the BDI.

We have observed that the sea freight rates paid by the company have remained constant throughout the year despite significant reduction in crude oil prices. Please refer Annexure II for comparison of freight cost incurred by the company vis. a vis. crude oil prices.

Key notings from the analysis are as under:

- Crude oil prices have fallen from **USD 109 per barrel to USD 48** per barrel.
- Shipping cost is more or less constant through out the year.

We have been explained that ENS and LSS charges have been levied additionally by the forwarders, however we are of the opinion that this does not explain the reason for no reduction in freight charges. The current macro indicators suggest that the crude oil will remain below USD 70 per barrel and the company stands a very good chance to reduce the freight costs

#### **Root cause:**

Freight rates are not monitored closely with global price trends

### Recommendations

We recommend that the Company should renegotiate the rates with the freight contractors on an urgent basis. We foresee a significant saving by carrying out this exercise.

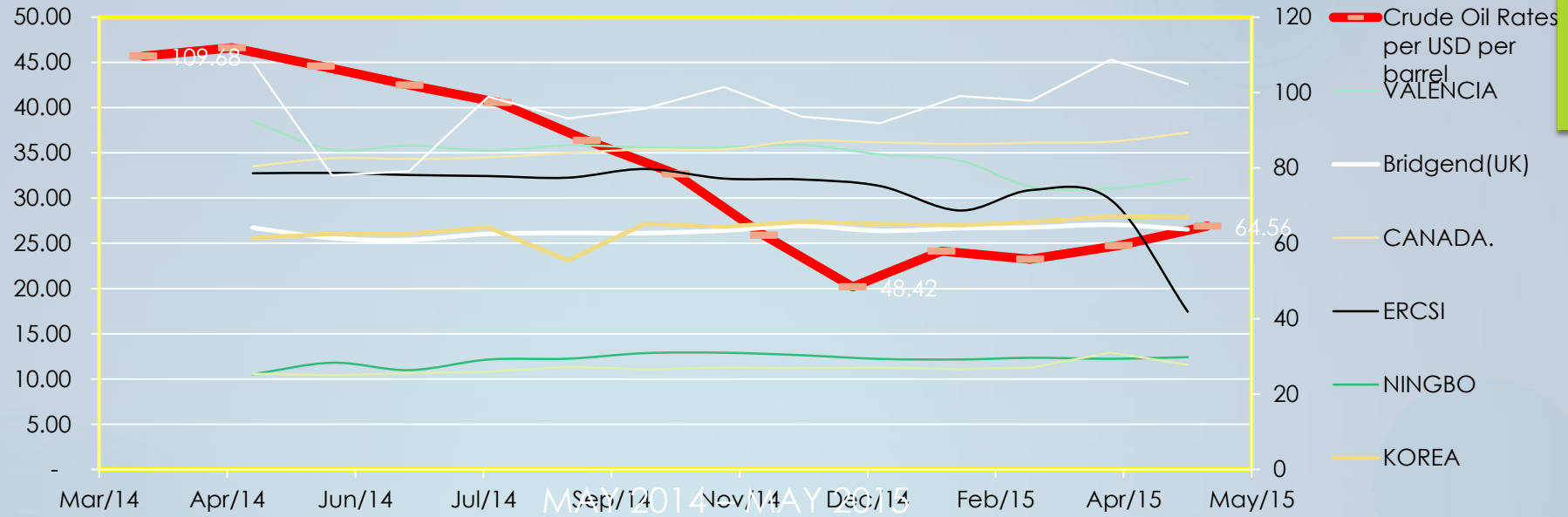
### Management Comments

**We explore the cost reduction opportunity and negotiate with the respective freight vendors**

**Responsibility: Sales department**

**Implementation Date: Immediate**

# Annexure 4A : Shipping rates vs. Crude oil



# Baltic Dry Index



## 5. Scope for Scrap rate negotiation

### Observation

We understand that, Company has scrap income of Rs. 1. 2 Crores for a year. We studied the scrap at which company is selling to the vendors.

To study the scrap rate offered by scrap vendor to the Company, we compared the those rates with the purchase rate is same scrap for manufacturer who used it for further manufacturing. The details are as follows -

<b>Brass Scrap Rate</b>	<b>– Rs. 167</b>
<b>Purchase rate for Manufacturer</b>	<b>– Rs. 346</b>
<b>Difference</b>	<b>-- Rs. 179</b>
<b>%</b>	<b>-- 51%</b>

We can easily observe that there is reasonably high average profit margin which scrap vendor is getting in the trading.

Even considering the fact that current scrap vendor is 2<sup>nd</sup>/3<sup>rd</sup> stage dealer in the scrap selling chain, there is a reasonable scope for rate negotiation with the vendor to the extent of 10-15%.

#### **Root Cause:**

Selling of scrap at a lower rate

### Implication

Scrap sales will be at lower prices which will result in loss of revenue.

### Recommendations

We recommend the Company to renegotiate the scrap sales prices for all types of material including brass and stainless steel which comprises major part of scrap at least to the extent of 10-15% of current prices which may result in additional revenue of **Rs. 50 - 60 lakhs**

### Management Comments

Suggestion accepted and well appreciated. We will do the scrap generating processes in foreign group company and purchase processed goods from them at a lower rate.

**Responsibility:** Store Department

**Date of implementation:**



## 6. Higher revenue share from Ford having potential decrease in demand

### Observation

Ford is one of the major customer of company for automobile part According to our research relating to Ford, they are facing challenges due to WAR and Covid, resulting in reduction in production from various parts of world also it seems that they are more focusing on electric vehicles instead of fuel based or hybrid vehicles. Currently company is having 29% of revenue share from Ford itself

**There are some indicators showing the potential to threat to upcoming demand from Ford.**

- i. Due to suspension of factories in US for reason of short availability of semiconductor chip sales in US is falls for 6-7 %
- ii. Ford's results presents a challenge to Chief Executives , who are trying to accelerate the company's pivot toward electric vehicles. Ford said it has around 2.7 lakhs orders for E-vehicles and expects to double electric vehicle production capacity to 600,000 vehicles a year by 2023.
- iii. Ford has stopped taking orders for the Galaxy and S-Max minivans, both built in Valencia, Spain, because of global microchip shortages

Things are not much different with General motors also, Whereas TATA Motors who have reported 82% increase in May 2022 as compared to May 2021, have lower share in the company revenue

### Implication

Hurdles in the demand and production of Ford directly impacting the Revenue and production cycle of the compnay.  
Higher dependency on single customer in dynamic demand scenario is loosing negotiable authority of company.

### Recommendations

Company can focus to develop diverse customer base with pro -active demand tracking from Ford  
TATA motors and other customer demand can also captured subject with considering the existing capacity of the plant. Company may focus on companies having hybrid vehicles.

### Management Comments

.Company has a compensating business against the reduction in Ford's turnover so company will ensure there won't be any impact on turnover due to Ford in succeeding years.

