CHAPTER 3
SOCIAL AUDIT & SIMILAR PROVISIONS UNDER INDIAN COMPANIES ACT

SOCIAL AUDIT

Bowen first initiated social Audit in 1953 as a report of social performance was to voluntarily undertaken by the concern itself. Its main object was to serve for the satisfaction of society. Social Audit is related to the examination of Companies Social Activities. It Analyses various social costs and social benefits. This Audit tries to appraise the performance of a business concern from the social angle. The resources put at the disposal of business concern in fact belong to the society and as such must be used for the optimal social good. Conceptually, social audit is a scientific and sophisticated technique of testing the truth of social performance of tourism industry with reference to its objectives and means by an independent authority.

Social Audit is nothing more than a reaction to the spirit of social irresponsibility. In social audit is measured, how successful business enterprise has been fulfilling its social responsibility. By Social Audit techniques, efforts are made to measure the contribution an enterprise makes to society.\(^\text{15}\)

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\(^{15}\) According to Chales: Mcdowar, “Social audit angues That the people, mus be allowed to know about the decision making done in their name and must then be allowed to play the utmost part in controlling their lives.
Social Audit is a systematic study and evaluation of an organisation’s social performance. It is concerned with possible influences on the social quality of life. Social Audit is commitment to undertake systematic assessment of the reporting of corporate activities, which have a social impact.

Further, it has been rightly pointed out “The concept of Social Audit is a vision that at some further time the corporation will assess their social performance in a systematic manner as they now assess their financial performance. Furthermore the evaluation of socio-economic effect from any business, companies, enterprise, Govt. Policies etc. is called Social Audit. Social Auditing as suggested by Parwal is often equated with the use of independent auditing firms to verify records of social performance.”

Social Audit is a logical response to the concept of social responsibility of business. Therefore, social audit provides an objective assessment as to how an economic entity has been able to discharge its social obligations in the course of its operations. It is an answer to social accountability rather than providing a system of audit of social accounts.

The Social Audit is neither statutory audit nor performance audit, but it is the mixture of both. Therefore, in nutshell, the social audit is more

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16 N. J. Yassasway :-“Social Audit as an audit of Social Costs. Caused by an organisation and social benefits generated by it.”
than such traditional audits and new emerging dimensions in audit literature\textsuperscript{17}.

**AUDIT UNDER SECTION 227 (4A) RELATING TO MANUFACTURING AND OTHER COMPANIES:**

The accounts and audit of a Company in India Governed by the Companies Act 1956 section 227(2) of the Companies Act. Provides that the auditor shall make a report to the members of the companies on the accounts examined by him in a prescribed form to that he has obtained required information & explanation proper books of accounts have been maintained accounts are in agreement with the books of accounts and sections, and the said accounts give a true and fair view. In case of the balance sheet of the state of the company’s affairs as at the end of the financial year the phrase “true and fair” was inserted in the Companies Act 1956 in the place of the phrase”. “True and correct” used previously. This was primarily because the term “true and correct” could be interpreted in different ways. Some accountant urged that “true and correct” implied that the financial statements were arithmetically correct. They corresponding to the figures in the books of accounts but did not specifically mean that the financial statements were arithmetically correct and that they corresponded to the figures in the books of accounts but did not specifically mean that the financial statements represented the actual state of affairs and the actual working results.

\textsuperscript{17} Dr. Agarwal observed : “Social Audit or distinguish from financial audit is such an audit in which social performance is analysed to know whether, the activity of an entity have affected the society, positively and negatively.”
Again, in 1965 the Companies Act was amended and additional responsibilities were cost on the auditor to enquire into the adequacy of security in the case of loans given, prejudicial books entries, sale, prices of investments sold etc. If on the enquiry auditor is not satisfied with regard to any of these matters, he is required to comment in his report to the shareholders. In cause of time, this was also found to be inadequate the prevailing view is that the Auditor’s Report should be very comprehensive and should touch upon some of the managerial performance. It has now been widely recognized that the principal processes and procedures so far in vague has been conventional, emphasis has been mainly on financial audit whose purpose is to see whether expenditure incurred has been properly recorded and income and position statement represent a true and fair picture of the concern as a whole in financial times. Since the evaluation of professional management and because emphasis on operational rationality in managing Men, Materials, Machine and Money this emphasis has been shifted from financial administration to the achievement of maximum output with minimum cost. Audit is no longer confined to checking and verification of financial transactions, but also has expanded to the appraisal and evaluation of results occurring to society from expenditure incurred to recognize this statutorily the Government, therefore, exercised its power under sub section 4A of section 227 of the Indian Companies Act, 1956.

