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Foreword

The articles in the journal have been written keeping in view the clients served by this Institute, the cuting edge of audit namely Audit Officers and staff of the IA&AD . This volume has articles on practical auditing.

I thank the contributors and others who helped in publishing this volume.

Ashutosh Joshi
Director General
RTI, Jaipur

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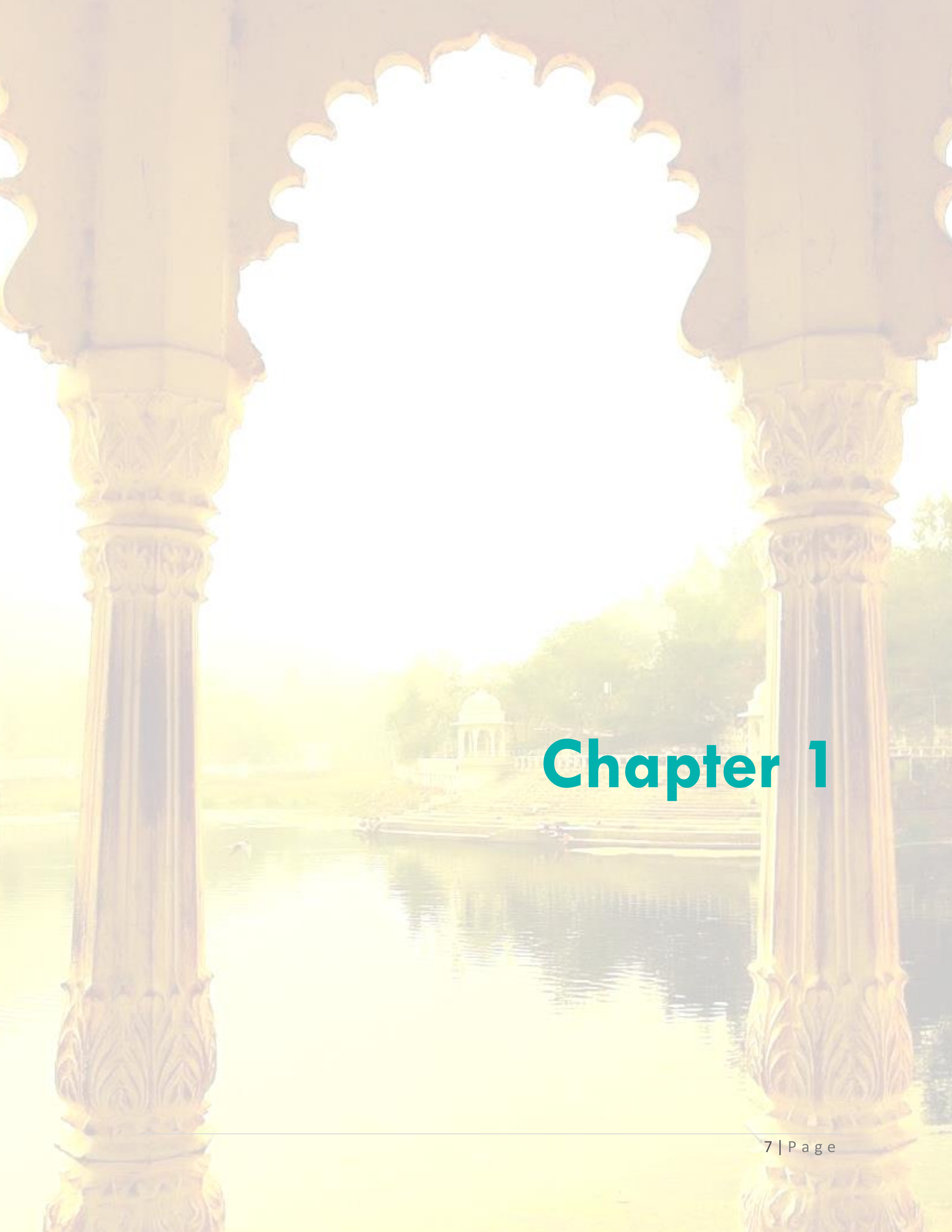

Chapter 1

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Conducting effective financial audit of Central/State Public Sector Undertakings / Autonomous Bodies.