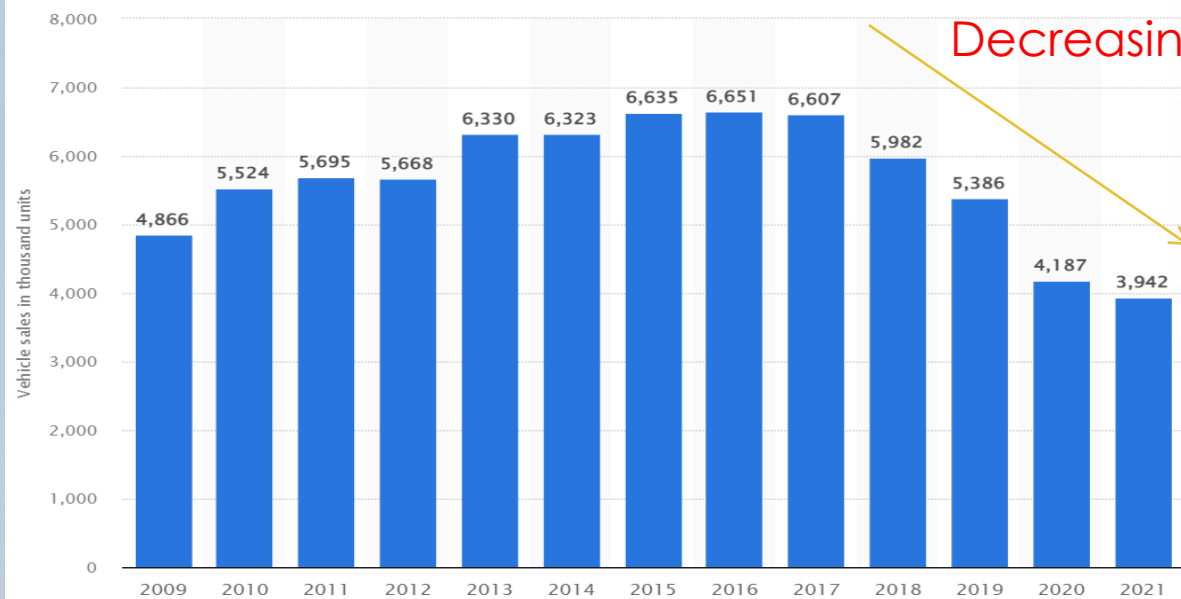
**Department- Sales**

## Annexure 6A: Ford's share as a customer and its global sales trend over the period.

Sum of Total Value	Column Labels					Grand Total	Composition Of Sales
Row Labels	Jan	Feb	Mar	Apr	May		
Ford Motors	16,86,07,165	16,66,47,437	17,26,79,804	14,70,03,804	8,16,95,317	73,66,33,527	29%
General Motors	6,20,96,002	6,68,65,032	7,17,70,642	6,03,07,561	7,84,75,819	33,95,15,056	13%
SUZUKI MOTOR GUJARAT PRIVATE LIMITE	4,89,08,464	5,64,07,006	7,15,67,779	2,85,39,388	4,58,61,041	25,12,83,678	10%
UZAUTO MOTORS POWERTRAIN JSC	3,53,89,582	3,57,02,020	4,41,79,230	3,62,24,752	3,78,92,568	18,93,88,152	7%
TOYOTA INDUSTRIES ENGINE INDIA PVT	2,10,86,945	2,63,58,682	3,29,48,352	3,29,48,352	2,89,94,550	14,23,36,881	6%
TATA Motors	2,32,59,469	2,33,24,677	2,48,44,086	2,45,12,321	1,72,08,923	11,31,49,476	4%

### Ford Motor Company's vehicle sales at wholesale from FY 2009 to FY 2021

(in 1,000 units)



Source link:  
<https://www.statista.com/statistics/297315/ford-vehicle-sales/>

## 7. Raising of Purchase order for Quantity more than requirement

### Observation

Company has a process to generate Purchase orders with the quantities calculated through MRP run. As per information received, MRP run basically calculates the Quantity requirement based on the BOMs present in the system and the sales plan decided by the sales department. There is no manual intervention. Sales plan is prepared based by sales department based on the customer requirement.

We noticed that in case certain A class items, Company is raising POs in excess of requirement for that respective month. This results in the additional quantity pending in the “still to be delivered”. This is due to constant updation of Sales Plan after the MRP Run is conducted. Another reason for this is the revision of BOM.

Please refer the Annexure 7

There might be possibility consumption of lesser material as compared to the BOM Quantity.

#### Root Cause:

Multiple revisions in Sales Plan after MRP run. Gap in the Actual quantity consumed and BOM quantity

### Implications

This will trigger to higher purchase order and vendor may send the goods based on the basis of Purchase order. Currently the communication is done verbally which may create issues due to manual intervention. Chances of overstocking also are increased due to the said process.

### Recommendations

We recommend the company to review the BOM configured in the SAP and align it with the actual consumption so that the accuracy in the Quantity ordered can be increased and overstocking possibility can be decreased to a reasonable extent.

Also, it is recommended that major updation of Sales Plan after MRP run should be avoided.

### Management Comments

We will have a review of BOM in system also see that there will not be any revision in Sales plan after MRP run on monthly basis.

**Department- Purchase Department and SAP department**

## Annexure 7A – Details of Materials having Order quantity more than requirement

Particulars	Still to be delivered (Value)	Order (Value)	% of Delivery Pending
<b>COPPER SCRAP WIRE</b>			
01-04-2022	25,20,000	25,20,000	100%
01-05-2022	19,12,500	19,12,500	100%
01-07-2022	1,44,900	17,25,000	8%
<b>M S SCRAP (ANGLE, CHANNEL END CUTTINGS)</b>			
01-04-2022	45,05,000	45,05,000	100%
<b>RESIN COATED SAND (4.5%) - IVP</b>			
01-04-2022	47,82,240	1,24,90,200	38%
01-09-2022	13,16,520	43,47,000	30%
<b>RESIN COATED SAND (4.8 %)</b>			
01-04-2022	1,19,13,700	3,29,85,000	36%
01-07-2022	47,000	1,55,10,000	0%
01-09-2022	63,36,960	1,32,02,000	48%
01-06-2022	42,06,500	3,29,85,000	13%
<b>RESIN COATED SAND (4.8%) - IVP</b>			
01-04-2022	2,10,15,160	7,35,11,200	29%
01-05-2022	2,13,84,000	5,34,12,400	40%
01-07-2022	31,66,380	3,31,93,600	10%
01-08-2022	2,18,73,630	7,91,94,200	28%
01-09-2022	3,24,20,620	4,04,37,700	80%
01-06-2022	61,81,700	5,26,41,200	12%
<b>RESIN COATED SAND (5%) - IVP</b>			
01-04-2022	60,72,390	3,32,08,000	18%
01-05-2022	1,44,48,030	1,56,13,000	93%
01-07-2022	65,89,000	2,16,83,800	30%
01-08-2022	1,64,360	3,62,26,800	0%
01-09-2022	70,79,220	1,17,40,000	60%
01-06-2022	61,20,400	1,78,23,000	34%

## Annexure 7A – Details of Materials having Order quantity more than requirement

Particulars	Still to be delivered (Value)	Order (Value)	% of Delivery Pending
<b>RESIN COATED SAND 3.5%-GARGI/IVP</b>			
01-04-2022	84,06,000	84,06,000	100%
01-05-2022	44,23,500	44,23,500	100%
01-07-2022	34,40,500	34,40,500	100%
01-06-2022	42,48,000	42,48,000	100%
<b>CORRUGATED BOX TYPE-59</b>			
01-04-2022	4,42,083	5,14,050	86%
01-05-2022	16,40,660	16,44,050	100%
01-07-2022	5,65,000	5,65,000	100%
01-08-2022	4,24,000	4,24,000	100%
01-09-2022	2,12,000	2,12,000	100%
<b>LIQUID PETROLEUM GAS</b>			
01-04-2022	15,90,397	1,81,98,180	9%
01-05-2022	76,61,879	1,93,07,340	40%
01-07-2022	39,98,884	1,62,79,380	25%
01-08-2022	37,86,506	1,54,41,660	25%
01-09-2022	24,38,351	1,33,57,440	18%
01-06-2022	58,25,744	1,81,27,980	32%
<b>TYPE 16 CORRUGATED BOX</b>			
01-04-2022	1,54,215	2,05,620	75%
01-05-2022	6,12,420	6,57,620	93%
01-07-2022	2,26,000	2,26,000	100%
01-08-2022	2,65,000	2,65,000	100%
01-09-2022	1,59,000	1,59,000	100%
<b>Total</b>	<b>23,47,20,348</b>	<b>71,69,68,920</b>	

## Annexure 7B: Comparison of Standard consumption based on BOM and actual consumption

Material Code	Material Description	Consumption as per BOM	Actual Consumption	Diff Qty	Diff %
101002001	Pig Iron	43,63,314	41,53,405	2,09,909	5%
101001001	M S Scrap	13,76,974	10,68,703	3,08,270	22%
101004000	IG	1,22,44,724	1,28,62,909	-6,18,185	-5%
102001011	Copper	71,022	52,514	18,508	26%
102001002	Fe Molly	28,575	16,924	11,651	41%
102001003	Fe Silicon	1,02,601	38,775	63,826	62%
102001005	Fe Manganese	61,441	39,316	22,125	36%
102001004	Fe Chrome	46,602	30,076	16,527	35%
102001016	CPC	61,121	43,609	17,512	29%
102001015	Tin Metal	18,719	10,890	7,828	42%
102001013	Si Carbide	28,525	9,187	19,338	68%
102001018	Fe Sulpher	16,866	10,581	6,285	37%
102001008	Nickel	14,177	7,541	6,636	47%
102001025	PIG IRON S.G. GRADE	6,44,449	0	6,44,449	100%
102001020	CRCA SCRAP	30,15,160	23,97,993	6,17,167	20%
102001038	CRCA SCRAP (LB) INDIAN	5,92,376	5,22,820	69,556	12%
102001033	CRCA SCRAP (LB) JAPANEEZ	2,53,833	2,51,670	2,163	1%
102001023	SHELL COKE	3,24,909	3,09,316	15,593	5%
102001022	FE MANESIUM	1,65,146	1,36,779	28,366	17%
102001021	CRCA PUNCHING	1,55,425	1,38,188	17,238	11%
102001024	INNACULATION	18,119	13,375	4,744	26%
103001169	R C Sand	2,88,21,331	2,86,07,061	2,14,269	1%
203001031	Keracron Sand	43,925	55,059	-11,134	-25%
203001019	ASAHI INS 024	1,50,073	1,48,197	1,876	1%

## 8. Inconsistency between INCO Terms and mutually agreed terms of import purchases

### Observation

We understand that ABC India makes Import purchase from ABC Germany which is on CIP Mumbai basis ( Carriage Insurance Paid till Mumbai) . As per CIP Mumbai INCO term, the seller is responsible for all freight and insurance costs until the goods delivered to named port of destination i.e. Mumbai. ABC Germany is liable to bear freight cost till Mumbai Port. But, as per information available to us, ABC Germany is recharging freight cost to ABC India on monthly basis for the purchases made from ABC Germany On CIP Mumbai basis. As per our opinion, there is conflict between Inco Term CIP Mumbai used and the transaction structured as freight cost is getting recharged back to ABC India.