Under section 227 (4A) of the Indian Companies Act 1956 the Central Government has the power to direct by general or special as may be specified in the order. The Government may also specify the clauses of
the companies for this purpose. Before making any such order, the Central Government may, if it considers it necessary or expedient to do so. Consult the Institute of Chartered Account of India in accordance with the power. Confirmed under section 227 (4A). The Central Government issued “the manufacturing and other companies (Auditor’s Report) order 1975 directing the auditor to include in his report a statement on various matters specified in the order.

In order to provide guidelines to the auditors the institute of Chartered Accountant of India issued a statement in 1977 containing certain suggestions and clarification on the order issued Under Section 227 (4A). The statement issued by the institute is neither exhaustive nor mandatory it is simply to provide general guiding rules to be adopted in specific circumstances or case.

The order under section 227 (4B) supplements the existing provisions regarding the audit report in case of specified companies. However, it should be noted that under the provisions of the order, the auditor is required to enquire into certain matters and report only if he thinks it necessary to make a comment. The provisions of the order are in addition to the direction issued by controller and auditor general under Section 619 of the Companies Act 1956.

**THE MANUFACTURING AND OTHER COMPANIES (AUDITOR’S REPORT) ORDER 1975:**

Under sub – section 4A of section 227 of the Companies Act 1956 (1 of 1956), the company Law Board issued the manufacturing and other Companies (Auditor’s Report) Order, 1975. This order is applicable to
every company, which is engaged in one or more of the following activity namely:-

a. Manufacturing, mining or processing

b. Supply and sending services

c. Trading and

d. The business of financing investment, chit fund, Nidhi or mutual benefits societies

This Order comes into force from 1st Jan. 1976

MANUFACTURING COMPANY:-

Manufacturing Company means a Company engaged in any manufacturing process as defined in the Factories Act 1948. (63 of 1948)

MINING COMPANY:-

Mining Companies means a Company swings a mine and includes a Company which carries on the business of a mine either as a lessee or occupier thereof.

PROCESSING COMPANY:-

Processing Company means a Company engaged in the business of processing materials with a view to it use, sale, delivery or disposal.
SERVICE COMPANY:-

Service Company means a Company engaged in the business of supplying, providing, maintaining and operating any service, facilities, convenience and like for the benefit of others.

TRADING COMPANY:-

Trading Company means a Company engaged in the business of buying and selling goods.

FINANCING COMPANY:-

Finance Company means a Company engaged in the business of financing whether by making loans or advances or otherwise of any industry, commerce or agriculture and includes any company engaged in the business of hire purchase and of financing of housing.

INVESTMENT COMPANY:-

Investment Company means a Company engaged in the business of acquisition and holding, or dealing in shares, stocks, bonds, debentures, stocks or securities issued by the control or any other state government or by the local authority or in other market-able securities of alike nature.
CHIT FUND ‘NIDHI’ OR MUTUAL BENEFITS:-

Chit fund ‘NIDHI’ or Mutual benefit Company means a Company engaged in the business of managing, conducting or supervising as a supervisor or agent of any transaction. Alternatively, arrangement by which it enters into an agreement with a number of subscribes that every one of them shall subscribe a certain sum of installments for a definite period. That each subscribe in his turn as determined by lot or auction or by tender or in such other manner as may be provided for in the agreement shall be entitled to a prize amount, and included companies whose principles business is accepting fixed deposits from its members and lending money to them.

The main object of this order is to ensure that the social objective of the company audit is achieved in a greater measure, considering the basic facts that under modern conditions. Companies have to sub serve public interest rather than purely private gains of the investors.

Every report made by the auditors under sec. 227 of Companies Act 1956 (1 of 1956) on the account of every company. Examined by him to whom this order applies for every financial year ending any day on or of the commencement of this order shall contain the matters specified in the order. The matters specified in the order for various classes of companies are as under:-
THE MATTERS TO BE INCLUDED IN THE AUDITOR’S REPORT:-

The auditor’s report because of the companies to which this order applied shall includes a statement on the following matters namely.