(Continued from second edition of Focus; RTI Journal)

(This article has been penned by Shri Brijeshwar Prasad Tripathi, Senior Audit Officer, O/o- the Principal Accountant General (Audit-II) Uttar Pradesh, Lucknow. He has used his knowledge and experience gained nationally and internationally to present systemically arranged guidance material for conducting effective financial audit of the Central/State Public Sector Undertakings (PSUs)/ Autonomous Bodies (ABs). This material provides a practical approach to the audit of Annual Financial Statements(AFSs). This material has already been used in imparting online trainings by him to the participating officers of Civil and Commercial streams, through RTI, Jaipur and RTI, Prayagraj. The key feature is the Comprehensive Top-down Drilling Approach (CTDA) evolved by Shri B P Tripathi for systematic and comprehensive audit of Annual Financial Statements

The material is presented in four sections:

1. Basic Inputs-Learning objectives, types of financial audit, types and constituents of the financial statements, etc.
2. Start to End Audit process including Comprehensive Top-down Drilling Approach (CTDA)
3. Framing, classifying, drafting and reporting the comments, with illustrative structures
4. Interesting Case Studies based on actual audits

In this edition of our Journal, we bring you the third sections of the article)

Section III

Framing, classifying, drafting and reporting the comments on the Annual Financial Statements

In the foregoing segments of this article “Conducting Effective Financial Audit”, a practical approach and audit techniques to identify and unearth the inadvertent as well as the managed errors i.e. ‘window dressing’ in the Annual Financial Statements (AFSs) have been discussed. While identification and detection of errors in the AFSs require adequate audit intelligence and experience, “to-the-point and easily understandable presentation” of these errors in the form of ‘Comments’ in the Auditor’s Report/Certificate call for sincere efforts in augmentation of drafting and reporting skill. The standards on auditing (SAs) prescribe formats/template for Report to be prepared and opinion to be framed by the Statutory Auditors, based on audit of the AFSs by them. Similarly, circulars issued by the CAG Headquarters prescribe different formats/template of 'Certificate' and 'Separate Audit Report (SAR)' to be issued by the CAG in case of Supplementary audit and Sole audit respectively, as already outlined in the foregoing segment of this article. However, there has always been a curiosity to know how to draft a "to-the point and easily understandable comment". This would basically enable the understanding about the structure and contents of a comment. Brevity without compromising the clarity is a vital requirement for drafting a comment. Keeping in view the varieties in nature of comments, there is no predetermined template for drafting a comment. Therefore, cases can be seen where not only brevity and clarity but also uniformity and consistency in drafting of a comment are compromised. To address this problem, an attempt has been made to at least bring out the illustrative structure and contents of various types of comments to maintain the uniformity and consistency in drafting of a comment to the possible extent. Accordingly, the requisites, structure, and contents for drafting "to-the point and easily understandable comment" are discussed in the succeeding four sub-sections viz. (A) Fundamental constituents of a comment (B) Classification of comments (C) Illustrative drafting of a comment and (D) Reporting of comments.

A. Fundamental constituents of a comment

Similar to the case of preparation of a draft paragraph based on the four C's (criteria, condition, cause and consequence), there are certain constituents of a comment, which need to be kept in mind while framing and drafting a "to-the point and easily understandable comment". However, it is noteworthy that a comment on AFSs is not a draft paragraph, hence, it should not be framed like a draft paragraph. Instances of framing a comment like a draft paragraph are sometimes seen while processing and finalising the draft comments. Hence, the drafting of a comment if required, should be modified at the stage of processing and finalising the draft comments. It is, therefore, necessary to know the fundamental constituents of a comment which help in framing its structure and contents. The fundamental constituents of a comment are enumerated as below:

(a) Application of Double Entry System: For framing the structure and contents of a comment, one should be aware of the fundamentals of the 'Double Entry System (DES)'which has been the universally accepted accounting system since long. The DES provides a fundamental principle that each accounting transaction has two distinct sides (Debit-'Dr' and Credit-'Cr') representing to a separate account/account code and forming an accounting equation which entails that 'Dr' always equals to 'Cr'. This accounting equation also provides that any increase/decrease in 'Dr' should carry an impact of parallel increase/decrease in 'Cr' or vice versa. The impact of this concomitant change in 'Dr' and 'Cr' is helpful in correctly pointing out the financial impact of any error/omission/misstatements/deficiencies in AFSs, which can be further simplified as below:

- **(i) Decrease in any 'Dr' account→ Increase in any other 'Dr' account or Decrease in any 'Cr' account**
- **(ii) Increase in any 'Dr' account→ Decrease in any other 'Dr' account or increase in any 'Cr' account**
- **(iii) Decrease in any 'Cr' account→ Increase in any other 'Cr' account or decrease in any 'Dr' account**
- **(iv) Increase in any 'Cr' account→ Decrease in any other 'Cr' account or increase in any 'Dr' account**

(b) Identification of accounting transaction: The DES and the accounting equation along with the concomitant change in 'Dr' and 'Cr' are applicable in case of an accounting transaction. Therefore, it is necessary to distinct clearly the accounting transactions from the disclosure of other facts in the AFSs, as no such impact of concomitant change in 'Dr' and 'Cr' can be pointed out under the category of "Comments on disclosure" discussed in the subsequent paragraph (Classification of comments).