#### Root Cause:

Discrepancy in structuring of the Import transaction

### Implication

The company may face difficulty during income tax assessment regarding allowability of recharged freight expense. This might also be looked upon by the statutory auditors as a cost which the company should not incur.

Approximate impact on yearly basis would be Rs. 15.45 lakhs

### Recommendations

We recommend the Company to opt any option out of following

- To change in INCO Terms for such purchases from CIP Mumbai to FOB (Free On Board) or CIP Germany.
- To raise debit note for the freight cost recharged and discontinue the policy of recharging freight cost hence forth.

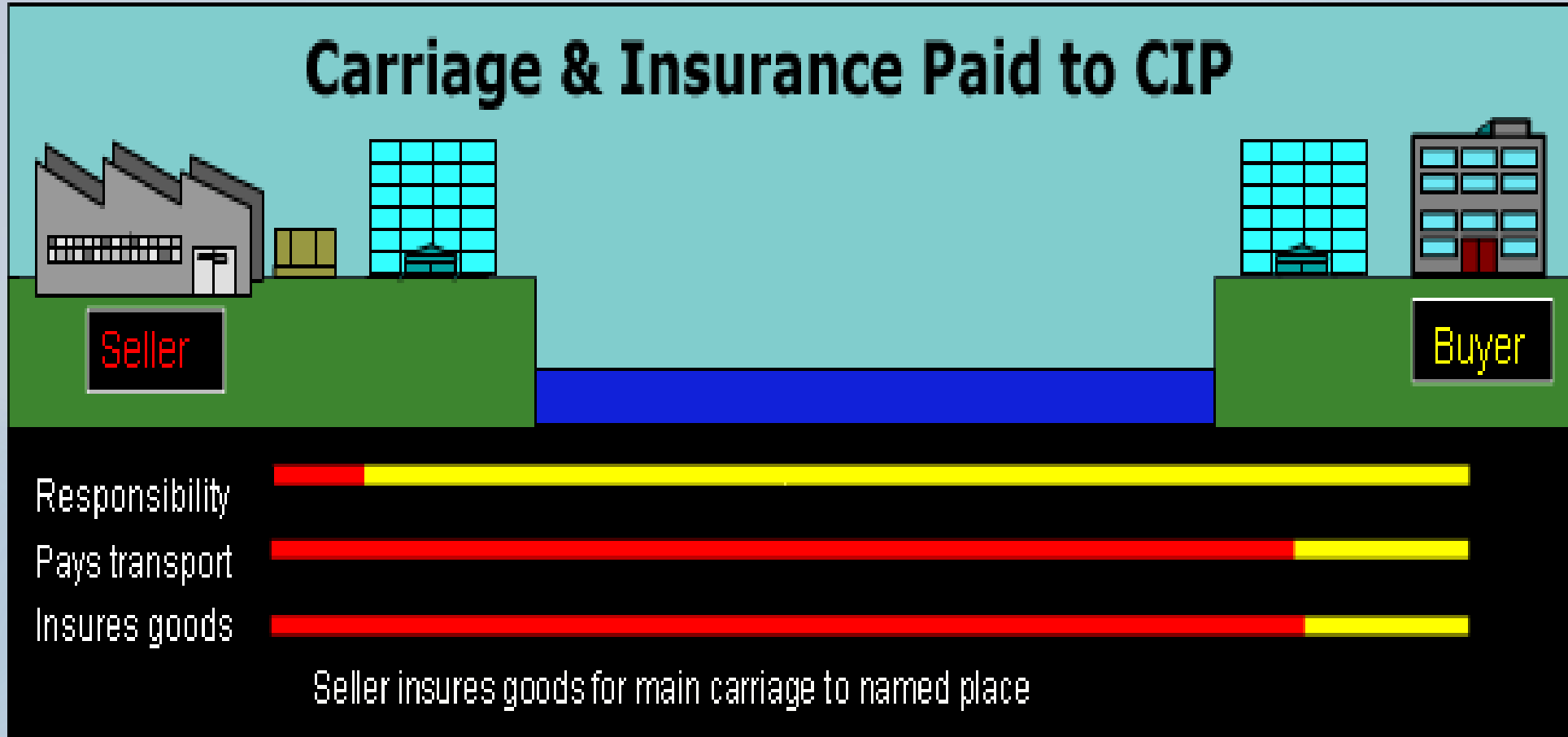
### Management Comments

Further w.e.f. January 2016, the prices charged by ABC Germany would be inclusive of freight cost at 3.6% and hence no separate recharges debit notes would be raised by ABC Germany.

**Responsibility: Logistic Department**

**Date of implementation: January 2016**

## 8A : Carriage Insurance Paid to Mumbai



**In case of CIP, transportation cost up till named destination should be borne by seller**





## 9. Provision for purchase without involving vendor accounts

### Observation

We observed that, AXEPTA has a facility of passing accounting entry for purchases through Journal Voucher as -

Purchases A/c Dr .	XXX
To Bank A/c.	XXX

We have been informed that this entry is only allowable if approved through the login of Finance head. However, we did not receive any business logic to allow such a transaction in the ERP system as it violates the rules of segregation of duties. This type of transactions give sole authority to a single department to execute financial transaction.

Also, as such entry is booked as a Journal voucher, purchases can be accounted for without PO, GRN and other key details from material module. We would also like to mention that we have not observed any entry in this fashion during our period of audit, however the potential risk is high.

**Root cause:** Incorrect control settings in ERP

### Implication

No segregation of duties in payment process is a fraud risk factor. In case of non detection, this control lapse may result in financial loss to the company

### Recommendations

The Company should block bank payment unless debited to vendor account.

### Management Comments

Vendor payment procedure currently followed has multi – layer checks / approvals in place to avoid any un-authorized payments. Specifically in case of one time vendor payments / such kind of expense payments, the cheques drawn and kept with authorized signatories are normally backed up by proper supporting documents duly authorized in multi – layer approval process.

Further we understand that, in new AX 2009 system, the vendor payments can be made only through vendor sub ledgers and this would minimize the above mentioned risk since in such cases, either regular vendor account /one – time vendor account need to be opened before making payment.

**Responsibility:** Finance Department

**Date of implementation:** May 01, 2016



## 10. Reduction in employee transport cost of employees

### Observation

We understand that Company has hired 32 seater and 42 seater buses from Balaji Transport. As per agreement, Contractor is charging Rs. 9966 for 42 seater bus. Company has taken quotations from other contractors for the comparison while vendor selection.

We analysed the cost to be incurred by the contractor for the purpose of providing services to the company.

As per our working, we have observed that, transportation charges of Rs. 9966 for the 42 seater bus are on higher side.

We understand that, Company has just effected reduction in that recently. But, according to us, there is still scope to negotiate the rate of 42 seater.

Kindly refer **Annexure 10A** transport charges costing for better understanding.

### Implication

Company has to pay excessive contract charges which is effected into excess outflow.

### Recommendations

We recommend the company to renegotiate the transport charges for 42 seater and suggest to reduce it by 10%.

This would save Rs. 3 lakhs for the company.

### Management Comments

Looking to the distance of factory from main city and company's future requirement, contract for 42 seater bus was executed. However, Company will take steps to rationalize the rates.

Department : H R Department

## Annexure 10 A

### Costing sheet of Transport charges

Particulars	Dodballapur 32 seater	Yelhanka 41 seater
Charges for 3 shifts	5,375	9,966
No of kms per shift	50	60
Total km	150	180
Cost Per km	36	55
Fuel cost	1,190	1,428
Driver's salary	692	769
Depreciation	2,100	3,288
Repairs	192	269
Insurance	833	1,556
Management cost	100	146
Total cost	5,109	7,456
Profit	266	2,510
Profit %	5.0%	25.2%



## 11. Discrepancy in valuation of inter plant asset transfer

### Observation

We have observed that there are a few assets sent from Chakan to Bangalore Plant after some processing and value addition so as to make the machines compatible for the purpose of manufacturing purpose.