(a) In case of Manufacturing, mining or processing company:-

i) Whether the company has maintained proper records to show full particulars including, quantitative, details and situations of fixed assets, whether the management has physically verified these fixed assets and if serious discrepancies were noticed on such verification whether the same have been properly dealt with in the books of account.

What are proper records has not been specified in general the seconds should contain the particulars in respect of all the fixed assets i.e. sufficient description, classification, location quantity rate of depreciation etc. The relevant details may not be acquired prior to 1 April 1956 in fact even schedule VI to the act provides that where the original cost cannot be ascertained. The book value as at 1 April 1956 may be considered as cost. The auditor should examine whether the method of verification was reasonable in the circumstances relating to each asset.

ii) Whether any of the fixed assets have been revalued during the year the basis of revaluation should be indicated.

The auditor is required to report whether any of the fixed asset have been revalued during the year. In case a revaluation has taken place, the auditor should examine the basis of revaluation
of fixed assets is by appraisal, normally undertaken by the competent values.

It may be noted in this connection that adjustment made to the book value of fixed assets consequent on adjustment in the figures of the liabilities in the foreign exchange does not amount to revaluation of the assets but is only an adjustment to the cost of assets.

iii) Whether physical verification has been conducted by the management at reasonable intervals in respect of finished goods, stores, spare parts and raw material. [Paragraph 4 (A) (iii)]

Physical verification of stocks is the responsibility of management of the company, which should verify that all material items at least ones in a year and more often in appropriate cases. It may be useful for the company to determine the frequency of verification by ABC classification of stocks. A category items being verified more frequently than B category and the later more frequently than C category items.

iv) Are the procedures of physical verification of stocks followed by the management reasonable and adequate in relation to the size of the company and the nature of its business if not the inadequacies in such procedures should be reported. [Paragraph 4 (A) (IV)].
This clause requires the auditors to comment on the reasonableness and adequacy of the stock verification procedures allowed by the management of the company. In case the procedure of physical verification of stock in the opinion of the auditor, are not reasonable and adequate in relation to the size of the company and the nature of the business he has to report about the inadequacies also.

v) Whether any material discrepancies have been noticed a physical verification of stocks as compared to books records and if so, whether the same have been properly dealt with in the books of accounts.

[Paragraph 4(A) (V)]

The order requires the auditor to examine if significant discrepancies have been noticed on verification of stock. When compared with books records such an examination is possible when quantity records are maintained sometimes companies have not maintained day-to-day records. In that case, the auditor will have to report that he is unable to determine the discrepancy if any a physical verification for the terms or class of items to be specified.

vi) Whether the auditor based on his examination of stocks, is satisfied that such valuation is fair and proper in accordance with the normally accepted accounting principles is the basic of
valuation of stocks same as in the proceeding year. If there is any derivation based on valuation, the effect of such derivation, if material should be reported. [Paragraph 4A]

The clause requires to auditor report whether he is satisfied based on his examination of stocks, that valuation is fair and proper in accordance to accounting standard 2(As-2) valuation of inventory issued by the institute. The auditor is also required to report whether the basis of valuation of stocks is the same as in the preceding years. In case of any deviation the auditor has to report the effect of such deviation if material the accounting standard 5 (AS-5) stated that the prior period and extra ordinary items and changes in accounting politics provides that any change in an accounting policy, which has a material effect in a state period, should be disclosed. It may be noted that the examination envisaged under this clause would cover records pertaining to works in progress also.

vii) If the company has taken any loans, secured or unsecured from companies firms or other parties listed in the register maintained under sec. 301 and 370 (ic) of the Companies Act 1956 (1 of 1956) whether the rate of interest and the terms and conditions of such loans are prime facie prejudicial to the interest of the company.

This clause requires the auditor to comment on the rate of interest and other terms and conditions of loans taken by the company from the above-specified clauses. When company has
not maintained proper records under section 301, the auditor should obtain the necessary information from the management of the company. While reporting on this clause the auditor should clearly mention the fact of improper maintenance of the previously mentioned register. The auditor should obtain from the management a list of companies under the same management as defined under section 370 (1B) of the Act. The auditor’s duty is to determine whether in his opinion the rate of interest and other terms and conditions of the loans are prima facie prejudicial to the interest of the company.