(c) Identification of two heads of account: Once the accounting transaction is identified, it is necessary to understand the two distinct accounts-'Dr' and 'Cr' applied in the accounting transaction along with accuracy of their application as per the prescribed accounting principles. It is also necessary to identify the main/sub head of accounts relating to an accounting transaction, through the details of compilation and consolidation of different accounts as depicted in the Trial Balance, AFSs and the schedules/notes forming an integral part of the AFSs. The impacted two heads of account can further be designated as below:

- **(i) Direct head of accounts:** It indicates the error/omission/misstatement contained therein/emerged therefrom directly.
- **(ii) Indirect head of accounts:** It indicates the head of account being impacted indirectly due to any error/omission/misstatement in the direct head of account as per the concomitant change in the accounting equation discussed as above.

The aforesaid identification of heads of account (Direct and Indirect) is helpful in assigning reference/linkage to the correct head of accounts impacted due to any error/omission/misstatement, while drafting a comment.

(d) Depiction of financial impact of any error/omission/misstatement etc.: From the aforesaid discussion, it is evident that the financial impact of any error/omission/misstatement needs to be pointed to the related two heads of account. This impact can be ascertained as per the accounting equation and the concomitant change in 'Dr'/'Cr' as discussed above and be mentioned in terms of ‘understatement’ (decrease) or ‘overstatement’ (increase) of the impacted two heads of accounts in order of direct head of account and indirect head of account.

While stating the financial impact on the two heads of accounts also having a consequential impact on profitability, it needs to be mentioned as ‘understatement’ (decrease) or ‘overstatement’ (increase) of profit/surplus or loss/deficit. This impact can also be easily identified and pointed out correctly as per the accounting equation mentioned above.

(e) Framing the structure and contents of a comment: While framing the structure and contents of a comment, the fundamental facts applied in drafting viz. accuracy, brevity, clarity, and understandability should be borne in mind. Accordingly, the comment should be straightforward containing generally (i) linkage with the direct head of account from which the error/omission/misstatement emanates (ii) criteria and/or reference(reference can be of already disclosed facts in Notes to AFSs or errors/omissions/misstatements pointed out in the Statutory Auditors’ Report) which lead to identification of error/omission/misstatement (iii) brief of the underlying accounting issue/error (‘what wrong is done) (iv) period of occurrence of accounting issue/error (v) required accounting solution (what should have been done) (vi) financial impact of error/omission/misstatement on two heads of account (vii) consequential financial impact on profitability, in case of comments on profitability. (viii) impact on Statutory Auditors’ Report in case, an accounting issue/error already pointed out therein has been deficient and accordingly supplemented through further comment. Further, the structure and contents of a comment as per its type and nature are illustrated in the succeeding sub-section ‘Illustrative drafting of a comment’.

B. Classification of comments

For better appraisal of errors/misstatements/deficiencies, if any in the AFSs by the users/stakeholders, as pointed out by audit, the comments are classified into different categories as per their types and nature. Accordingly, these comments are presented in the CAG’s Certificate/SAR. Therefore, due care needs to be taken in correct classification of the comments at the stage of processing and finalising the draft comments on the AFSs. As per the prevalent instructions, the comments in respect of Supplementary audit and Sole Audit/SAR are classified and presented as follows:

(a) Classification of comments in respect of Supplementary audit:(i) comments on profitability (ii) comments on Financial Position (iii) comments on Cash Flow Statements (iv) comments on Statutory Auditors’ Report (v) comments on disclosure and (vi) Other comments.

(b) Classification of comments in respect of Sole Audit/SAR: (i) comments on Balance Sheet(ii) comments on Profit & Loss Account/Income and Expenditure Account (iii) comments on Receipt and Payment Account (iv) comments on accounting policies (v) General comments

While classifying the comment as per its type and nature, the following facts should also be kept in mind:

- Comments impacting the profitability directly or indirectly should be classified under Comments on Profitability/Profit & Loss Account/Income and Expenditure Account
- Comments exclusively impacting the financial position should be classified under Comments on Financial Position/Balance Sheet**.**
- Comments exclusively on Statutory Auditors' Report may have issues relating to form and structure of the Report, non-compliance with Standards on Auditing/Accounting Standards/other statutory requirements/CAG's directions/sub-directions etc. Further, there may be issues relating to the profitability/financial position/disclosure etc. deficiently pointed out by the Statutory Auditors in their Report, which need to be supplemented to by the CAG's comments. It is advisable that, to draw attention of the user/stakeholder of the AFSs, the issues having substantial impact on profitability and financial position should be classified under comments on profitability and financial position, as the case may be, after citing the appropriate reference of the para/comment as mentioned in the Statutory Auditors' Report.
- Comments on disclosure relate to disclosure issues relating to accounting policies, facts and figures depicted on the AFSs and related schedules/notes and other compliances with the requirement of act/regulations/rules/orders/circulars etc.