As per information received, these machines are removed from Chakan factory under Rule 3(5) of Cenvat Credit Rules and the duty paid on purchases is passed on plus 12.5% only on value addition. Rule 3(5) is applicable when the inputs or capital goods, are removed **as such** from the factory. Considering the quantum of value added in the cost of machinery, it is evident that the utility and compatibility of the asset has been increased to a reasonable extent. So, it has amounted to 'manufacture'. Hence, according to us, it can not be treated as 'REMOVED AS SUCH'

For the given case, Rule 8 of Central Excise Valuation Rules, 2000- should be applicable which states that *where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value shall be one hundred and ten per cent of the cost of production or manufacture of such goods*". Applicability of Rule 8 leads to valuation as per CAS 4 which states the costing methodology of material transferred.

**Root Cause :** Incorrect application of Excise provisions

### Implication

Incorrect valuation of capital goods transferred to Bangalore plant resulted in the short payment of excise liability to the extent of Rs. **10.21 lakhs**.

Company should explore the option for assembling machines at destination plant only to simplify the excise implications.

### Recommendations

We recommend the company to get the expert opinion on this issue.

### Management Comments

**Audit suggestion is accepted and the process will be initiated for valuation.**

**Responsibility:** Dispatch department

**Date of implementation:**

## 12. Acceptance of same PAN and Bank Account Number by Ascent

### Observation

It is observed that, while entering the details of any new employee, the software allows the super user to enter the same PAN as that of the old employee.

It is also observed that, one bank account number can be entered for more than one employee.

In the current system, while entering the same PAN or same bank account number, system generates a pop up message. But it doesn't prohibit from recording it.

The said loophole in the system can be used which may not be in the interest of company. We have not noticed any issues in payment of salary as such.

Please refer screen shot for the reference.

**Root Cause:** Acceptance of Duplicate PAN and Bank account number

### Implication

There can be duplication of the details of employees in the systems, which can lead to misstatements.

### Recommendations

#### **We recommend the following:**

System should be customized in such a way that, once a PAN or bank account number is entered, it will not accept the same details for any next employee after that.

### Management Comments

**We will communicate with the Software consultant and get it rectified**

**Responsible person : HR Dept**

**Date of implementation :**

## Annexure 12A: Acceptance of same PAN and Bank Account Number by Ascent

- The system allows to alter the bank account number.

The screenshot displays the 'Employee' form in the Ascent Payroll 5.5.6.0 application. The form is divided into several sections: Personal Information, Job Information, and Bank Information. A warning dialog box is overlaid on the form, indicating a conflict with an existing employee record.

**Employee Form Fields:**

- Emp No: 410093
- Last Name: H S
- First Name: KAVITHA
- Middle Name:
- Display Name: KAVITHA H S
- Father/Husband Name: Somathekar
- Gender: Female
- PAN: DURPK7171N
- Date of Birth: 15/02/1990
- Age in years: 28 Year(s) 10
- Director: No
- Auto Grossing up Salary (Expat):
- Payroll Code: 3
- Date of Joining: 02/05/2016
- Current Exp: 2 Year(s) 7 Month(s)
- Group Joining Date: 02/05/2016
- Active/Inactive: Active
- From: / /
- Reason:
- Photo File Path: ...

**Job Information Section:**

- Grade: S-2 SUPERVISOR
- Designation: SUPERVISOR
- Category: 01 STAFF
- Status: 01 Permanent
- Cost Centre: D3040 HR & ADMN.
- Business Area: 00 Default
- Location: 02 Bengaluru
- Reports To / Line Manager: 410003 A RAGHAVENDRA PRASAD
- Email ID:
- Mobile:

**Bank Information Section:**

- Code: AXIS
- Bank: AXIS
- MICR:
- IFSC: UTIB0001204
- A/c No.: 914010032988315
- A/c Name:

**Warning Dialog Box:**

Ascent Payroll - Warning

This Account No is already assigned to Employee 410011 - MANGALA KARADI

Do you want to change it?

Yes No

[Click here](#) to search ifsc code online

Buttons: Reset, Delete, Ok, Close

Contd...

## Annexure 12B: Acceptance of same PAN and Bank Account Number by Ascent

- The system allows to alter the permanent account number.

The screenshot displays the 'Employee' form in the Ascent Payroll 5.5.6.0 application. The form is divided into several sections: Personal Information, Job Information, and Bank Information. A warning dialog box is overlaid on the form, indicating a conflict with the PAN number.

**Employee Form Data:**

- Emp No: 410093
- Last Name: H S
- First Name: KAVITHA
- Display Name: KAVITHA H S
- Father/Husband Name: Somathekar
- Gender: Female
- PAN: BPMFK5211E
- Date of Birth: 15/02/1990
- Age in years: 28 Year(s) 10
- Director: No
- Payroll Code: 3
- Date of Joining: 02/05/2016
- Current Exp: 2 Year(s) 7 Month(s)
- Group Joining Date: 02/05/2016
- Active:  Active
- Auto Grossing up Salary (Expt):

**Job Information:**

- Grade: S-2 SUPERVISOR
- Designation: SUPERVISOR
- Category: 01 STAFF
- Status: 01 Permanent
- Cost Centre: D3040 HR & ADMN
- Business Area: 00 Default
- Location: 02 Bengaluru
- Reports To / Line Manager: 410003 A RAGHAVENDRA PRASAD
- Email ID: [Redacted]
- Mobile: [Redacted]

**Bank Information:**

- Code: A03
- Bank: A03
- MICR: [Redacted]
- IFSC: UTIB0001204
- A/c No.: 916010019343638
- A/c Name: [Redacted]

**Warning Dialog Box:**

Ascent Payroll - Warning

This PAN No is already assigned to employee 410011 -MANGALA KARADI

Do you want to change it?

Yes No

[Click here](#) to search ifsc code online

Buttons: Reset, Delete, Ok, Close

# 13. Absence of maker checker system in Subcontracting process

## Observation

SAP has different codes for internal inventory movements. According to us, the purpose of the stock movement is to keep trail of the inventory movements in the SAP, allocate responsibility and maintain the maker checker in the SAP.

As per current process, production person uploads the semi fettled finished automobile part through 101 movement to 56 warehouse. Then, Commercial person transfers stock from 56 to 52 warehouse through 311 movement based on a physical slip issued (*Refer sample slips in Annexure 16A*) and again stock moved from 52 to vendor location through 541 movement. Currently, commercial department only passes 311 as well as 541 movement. This defeats the prime motive of the two different movements i.e. maker checker.

Hence, a person who is signing is not able to confirm the number of units sent and a person who is counting the units is not signing any document. This will have unrestricted access to the subcontractor to the whole finished goods.

### Root Cause:

No segregation of duties relating to goods sent to contractors for further processing.

## Implication

1. The discrepancy in the delivery challan may not be identified by the current system.
2. The responsibility of any discrepancy may not be allocated appropriately.

## Recommendation

We recommend that the 311 movement should be booked by the production and the entry no should be communicated to Commercial person at the Gate No. 3 based on which he will pass the delivery challan. Also Company should avoid physical slips and need to use proper Form containing Name, Goods description, code and Qty etc.