If the auditor finds that better terms could have been obtained he would be well advised to obtain the company’s explanation in writing as to why the company considers that the terms obtained are not prejudicial to the interest of the company. If the auditor does not find satisfactory explanation, it will be necessary to him to state that the terms obtained by the company have been prejudicial to its interest.

viii) If the Company has granted any loans, secured or unsecured loans to companies, firms or other parties listed in the register maintained under sec. 301 and or to the companies under the same management as defined under subsection (1B) of section 370 of the companies act, 1956 (1 of 1956). Whether the rate of interest and other terms and conditions of such loans are prima
facie prejudicial to the interest of the company [Paragraph 4(A) viii]

This clause requires the auditors to comment on the rate of interest and other terms and conditions of loan granted by company to the above-specified clauses c. This clause is similar to previous clause except, that where is this clause covers, loans granted by the company that clause covers loans taken by company from specified parties. Therefore, the previous comments would apply here also. In this clause the auditor, also inquire whether loans and advances made by the company based on the security have been properly secured, whether the terms on which they have been made properly secured, and whether the terms on which they have been made are not prejudicial to the interest of the company or its members. The auditor’s inquiry under the previously mentioned clause may also be useful for reporting under this clause.

ix) Whether the parties to whom the loans or advances in the nature of loans have been given by the company are repaying the principal amounts as stipulated and are also regular in payment of the interest and if not, whether reasonable steps have been taken by the company for recovery of the principal and interest.

The enquiry by the auditor falls into two parts. First whether the repayment of loan and payment of interest are being made as stipulated and secondly whether in the absence of regular
repayment of loan and the payment of interest reasonable steps have been taken for recovery. The auditor has to examine whether the payment of interest is regular. The word regular means interest should be paid when it falls due or immediately thereafter, where no stipulation has been made for the repayment of the loan or the payment of the interest or both. The auditor should state that fact that he has not made any comment because the terms of repayment and/or interest have not been specified.

Where the repayment of loan is not made or stipulated or where interest is not paid regularly. The auditor has to examine the steps if any and ask the management to give in writing the steps, which have been taken the auditor should arrive at his opinion only of the consideration of management & representation.

x) Is there an adequate internal control procedure commensurate with the size of the company and the nature of its business for the purchase of stores, raw material including company’s plant and machinery, equipment and other assets?

The system of internal control is the plan of organization and all the methods and procedures adopted by the management of an entity to assist in achieving management objective of ensuring as far as practicable the orderly and efficient conducting of business.
There are a number of methods, by which the system of internal control can be studied and evaluated. The auditor is free to select any one or more of the methods, which considers the best suited to the circumstances of the case. In making the evaluation, the auditors has to give due regard not merely to the size of the company and the nature of its business but also to the organizational structure.

xi) Where any stores, raw material of components exceeding Rs. 10,000 in value for each type thereof are purchased during the year from the subsidiaries, firms or companies or other parties in which directors are interested, whether the prices, paid for such items are reasonable or compared to the prices of similar items supplied by other parties.

This clause is however, of a much wider impact and covers transactions of purchase of goods & materials and sale of goods, materials and services goods and materials would include finished goods. However, this clause does not cover transactions of purchases of services.

The limit of Rs. 50,000/- has to be applied to the aggregate of the transactions of purchase of goods and materials and sale of goods, materials and services the auditor has to examine. Whether the
prices paid for the transactions purchases and sale examined by him are reasonable and having regard to the prevailing market prices or the prices at which transactions for similar goods and services have been made within other parties.

xii) Whether any unserviceable or damaged stores and raw material are determined and whether provision for the loss, if any has been made in the accounts. [Paragraph 4(A) xii)]

This clause is covers raw materials stores and finished goods but does not include work in process for the purpose of this clause, the term ‘stores’ should be deemed to include spares. The order does not require the auditor to examine whether the stock of stores, raw materials and finished goods is excessive to normal requirements. However, excessive stocks may indicate unserviceable or damages when further purchase were being made and inventory levels are going up. The auditor is requires to satisfy himself that adequate provisions have been made for the loss arising an account of unserviceable or damaged stores, raw materials and finished goods.