C. Illustrative drafting of a comment

Though there is no standardised format for drafting of a comment, through this article, efforts have been made to prepare and present an illustrative draft of a comment as per its type and nature, which is expected to be helpful in understanding and framing the structure and contents of a "to the point and easily understandable comment". As per the type and nature of the comment, the illustrative draft is mentioned as below:

(a) Comments on profitability

The comment should be straightforward and generally having a mention of inclusion/non-inclusion of amount in the direct head of account from which the comment emanates, Criteria/reference, brief of the accounting issue including period of occurrence, required rectification and financial impact on two heads of accounts with the consequential impact on profit/surplus or loss/deficit. The following illustrative template with the required modification may be useful, while drafting a comment on profitability.

Example: The above includes/wrongly includes/does not include an amount of Rs……A reference is invited to (Criteria/reference to be mentioned viz. Section/Rule/Order/Circular/Para of Accounting Standards/Para of Accounting policies/Notes to accounts/para of Statutory Auditors' Report etc.)………., which provides that………….Accordingly, the Company should have…….However, in contravention to the above….,the Company has …………………..

This resulted in overstatement/understatement of 'A' (direct head of account) and overstatement/understatement of 'B' (indirect head of account) with the consequential overstatement/understatement of profit/surplus or loss/deficit for the year by Rs.......

(b) Comments on financial position

Similarly, the comment on financial position should be straightforward and generally having a mention of inclusion/non-inclusion of amount in the direct head of account from which the comment emanates, Criteria/reference, brief of the accounting issue including period of occurrence, required rectification and financial impact on two heads of accounts. The following illustrative template with the required modification may be useful, while drafting a comment on financial position.

Example: The above includes/wrongly includes/does not include an amount of Rs……A reference is invited to (Criteria/reference to be mentioned viz. Section/Rule/Order/Circular/Para of Accounting Standards/Para of Accounting policies/Notes to accounts/para of Statutory Auditors' Report etc.)…….., which provides that………….Accordingly, the Company should have…….However, in contravention to the above….,the Company has …………………..

This resulted in overstatement/understatement of 'A' (direct head of account) and overstatement/understatement of 'B' (indirect head of account) by Rs.....

(c) Comments on Cash Flow Statement

Such comments relate specifically to Cash Flow Statement (CFS), which can be in terms of non-compliance of the accounting standards and/or depiction of incorrect figures in the CFS thereby adjusting some other related figures just to arrive at the similar balance of Cash and Cash Equivalents through the CFS as depicted in the Statement of Financial Position/Balance Sheet. To detect such types of errors in CFS, the bank balances as per Ledger and Bank statements along with Bank Reconciliation Statements and third-party report etc. as on the Balance Sheet date are required to be reviewed thoroughly besides a review of the interrelated figures of Statement of Profit and Loss Account and Statement of Financial Position as brought out in the CFS.

Accordingly, the comment on CFS should be straightforward and generally having a mention of non/incorrect depiction of figures under the particular item of CFS, Criteria/reference, brief of the accounting issue including period of occurrence, required rectification and financial impact on the related items of CFS. The following illustrative template with the required modification may be useful, while drafting a comment on CFS.

Example: The above (name of item of CFS) does not include/wrongly includes an amount of Rs……A reference is invited to (Criteria/reference to be mentioned viz. Section/Rule/Order/Circular/Para of Accounting Standards/Para of Accounting policies/Notes to accounts/para of Statutory Auditors' Report etc.)…….., which provides that………….Accordingly, the Company should have…….However, in contravention to the above….,the Company has …………………..

This resulted in overstatement/understatement of 'A' (mention the directly related item of CFS) and overstatement/understatement of 'B' (mention the indirectly related item of CFS) by Rs.......Further, the Cash and Cash Equivalents depicted in the CFS do not flow automatically and have been incorrectly adjusted to match the same depicted in the Statement of Financial Position.

(d) Comments on Statutory Auditors' Report

A comment exclusively related to Statutory Auditors' Report should be straightforward and having reference of the particular para of the Report, Criteria reference (standards on auditing/accounting standards/statutory requirements/CAG's directions/sub-directions), brief of the reporting issue, impact on report etc. Further, comment having substantial financial impact on profitability and financial position pointed out deficiently by the Statutory Auditors, which needs to be supplemented to by the CAG's comments, should be drafted as illustrated in case of comments on profitability and financial position. Therefore, the comment exclusively related to Statutory Auditors' Report has been illustrated as under:

Example: A reference is invited to Para no. of the Statutory/Independent Auditors' Report, which states that ………………….As per Section/Rule/Order/Circular/Para of Accounting Standards/Para of Auditing Standards/ Para of Accounting policies/Notes to accounts, the Independent Auditors should have pointed out…….., which was incorrectly/not done by them. Therefore, the Statutory/Independent Auditors' Report is deficient to the above extent.

Comments on disclosure

A comment on disclosure should be straightforward and having: Reference of the para of disclosure i.e. accounting policies or notes to accounts, para of Statutory Auditors' Report etc. (in case the existing disclosure is deficient), Criteria reference for disclosure (in case of non-disclosure), brief facts of disclosure, impact of deficient/non-disclosure.