## Management Comments

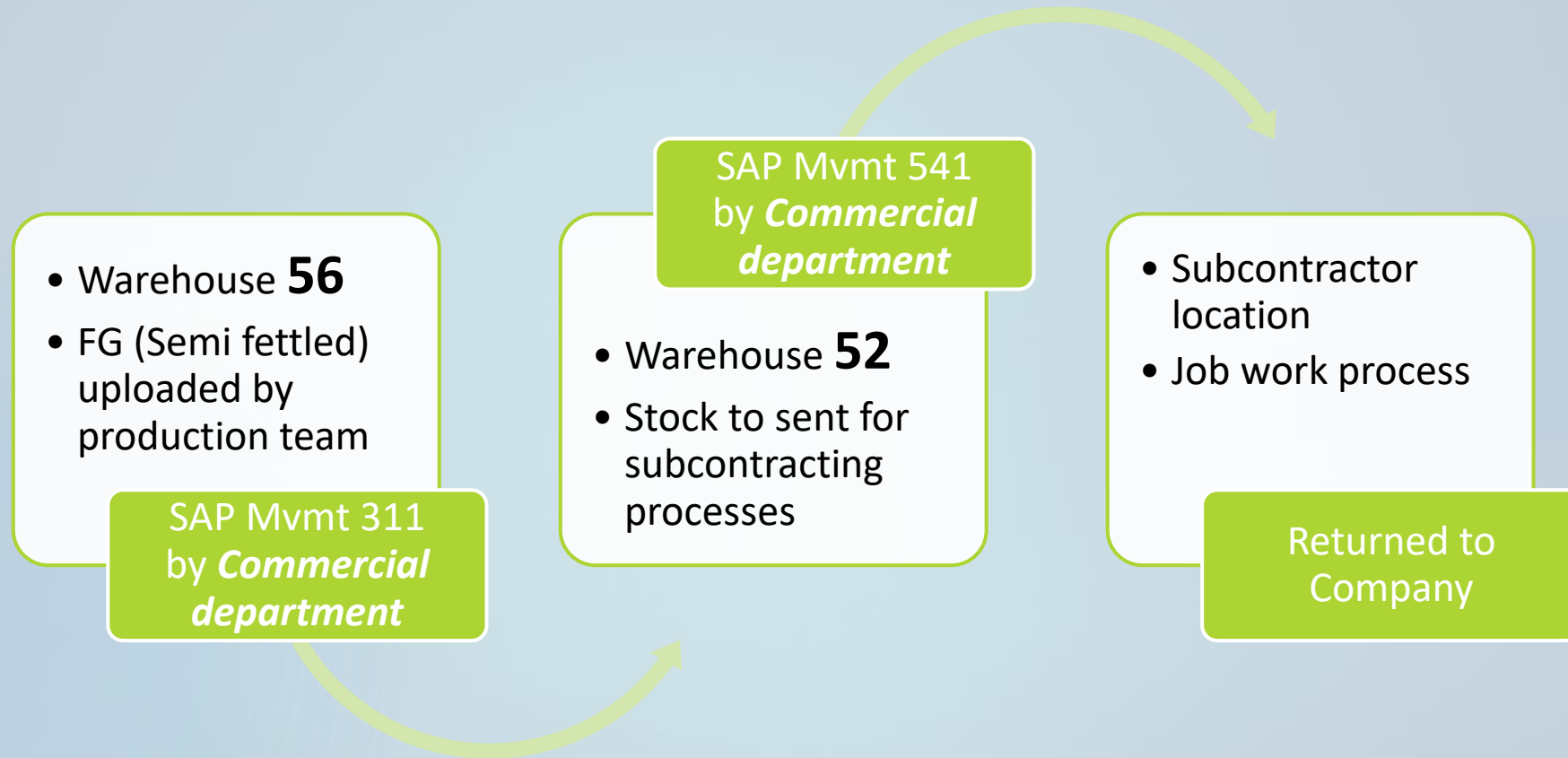
SAP department will take management approval for new manpower addition for this additional activity.

**Responsible person : Production Department**

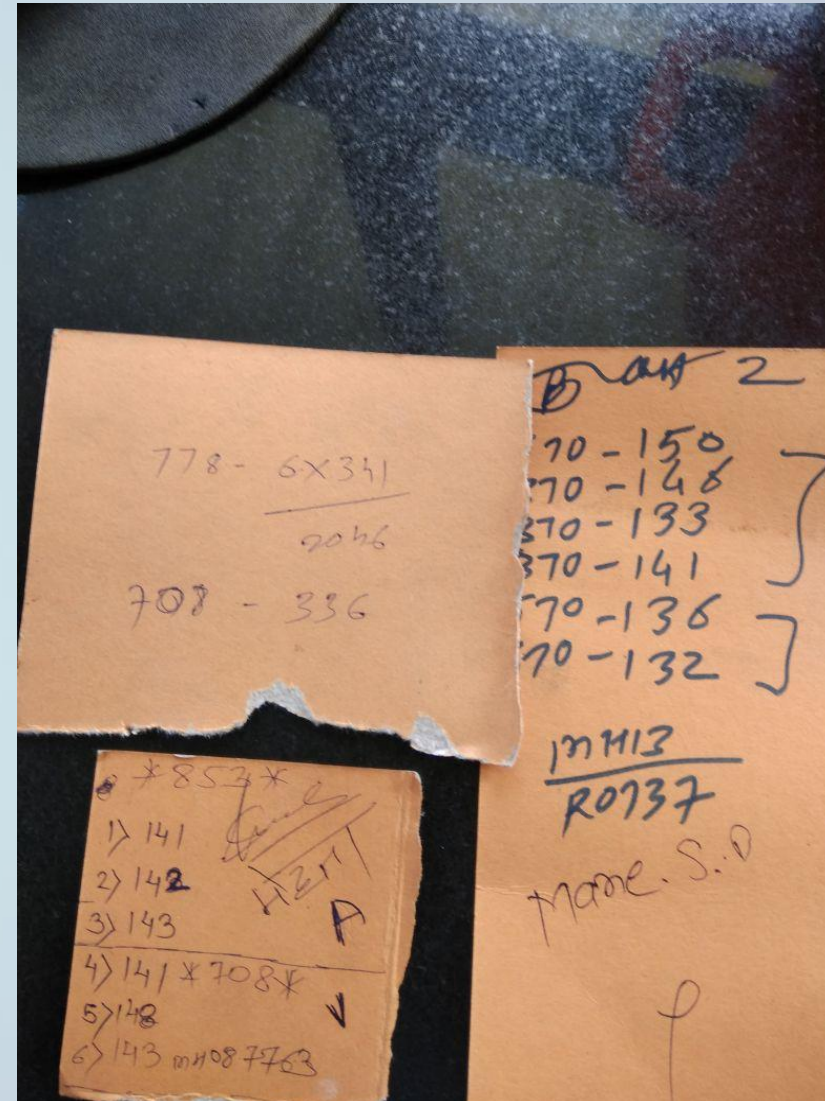
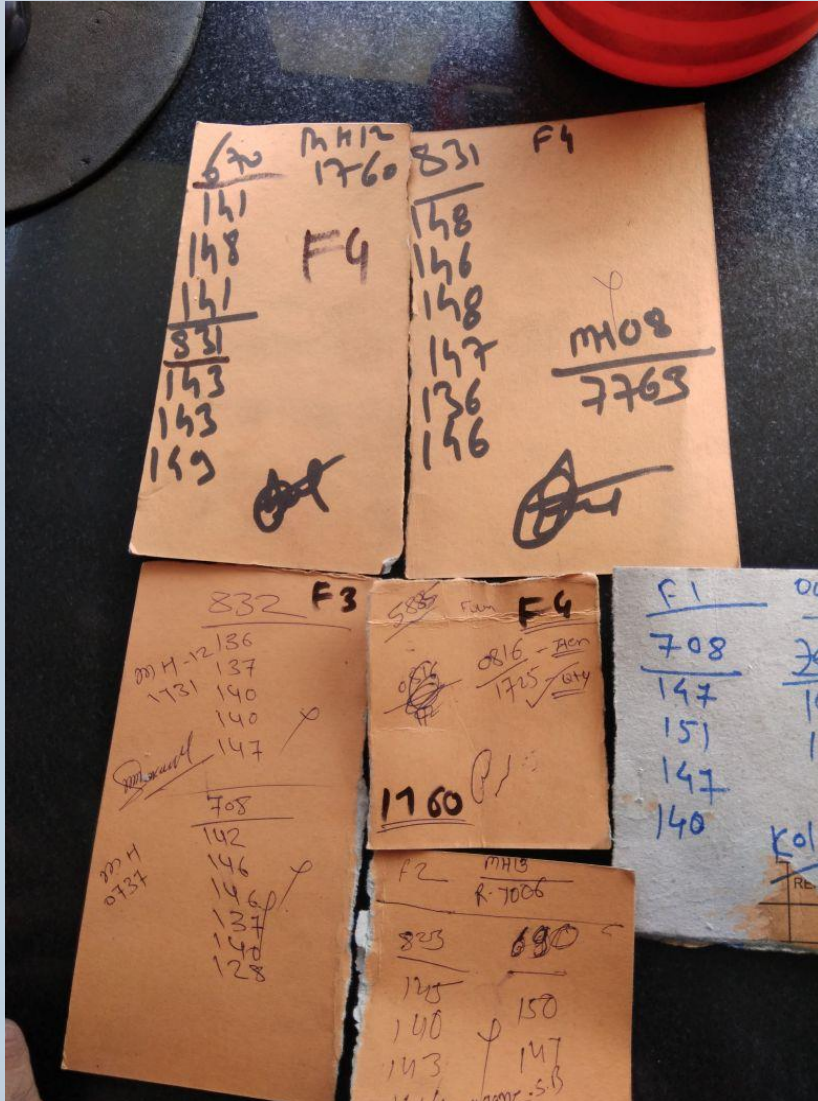
**Date of implementation :**



# Annexure 13A : Subcontracting process flow



Annexure 13B : Images of sample physical slip prepared for transfer of goods from Foundry (Prod Dept.) to Gate 3 (Commercial Dept.)