Example: A reference is invited to Para no. of accounting policy/notes to accounts/para of Statutory Auditors' Report/Section/Rule/Order/Circular, which states that……………..However, the Company has not disclosed the facts regarding ……………Therefore, the accounting policies/notes to accounts are deficient to that extent.

Other comments

These include general comments (which do not fall under Comments on Profitability, Financial Position, Cash Flow Statement, Statutory Auditors' Report and Disclosure) regarding non-compliances with the provisions of the companies act/other legal/statutory requirements viz. totaling error, language/grammatical error, non-holding of required number of meetings of the BOD, non-preparation of Directors' Report/Annual Report, non-appointment of full time Company Secretary and non-filing of Annual Return with the Registrar of Companies, etc.

There is no standardised format for drafting the comments. However, a comment should be straightforward and having: Reference of Criteria, brief of the case, impact of non-compliance.

Example: As per Section ………….of the Companies Act, 2013, the Company is required to hold four meetings of the Board of Directors (BOD) during a financial year. However, the Company has held only two meeting of the BOD during the year……….This resulted in non-compliance with the aforesaid provisions of the Companies Act, which also attract ……………………….under Section…….of the above Act.

D. Reporting the comments

The comments on the AFSs, after their processing and finalisation, are to be reported to the concerned company/entity through the prescribed 'Certificate' and SAR in case of supplementary audit and Sole audit respectively for their onwards submission before the competent authority (Board/Governing body), and State Legislature (in case of SAR). Therefore, reporting of final comments on the AFSs is a very important task being handled with due care and attention by the Accounts Processing Section (APS)/Accounts Processing Officer (APO) in the concerned field office as well as CAG

HQ. While processing, finalising and reporting the comments on AFSs, the following important points should be kept in mind:

- **Observance of timeliness**: Finalisation of comments within **60 days** as prescribed under Section 143 (6) of the Companies Act, 2013 and that prescribed in the CAG's Manual of Instructions for Audit of Autonomous Bodies, in case of Sole Audit/preparation of SAR.
- **Use of the correct format of certificate**, as prescribed by the CAG HQ for different cases, viz. Supplementary audit-(Standalone Financial Statements, Consolidated Financial Statements); and Comprehensive Audit i.e. preparation of the Separate Audit Report (SAR) viz. issue of comments, issue of Nil comment, revision of accounts at the instance of audit, revision of Statutory Auditors' Report at the instance of Audit and issue of Non-review certificate (NRC) etc.
- To ensure that exact, accurate and straightforward comments are issued, the APS/APO should carefully examine the proposed comments with reference to criteria/non-compliances, classification, materiality (value of individual comment equal to or exceeding 2% of Net profit/loss or line item of Balance Sheet or aggregate value of comments on P/L Account or Balance Sheet equal to or exceeding 3% of Net profit/loss or net assets/liabilities), sufficient supporting evidence/documents, and drafting of the comments
- The APS/APO should ensure that uniformity and consistency should not be compromised in case of similar nature of comments
- The APS/APO should ensure that True and fair view given by the Statutory Auditors is challenged in case (i) profit is converted into loss and vice versa or (ii) the value of aggregate comments of CAG and the Statutory Auditors on profitability exceeds 20 percent of the net profit/loss or (iii) those on Financial position exceeds 10 percent of total assets/liabilities, as per the prevalent instructions
- Prior to issue of the final comments to the concerned company/entity, the APS/APO in the concerned field offices should, on receipt of the approved comments from the CAG HQ, carefully re-examine the facts and figures of these comments to rectify the discrepancies, if any under intimation to APS/APO of CAG HQ.