## 14. Purchase executives authorized to pass GRN entries in the system

### Observation

As per our analysis of the data, there are events where at the purchase executive have passed the GRNs. GRNs should be passed by stores department only, whose job is to compare the PO terms with GRN. This acts as a checker system on the purchase executives.

After analyzing the reasons for such entries, we have been informed that the Purchases department were allowed to pass GRNs during audit period of January 2020 to September 2020. Also, the said authorization was given through verbal communication and thus we have not received any backup mail authorization. No GRNs were passed by purchase executives in 2021.

However, the said authorizations are still open and purchase executives can still pass GRN entries. This unauthorized access to pass GRN to departments other than Stores department is not according to standard practice.

Kindly refer Annexure 14A for GRN entries passed by purchase executives.

### Root Cause:

Purchase department still have the rights to book GRN in the system.

### Implication

Since the system still allows the purchase executives to make GRN, it would comprise the system of maker-checker system for GRN & PO.

### Recommendations

We recommend the company that:

The present authorization to Purchase executives should be blocked to retain the importance of the standard maker-checker system for GRN & PO.

### Management Comments

**Responsible Department: Strategic Procurement**

### **Response:**

SAP should not allow purchase executives to pass GRN entries. We will make suitable amendments in the system.



Annexure 14A – GRNs passed by Purchase executives

User name	Jan 2020	May 2020	June 2020	July 2020	Aug 2020	Sept 2020	Oct 2020	Total 2020	Department
CHAKAN.PU	4							4	Material Mgmt (Komal Patil)
JADHAO.AM						1		1	Material Mgmt
MEHTA.AB						101		101	Purchase
SAURABH.AB		5	29	25	16	27	38	140	Projects
SHINDE.MA						319		319	Purchase
TANPURE.HI						43		43	Purchase

User name	Jan 2021	June 2021	2021 Total	Department
MEHTA.AB	1	2	3	Purchase

## 15. Higher range of prices charged by Vendor for coils compared to rise in market prices

### Observation

One of the primary input materials of the company is “coil” which is used in PHE & TES segment.

As per our observation of the material prices, we have observed that the coil prices have rose by 5.64% in 2021 compared to 2020 as per Whole Sale Price Index of semi-finished stainless steel across India. However, we have observed that the Company has purchased the coils with 10.65% rise in 2021 compared to 2020. Thus, it implies that the Company is charged with higher rate than the market rise of prices.

Also, the quantity of procurement of coils by the Company is significant. However, as per our discussion with the purchase department, no vendor offers any discount to the Company based for the quantity.

Please refer Annexure 15A for reference.

#### **Root Cause:**

Lower negotiation with the coil vendors for the material prices.

### Implication

The Company has to bear the raised or constant price of charged by the Vendor

### Recommendations

We recommend to the Company that:

The Company should negotiate for reduction in coil prices accordingly.

Also, Company should ask for appropriate discount from Vendors based on the quantity offered.

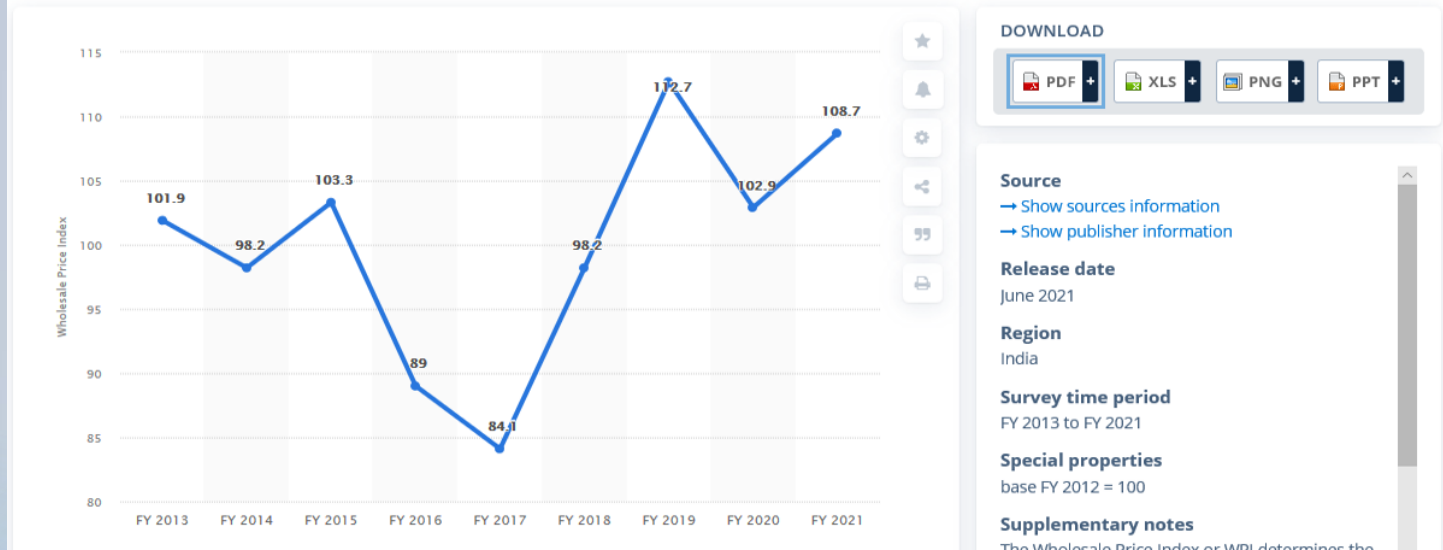
### Management Comments

**Responsible Department: Strategic Procurement**

**Response: We will renegotiate the prices with the vendors.**

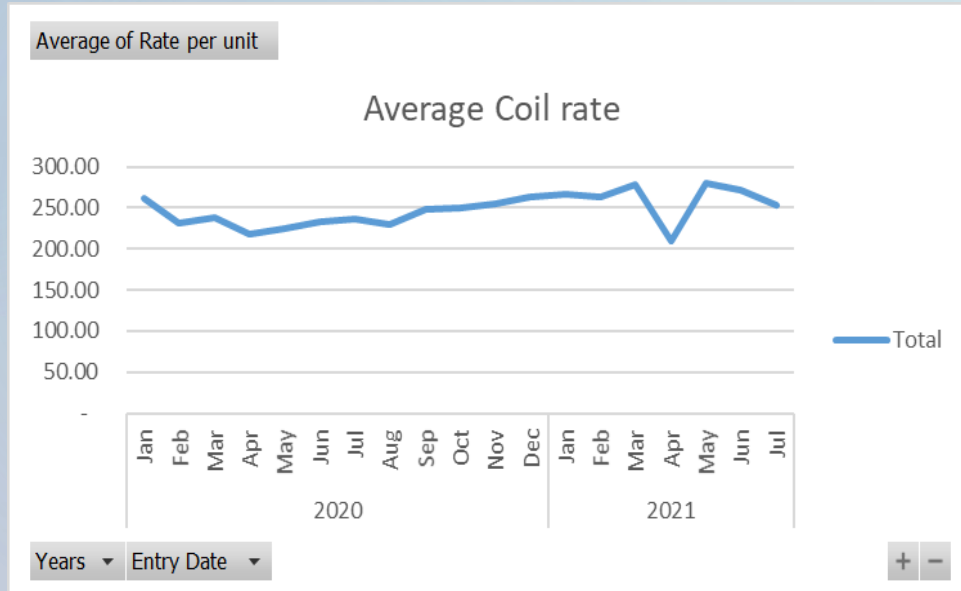
# Annexure 15A: Coil Price Analysis

## Wholesale Price Index of semi finished stainless steel across India from financial year 2013 to 2021



### Conclusion:

Particulars of price change in 2021 as compared to 2020	%
Rise in Wholesale coil index in India from 102 to 108	5.64%
<b>Actual Rise in coil Prices from Rs. 243 to 268</b>	<b>10.65%</b>



## 16. Higher manpower quantum as compared to companies in foundry businesses

### Observation

As a part of study, we compared the employee salary cost (without management) % w.r.t turnover with other listed companies similar to the ABC Ltd. We notice that ABC Ltd is having consistent higher % of salary cost by 5% on an average basis. We further analysed sales per employee is lowest in list i.e. 21 lakhs v/s 1.2 Cr average in respect of other companies. More over we compare asset turnover ratio which states the asset utilisation, almost matches with other companies. We understand that company has tried many times for automation since last 10 years

We understand that ABC has additional requirement of manpower due to inhouse additional process like fettling, metallurgical testing etc. but still difference of 5% w.r.t. Sales in salary cost and 1 Cr in sales per employee is on higher side

Please refer **Annexure 16A, 16B** for reference.

### Root Cause:

It seems that company is employing higher number of employees strength as compared to the other foundry companies.

### Recommendations

We recommend to the Company that:

Company need to relook the employee and labour number requirement technically and do the bench marking study for labour number requirement.