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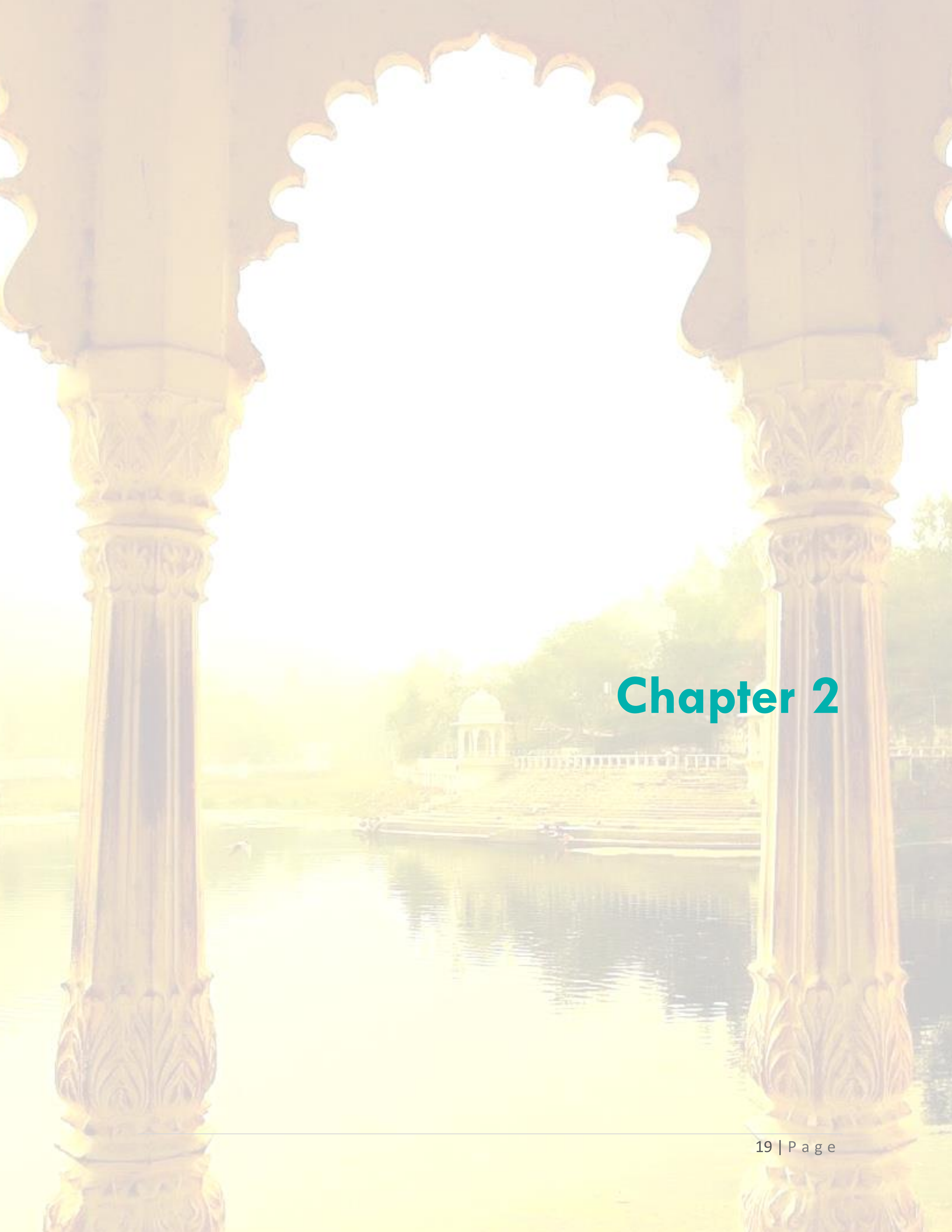

Chapter 2

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Auditing Financial Reporting practices in Government Accounts- Part I

(To raise pertinent comments on classification of transactions in government accounts, an auditor should examine transactions in government accounts in the light of form of accounts and rules prescribed for classification of transactions. This article, is intended as a series of such articles and touches on some of the important rules of classification and then discusses an approach to audit the use of minor head 800)

Introduction

1. The Union / State Finance Audit Report has a chapter on Financial Reporting practices[1] which includes audit observations on classification of expenditure / receipts in government accounts. These observations cover a variety of issues such as use of the minor head 800; outstanding balances under suspense and remittance heads; balances under personal deposit accounts; use of AC/DC bills amongst others.

2. In this article, we list some key rules dealing with classification of transactions in government accounts needed for audit and then review audit comments on use of the minor head 800 in accounts and suggest a possible standard way forward to follow up issues and recommendations being presently raised in audit.

The form of accounts and rules of classification in Government Accounts.

3. Any audit observation on classification of transactions must arise from the principles, rules and practices laid down for classification of transactions in government accounts. Therefore, prior to auditing classification of transactions in accounts it is worthwhile to study the prescribed framework of classification.

Constitution of India

4. Article 150 of the Constitution states that the form of accounts of the Union and of the States shall be as prescribed by the President on advice of the Comptroller and Auditor General of India.

Government Accounting Rules

5. In discharge of powers under Article 150, the President has notified, in consultation with the CAG, Government Accounting Rules 1990. These rules

[1] Chapter 4 'Quality of Accounts and Financial reporting practices' in the new guide to preparing State Finance Audit Report)

describe the Form of Accounts and the rules governing classification of transactions in Government accounts. Some key rules are given below in brief:

6. **Rule 28**: the word "Form" used under Article 150 has a comprehensive meaning so as to include the prescription not only of the broad form in which the accounts are to be kept but also the basis for selecting appropriate heads under which the transactions are to be classified".
7. **Rule 26** describes the structure of accounts. The rule states that the main unit of classification in the accounts shall be the Major Head which is further divided into minor heads which are further divided into sub-heads which in turn are divided into detailed heads. Sometimes the Major heads may be divided into sub major heads prior to division into Minor heads.
8. The same rule also explains what the units of classification represent. The Major head corresponds to the functions of the government such as Crop Husbandry, or Defense Services. The Minor heads subordinate to them represent programs undertaken to achieve the objectives of the function. The subheads correspond to the activities or schemes undertaken as a part of the program.

The List of Major and Minor heads of Accounts of the Union and the States

9. The detailed structure of accounts upto Minor heads is given in the List of Major Heads of Account of the Union and States (LMMH). The General Directions and the foot notes associated with various Major/Minor heads provide guidance on practices to be followed for classification of transactions under various Major and Minor heads. This guidance sometimes also includes instructions on the sub heads to be opened below the minor heads to accommodate transactions that arise under the specified minor heads.
10. Both the Government Accounting Rules and the LMMH (and general directions included therein) have been made in consultation with CAG. These can be modified only through issue of formal correction slips[2]. No new Minor heads can be opened under any major head except some specified ones[3] as described in the LMMH. The minor head 800-other expenditure is one such minor head along with several other minor heads such as 500 – receipts awaiting transfer; 798- International Cooperation etc.; these minor heads can be opened under any major head as required without any prior permission. The general directions to LMMH contain a comprehensive list of such minor heads and the instructions regarding their use.

[2] To make alterations / additions to the List of Major & Minor heads of the Union and States a formal correction slip thereto is issued by the Controller General of Accounts. Prior to the issue of the correction slip the concurrence of the budget division MoF GoI and the CAG must be obtained.

[3] Refer to General Directions to the List of Major & Minor heads of the Union and States

Understanding usage of Minor head 800 and relooking audit comments thereon.

11.The general directions (Para 2.3) in the LMMH provide that "the Minor head 800-other receipts may be opened under receipts major / sub major heads, wherever it has not been provided. Similar is the case for expenditure heads as provided for by general directions para 3.1(b). The same minor head can also be opened in the capital section and the loans and advances section of government accounts.

12. The Minor head 800 is already available under some of the major heads in the List of Major and Minor heads of accounts of the Union and the States and can be opened under others if needed. This head is used for recording receipts / expenditure that cannot be classified under any of the listed minor heads under a given major head.

13. **Further, the LMMH and GAR 1990[4] specify that certain transactions are required to be booked under the head 800- Other receipts/ Other Expenditure.** For example, the LMMH specifies that receipts on account of leave salary contribution, as also receipts from sale proceeds of deadstock, waste-paper and other articles, the cost of which was met from office expenses should be classified under Minor Head 800-Other Receipts under any receipt major head where such a receipt is to be recorded. **Similarly, for expenditure, the LMMH specifies that** under the major head 2405 expenditure on relief and welfare schemes of fishermen should be booked under minor head 800- other expenditure. The above two examples are illustrative and not exhaustive.

Classifying transactions in accounts[5]

14. To ensure that transactions have been booked to the correct head of account, first the appropriate major head is to be chosen, thereafter the most appropriate minor head listed under the chosen[6] major head and so on. At the minor head level if none of the listed minor heads appear appropriate, then the choice falls between standard minor heads (mentioned in paras) or the minor head 800- other receipt/ expenditure. If the rules (GAR 1990/ LMMH) specify that the minor head 800- Other receipt/ expenditure should be used for booking the transaction, then the head 800 must be used.

15. Other than this no other choice exists, no new minor head can be opened even for the purpose of improving depiction.

[4] E.g. see Rule 72(ii)
[5] Discussion limited to classification upto minor head which is the level represented in the Annual Accounts and also the subject of the audit observation under discussion.
[6] In actual practice this has to be done at the time of budget formulation.

A review of audit comments on the use of minor head 800

16. Review of 19[7] reports throw up three broad observations (a) the minor head 800 is to be used **only if** appropriate minor head is not provided; (b) the usage renders accounts opaque/nontransparent and such accounts lack disaggregated information on specific activities/ schemes/ programs which affects position of financial reporting; (c) classification under this head distorts proper analysis of allocative priorities and quality of expenditure.

17. The departmental guidance on preparing comment on the use of the minor head 800 requires that auditors check if the expenditure being commented upon can be booked under one of the existing other minor heads. A close consideration of the forgoing discussion under paragraphs 3 to 14 would show that only admissible comment is of misclassification and to establish it the auditor would have to also indicate the relevant minor head of account that should have been used. Such a practice is common in audit of commercial accounts.

18. Further, as annual accounts are prepared at minor head level they represent expenditure at the program level and so even without use of minor head 800 they would lack information on specific activities / schemes which are represented by accounting classifications below the minor head levels.

19. The crux of the problem lies in the quantum of expenditure being booked under the minor head 800. This is because annual accounts of the Union as well as states have several detailed statements which provide information upto minor head level in the accounts, even though Rule 26 of the GAR declares that the main unit of classification in accounts is the major head. This creates a problem of presentation as in many cases large percentages of expenditure on functions of Government (major heads) are shown as "other expenditure."