### Management Comments

**Responsible Department: Strategic Procurement**

**Response: Appropriate benchmark is not available for comparison.**

## Annexure 16 A: Comparison of Employee cost with Management cost Vs Turnover

Sr.no	Name of the Company	Nature of business	15-16 (in Cr)			16-17 (in Cr)			17-18 (in Cr)		
			Sales	Employee Cost (without Management)	Ratio	Sales	Employee Cost (without Management)	Ratio	Sales	Employee Cost (without Management)	Ratio
1	Bharat Forge	Forging Metals Automotive Defence Energy	Not Available			3616.22	348.56	<b>9.64%</b>	5006.11	405.46	<b>8.10%</b>
2	kirloskar Ferrous	Pig Iron and Iron Castings.	1113.93	33.77	<b>3.03%</b>	1133.71	4.60	<b>0.41%</b>	1729.03	34.80	<b>2.01%</b>
3	Rolex rings	designs and manufactures hot forged rolled rings	Not Available			694.50	29.64	<b>4.27%</b>	770.153	38.18	<b>4.96%</b>
4	Ratnamani Metals & pipes	stainless steel pipes and tubes, and carbon steel pipes	1719.27	80.52	<b>4.68%</b>	1489.93	74.75	<b>5.02%</b>	1822.229	83.54	<b>4.58%</b>
5	Electrosteel	Pig Iron, Billets, TMT Bars, Wire Rods and Ductile Iron Pipes	2004.30	168.31	<b>8.40%</b>	1929.12	173.62	<b>9.00%</b>	2023.582	177.06	<b>8.75%</b>
6	Talbros Engineering Ltd	manufactures rear axle shafts	141.37	11.80	<b>8.35%</b>	1623.57	145.43	<b>8.96%</b>	208.96	17.36	<b>8.31%</b>
	<b>Average</b>				<b>6.11%</b>			<b>6.21%</b>			<b>6.12%</b>
1	ABC Limited		438.13	53.42	12.19%	467.01	60.14	12.88%	419.19	49.35	11.77%
					<b>-6.08%</b>			<b>-6.66%</b>			<b>-5.65%</b>



## Annexure 16 B : Asset Turnover Ratio

Sr.no	Name of the Company	15-16 (in Cr)			16-17 (in Cr)			17-18 (in Cr)		
		Sales	Asset Value	Ratio	Sales	Asset Value	Ratio	Sales	Asset Value	Ratio
1	Bharat Forge	NA			3,616.22	2,361.21	<b>1.53</b>	5,006.11	2,514.61	<b>1.99</b>
2	Tata Steel	42,697.44	49,561.05	<b>0.86</b>	53,260.96	71,778.97	<b>0.74</b>	60,519.37	70,942.90	<b>0.85</b>
3	kirloskar Ferrous	1,113.93	546.02	<b>2.04</b>	1,133.71	569.98	<b>1.99</b>	1,729.03	556.80	<b>3.11</b>
4	Rolex rings	NA			694.50	345.09	<b>2.01</b>	770.15	335.14	<b>2.30</b>
5	Ratnamani Metals & pipes	1,719.27	445.12	<b>3.86</b>	1,489.93	447.48	<b>3.33</b>	1,822.23	444.52	<b>4.10</b>
6	Electrosteel	2,004.30	1,706.14	<b>1.17</b>	1,929.12	1,634.86	<b>1.18</b>	2,023.58	1,600.41	<b>1.26</b>
7	Talbros Engineering Ltd	141.37	21.23	<b>6.66</b>	162.36	41.12	<b>3.95</b>	208.96	53.25	<b>3.92</b>
	Average			<b>2.92</b>			<b>2.10</b>			<b>2.51</b>
8	ABC Ltd	438.13	190.52	2.3	467.01	215.29	2.17	419.19	241.87	1.73

## 17. Open Sales Orders

### Observation

As a part of audit procedure, we analyzed that the open orders in hand with the Company as on February 28, 2021. The total orders in hand today are Rs. 239 crores (exactly equivalent to revenue of FY 2019-2020), which are active & the Company expects to generate the sales in stages.

As per our analysis of the data, we are of the conclusion that the Company has Rs. 34 crores (for PHE product) of pending orders piling up through the year 2017 to 2019 which are non-project based orders. In respect of the said order, Gross margin to the extent of Rs. 11 crores is blocked till the current year.

#### Root Cause:

Lower control on the active open orders

### Implication

Delayed opportunity of earning the gross margin on timely basis

### Recommendations

We recommend the company that:

The Company should ensure active completion of the pending orders in hand

### Management Comments

Responsible department: Finance & Sales Department

Comments: Company has already initiated the process and the Note and Minutes have been sent for Management Approval

Implementation- Immediate

## Annexure 17: Year-wise Open Order of Non-project based work

Particulars	Amount of Sales	Amount of Gross Margin
2015	33,988	11,279
2016	1	0
2017	2,08,49,071	63,57,451
2018	9,15,16,519	2,06,52,390
2019	24,43,78,703	8,76,70,867
2020	62,29,29,549	19,03,74,215
2021	19,19,52,872	5,27,79,656
<b>Grand Total</b>	<b>1,17,16,60,703</b>	<b>35,78,45,858</b>

## 18. Inappropriate insurance of stock, building and other assets

### Observation

In the Business Suraksha Insurance Global Policy, it has been found that there has been inappropriate allocation of insurance coverage. The stock at factory is underinsured by 32%, the stock at W57 is underinsured by 80% and the stock at KSH does not have an insurance coverage. The office building of ABC is also underinsured. The laptops at rented premises have been over insured.

Appropriate allocation and proper coverage of insurance is essential to make sure that all assets are well protected from uncertain events.

Kindly refer annexure 18A, 18B, 18C.

#### Root Cause:

Inappropriate insurance coverage to stock, building and other assets.

### Implications

Inappropriate insurance coverage leads to assets being exposed to uncertain and unfortunate events. Stock is under-insured by Rs. 29 crores, Building is under-insured by Rs. 11 lacs. Laptops are over-insured by more than Rs. 2 crores.

### Recommendations

The company is recommended to revise the insurance policies and make sure that all assets are fully insured.

### Management Comments

**Responsible Department:** Finance

**Response:** Accepted. Insurance contract will be reviewed

### Annexure 18A – Under insurance of Stock as per Value of stock

Particulars	Sum Assured	Value of Stock as on 02/04/2021	Under coverage	Under coverage %
Factory Stock	56,00,00,000	82,72,59,953	-26,72,59,953	-32%
W-57 Warehouse	60,00,000	2,90,32,243	-2,30,32,243	-79%
KSH Warehouse	0	39,25,743	-39,25,743	-100%
<b>Total</b>	<b>56,60,00,000</b>	<b>86,02,17,939</b>	<b>-29,42,17,939</b>	

### Annexure 18B – Under insurance of Building as per Cost of building

Particulars	Amount
Sum Insured	28,48,41,696
Cost of Building as on 31/03/2021	28,60,05,479
<b>Difference</b>	<b>-11,63,783</b>

## Annexure 18C – Over insurance of Machines as per Replacement Value

Particulars	Amount
Sum Insured of machines at Rental premises	2,26,00,000
Number of Laptops on Rental Premises	30
Replacement value of Laptops	18,00,000
<b>Multiples of Insurance</b>	<b>12.56</b>
<b>Comment</b>	<b>Over insurance</b>

Number of employees at rental premises

Sales Office location	Number of Employees	Number of Laptops Assumed
Bangalore	3	3
Chennai	3	3
Kolkata	5	5
New Delhi	8	8
Thane	3	3
Vadodara	8	8
<b>Grand Total</b>	<b>30</b>	<b>30</b>

## 19. Difference in salary receipt in hand versus amount paid to contractor

### Observation

The amount paid to the contractor includes the wages to be paid to the contract employees and service charges of the contractor. The contractor has obligation to pay the full amount to the contract employees as agreed in the agreement.

As a part of audit evaluation, we check whether the contract employees actually receive the amount specified in the monthly invoice. During the evaluation we observed that the contractor has specified that the contract employees have taken advance and hence, deductions were made on such account. On confirmation with the contract employees, they denied the receipt of any such advance. With the evidences available with us, we can conclude that there is a gap in the amount paid to contractor for the employee wages and the amount actually paid by the contractor to the said employees. We have estimated the amount as Rs. 28.21 lacs.

This has been observed in following service vendors:

Security services

Kindly refer Annexure 23A.

#### **Root Cause:**

Difference in salary receipt in hand versus amount paid to contractor

### Implications

The service contractor is earning the differential in excess of what has been agreed in the agreement hence paying excessive Rs. 28.21 Lacs.

The contract employees get lower pay in hand.