20. Excessive booking under 800 can happen primarily in two ways:

i) In India, classification in the accounts, follows the classification in the budget. Therefore, if in the detailed demands for grants, outlays are made against the minor head 800, the bookings in the accounts too shall then come under the same head. In this case there is no error of booking of expenditure.

ii) The expenditure is booked to the head 800 erroneously. This should get detected and rectified at some stage of the accounting/ auditing process under various checks and reviews prescribed for ensuring accuracy of accounts, provided they are adhered to with necessary due diligence.

[7] Telangana, Chhattisgarh, Odisha, Jharkhand, Bihar, Mizoram, Arunachal Pradesh, Assam, Meghalaya, Uttarakhand, Uttar Pradesh, Haryana, Punjab, Jammu & Kashmir, Kerala, Karnataka, Goa, Gujarat, Rajasthan

21. Let us examine in detail a case that falls in the former category, namely where the initial outlay in the budget is under minor head 800. The expenditure under Rastriya Krishi Vikas Yojana (RKVY) falls in this category. Examination of the detailed demand for grants of the Union and of a few states shows that outlays for RKVY made under 2401- Crop Husbandry are made at sub-head level under the minor head 800 – Other Expenditure.

22. To form a view on whether a case could be made for use of a minor head other than 800 for booking expenditure under RKVY let us examine the nature of expenditure being sanctioned under this scheme. State Level Sanctioning Committee meeting minutes were studied to determine the nature of projects being sanctioned under RKVY (for the major head crop husbandry). It was observed that the approved projects included among others:

i) Distribution of fruit saplings and vegetable seedling kits

ii) Procurement of machinery and equipment for setting up a biofertilizer and bio pesticide production unit

iii) Custom hiring centers for agricultural equipment

iv) Distribution of certified seeds

v) Strengthening fertilizer quality control

vi) Setting up vermicompost / organic compost units in departmental farms

vii) Conversion of departmental farms to organic demonstration farms.

23. There are 19 minor heads under the major head 2401 – Crop husbandry and 12 minor heads under the major head 4401 – Capital outlay on Crop Husbandry:

Some of these are:

a) 103 - Seeds,
(this minor head also records expenditure on seed farms);
b) 104 - Agricultural farms,
(this minor head includes expenditure on commercial farms and experimental farms other than seed farms);
c) 105 – Manures and fertilizers
d) 119 – Horticulture and vegetable crops,
(this minor head includes expenditure on schemes relating to fruits, vegetables, Nurseries, Kitchen gardens and Orchards, and suitable sub-heads for individual scheme or a group of schemes may be opened, with appropriate grouping under "Fruits", "Vegetables" and "Nursery".)

24. An examination of the nature of projects undertaken under RKVY and the classification heads available under Crop Husbandry / Capital outlay on Crop Husbandry prima facie suggests that some projects undertaken under the scheme

could be classified under some minor heads other than 800 under 2401 Crop Husbandry. For example, expenses on distribution of certified seeds can be booked under the minor head 103- Seeds under 2401 rather than 800 – other expenditure.

25. However, these bookings are appearing under 800 - other expenditure as outlay has been made under that minor head in the budget documents. As accounts follow the budget, therefore so long as the RKVY of any other such program is classified in the budget under the minor head 800 it will continue to appear under 800 (in fact it would be required to appear there) audit observation notwithstanding.

26. The issue can be resolved by initiating action as prescribed under MSO(A&E) volume I, note under para 3.4, by advising the state of alternate heads of account to be used in the budget for classifying the schemes for better understanding of the legislature and ensuring conformity with the form of accounts.

27. However, a word of caution is appropriate at this stage, the list of major and minor heads is the same for the union and all the states and so if advice to use alternate heads for programs such as RKVY or for other purposes is to be issued, it had to be done centrally by the CAG's office after review of case and due discussions with all stakeholders[8].

How to audit

28. Based on the above discussion a simple step by step audit procedure is discussed for identifying cases that fall under category mentioned in para 20(ii) above for comment in SFAR chapter four.

i) Identify major heads with large expenditures (say over 20 per cent[9]) booked under the minor head 800 from the accounts.

ii) review the detailed demand for grants where these major heads figure and identify the lines where budget outlay is made under the minor head 800. Identify the schemes and activities being funded.

iii) Review the nature of the schemes and activities. For this purpose, the scheme guidelines, sanction orders, project sanctioning and monitoring committee meeting minutes can be studied.

iv) Based on the review above, examine if the use of the minor head 800 for booking expenditure is mandated by the GAR 1990 or the LMMH. If not, then examine other minor heads under the given major head to see if their use for booking the expenditure would be more appropriate.

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[8] CGA; Budget Division, MoF GoI; and State Governments

[9] The percentage mentioned has been adopted for the sake of explanation.

v) This exercise should be repeated for all major heads identified in i) above. Thereafter the matter should be taken up with the Finance Department and the other concerned departments. A final view can be taken after receipt of the government response and the matter reported appropriately in SFAR.

vi) In case, the state agrees to change the head used, its impact on uniformity of classification (comparability of accounts) across the states and union should also be considered in consultation with the headquarters.

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