### Recommendations

We recommend the company that:

Company make use of the following rights

- a) To recover the said amount by raising a debit note for the FY 2020-2021.
- b) To take legal action against the contractor as per rights conferred by the agreement

### Management Comments

**Responsible Department:** HR & Admin

**Response:** We will investigate the same further. Contract will be reviewed.

## Annexure 19A – Calculation of Difference in Payment

### Swaraj Facilities

Name Of Employee	Designation	No. of Days in a Month	Per Day Rate*	Amount as per Jan 2021 Invoice	Actual Credit Of Salary in month of April 2022	Monthly Impact	Percentage Impact	Annual Impact
XXXXXXXX XXXXX	Guard	31	763.23	23,660	12,617	11,043	47%	1,32,516
XXXXXXXX XXXXX	Guard	31	763.23	23,660	15,417	8,243	35%	98,916
XXXXXXXX XXXXX	Driver	31	933.35	28,934	14,550	14,384	50%	1,72,608
XXXXXXXX XXXXX	Guard	31	763.23	23,660	13,515	10,145	43%	1,21,740
XXXXXXXX XXXXX	Guard	31	763.23	23,660	13,500	10,160	43%	1,21,920
<b>Average Percentage Impact</b>							<b>43%</b>	

### Extrapolation of Annual Impact

Security Type	Number Of People	Monthly Gross Pay as per Jan 2021	Total Payment For Jan 2021	Annual Payment
Supervisor	3	19,857	59,571	7,14,852
Guards	22	18,778	4,13,116	49,57,392
Driver cum Guard	3	22,963	68,889	8,26,668
<b>Total</b>				<b>64,98,912</b>
<b>Financial impact</b>				<b>28,21,128</b>

### Notes:

- 1 Rate Per day has been Considered as per contract for FY 20-21.
- 2 Salary never reduces on annual basis. Hence, the amount credited for the month of April 2022 relates to actual payment for the month.
- 3 We enquired the reason for lower payment and we found that the contractor consistently pays a lower amount every month.
- 4 Mr Satyawan Jadhav had received OT pay of Rs.4250. The amount of normal pay received is Rs. 13500. Hence, only normal pay is considered.



## 20. Incorrect computation of service charges

### Observation

Service charges are charges paid to contractor for providing the manpower services. These charges are paid as certain percentage which are agreed in contract. Generally, services charges are paid to the contractor on Gross wages (Basic+DA+Other Allowances) and no other expenses like Statutory dues and bonus are included in computation of Service charges as they do not increase any productivity.

While analyzing the security agreement of Swaraj Facility, we have observed that the Company is paying service charges at 10% to Swaraj Facilities. The Company is paying these charges on wages including all statutory due and also on bonus.

Kindly refer annexure 20A

#### **Root Cause:**

Incorrect computation of service charges.

### Implications

Company is paying higher amount of service charges to the security agency hence increasing the cost to the Company by Rs. 3.67 lacs.

### Recommendations

Company should revise the contract with security agency. The percentage of service fees to be paid should be fixed and the same should be computed on gross salary excluding all statutory dues.

### Management Comments

**Responsible Department:** HR & Admin

**Response:** Contract terms will be reviewed and renegotiated.

## Annexure 20A – Calculation of excess services charges

### Service charges as per correct computation

Particulars	Security Supervisor	Security guard	Bouncer cum Driver
Gross salary excluding Statutory dues	14,841	14,030	17,661
Service charge at 10% on above	1,484	1,403	1,766
Service charges actually paid	1,986	1,878	2,296
Excess service charges paid p.m	502	475	530
<b>Excess as a percentage of net salary</b>	<b>6%</b>	<b>6%</b>	<b>7%</b>

### Calculation of excess service charges paid

Month	Amount	Excess Service charges paid (6%)
Jan-21	2,35,331	14,120
Feb-21	6,41,456	38,487
Mar-21	6,54,618	39,277
	<b>15,31,405</b>	<b>91,884</b>
	Excess service charges paid for 3 months	91,884
	<b>Excess service charges for paid 12 months</b>	<b>3,67,537</b>

## 21. External Benchmarking rates are lower than the agreement rate for warehousing

### Observation

As per the internal audit procedure we have carried out the external benchmarking for warehousing. In doing so we have compared multiple warehousing facilities around Chakan to the current warehousing facility that we have. We found out that the other warehousing facilities surrounding Chakan are quoting a comparatively lesser amount for the same sq ft as the current warehouse provider. If appropriate quotations had been taken prior to the agreement with current service provider, the company would not have had to bear such high rates.

Kindly refer Annexure 21A.

#### **Root Cause:**

No quotations taken for comparison before entering into the current agreement.

### Implications

The company is paying a comparatively higher amount than the current market rate causing an excess cash outflow of Rs 13 lacs approximately.

### Recommendations

We recommend that the company compare various quotations before entering into any agreement.

### Management Comments

**Responsible Department:** Purchase Department

**Response:**

## Annexure 21A – External Benchmarking of Warehousing Expenses

Name of service		Warehousing				
Quotation Number		1				Financial Impact
Name of quotation Provider		Maharaja Warehouse				
Contact Number		9970111135				
Email ID (if available)						
Location of Service Provider		Chakan				
Particulars	Existing Vendor Rate	Quotation Rate	Inflation Adjusted 6% 2021	Inflation Adjusted 6% 2020	Difference	
Monthly Charges	148500	43,200	40,755	38,448	-1,10,052	-13,20,626
Per Square feet charges	55	16	15	14	-41	
Quotation Number		2				
Name of quotation Provider		Vatsalya Warehouse				
Contact Number		07947196126				
Email ID (if available)						
Location of Service Provider		Chakan				
Particulars	Existing Vendor Rate	Quotation Rate	Inflation Adjusted 6% 2021	Inflation Adjusted 6% 2020	Difference	
Monthly Charges	1,48,500	40,500	38,070	35,786	-1,12,714	-13,52,570
Per Squarefeet charges	55	15	14	13	-42	
Forklift per hour	Not Given	500				
Quotation Number		3				
Name of quotation Provider		Sadguru Warehouses				
Contact Number		9763855399				
Email ID (if available)						
Location of Service Provider		Chakan				
Particulars	Existing Vendor Rate	Quotation Rate	Inflation Adjusted 6%	Inflation Adjusted 6%	Difference	
Monthly Charges	1,48,500	43,200	40,608	38,172	-1,10,328	-13,23,942
Per Squarefeet charges	55	16	15	14	-41	
Forklift per hour	Not Given	800				
Crane Per Hour	Not Given	800				

## 22. Missing clauses in the agreement

### Observation

Agreement specifies the facts, terms and conditions of the contract to any third party taking cognizance of the same. For example, few basic things such as witnesses, date of sign, place of sign, etc. are essential for completeness of the contract.

We have observed the following issues in majority of the agreements:

- Blank Witnesses (Human evidence is missing)
- No date of signing (Reference date is missing)
- Place of signing missing (reference place is missing)
- Name of the person and designation (Clear name of authorised personnel and designation of the said person is missing)
- Indemnification (no clarity over responsibility in case of uncertain events)
- Force Majeure (no clarity of actions to be taken in case of unforeseen situations)

Kindly refer Annexure 22A.

#### **Root Cause:**

Missing clauses in the agreement.

### Implication

Lower clarity for the points which are missing in a standard agreement.

### Recommendations

We recommend the company:

To venture in to any contract only after considering all the points and revise the agreement from time to time as per requirements.

### Management Comments

**Responsible Department:** Finance

**Response:** We will review the agreements and amend it accordingly.

## Annexure 22A – Missing Clauses

Particulars	Canteen Expenses (Shourya)	Employee Transportation (40)	Employee Transportation (17)	Employee Transportation (Sumo)	Housekeeping (Amit Facilities)	Security Services (Swaraj & BSA)
Medical Examination	Available	Missing	Missing	Missing	Available	Available
Bank Payment Details	Missing	Missing	Missing	Missing	Missing	Missing
Insurance Specifications	Available	Available	Available	Available	Missing	Available
Force Majeure	Missing	Available	Available	Available	Missing	Missing
Alternate Arrangements	Available	Available	Available	Available	Available	Missing
Submission of Bills regarding Extra Payments	Missing	Missing	Missing	Missing	Available	Missing
Extra Requirements	Available	Missing	Missing	Missing	Missing	Missing
Amendments/ Alterations in Agreement	Available	Missing	Missing	Missing	Missing	Available
Arbitration Clause	Missing	Available	Available	Available	Available	Available
Service Deficiency Clause	Available	Available	Available	Available	Missing	Available
Authority & Details of Signing	Available	Missing	Missing	Missing	Missing	Missing

\*Available - Specifies that the criteria is present in the agreement



# Questions and Answers

THANK YOU