xiii) In case the company has accepted deposits from the public whether the directives issued by the Reserve Bank of India and the Provisions of Sections 58 of the Companies Act 1956 and the rules framed under, wherever applicable have been complied with.
The auditor has to examine whether compliance has been made with regard to all the matters specified in the rules and not merely to the limits of the deposits. The auditor is also required to report about the nature of contraventions in case the company has not complied with the relevant directions of the Reserve Bank of India or the Provisions of Section 58 A of the Companies Act 1956 and the rules framed these under.

xiv) Is the company maintaining reasonable records for the sale and disposal of realizable by products and scraps where applicable and significant?

In this clause, the term disposal seems to imply that the auditor has to report about the maintenance of records even of those by products and / or scrap, which are consumed internally. The examination by the auditor covers both by products and by scrap. By products represents products whose manufacture results incidentally from the manufacture of the main product or where the waste arising in the manufacturing of a main product is further processed to create a by – product. It is important that the auditor is responsible to check those by products and scrap which are realizable.

Whether an item of Expenditure is of the nature of personal expenses of the employees and/or directors in normal and is recognized by the department of company, affairs and other
authorities. The charging of such expenses to revenue account either based on contractual obligations or in accordance with generally accepted business practices is normal and does not call for any comment by the auditor. Where however such expenses are not cared by contractual obligation and are changed to revenue account, the auditor should report there on.

(xx) Where the company is sick, industrial company with the meaning of clause (o) of sub section (1) of section 3 of the sick Industrial Companies (Special Provisional Act 1985 (1 of 1986)). If yes, whether reference has been made to the Board for Industrial and financial Reconstruction under section 15 of that Act [Paragraph 4(A) (xx)].

In this clause the sick Industrial Companies means an industrial Company which has at the end of any financial year accumulated losses equal to or exceeding in entice net worth and has also suffered cash losses in such financial year and the financial year immediately preceding such financial year.

**MATTERS TO BE INCLUDED IN THE AUDITOR REPORT IN CASE OF SERVICE COMPANY:**

In case of a service company, the order requires a specific report on their additional matters:-

(i) Whether the Company has a reasonable system of recording receipts, issue and consumption of material and stores and
allocating material consumed to the relation jobs, commensurate with in size and nature of its business [Paragraph 4(B) (iii)].

The system for recording transactions materials and stores and allocating materials consumed to the relation jobs should be reasonable having regard to the size of the Company and the nature of its business.

The purpose of recording of receipts, issue and consumption of materials and stores and allocation of materials consumed to the relation jobs is to ensure that all materials and stores are accounted for and there is a reasonable basis of ascertainment of cost of individual jobs. If in the circumstances of the case, the auditor is satisfied, that these objectives are achieved by the system in force he should not make an adverse report.

(i) Whether the company has a reasonable system of allocating person-hours utilized to the relation jobs connection waste within size and nature of its business. [Paragraph .4(B) (iii)]

The term person-hours in this clause seem to refer to labour cost incurred by the company. There can be various bases to allocating labour costs to the relation jobs. The auditor should satisfy himself that the basis adopted by the company ensures that all labour costs are accounted for and that there is a reasonable basis of ascertainment of cost of individual jobs.

(ii) Whether there is reasonable system of authorization at proper levels and an adequate system of internal control commensurate
with the size of the company and the nature of in business, on issue of stores and allocation of stores and labour to jobs. [Paragraph .4(B) (IV)]

This clause requires the auditors to report on the adequacy of the system of authorization and control and issue of shares and all allocation of stores and labour to jobs. This clause also requires the auditor to report on the adequacy of the system of internal control on issue of stores and labour to job. This clause also require that the auditors to report on the adequacy of the system of internal control on issue of stores and allocation of stores and labour to jobs. The adequacy has to be evaluated with reference to the size of the company and nature of its business.

**MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT IN CASE OF A TRADING COMPANY:**

In the case of a trading company the order requires a specific report on one additional matter as discussed as follows :-

1) Have the damaged goods been determined and if the value of such goods is significant has provision such goods is significant has provision been made for the loss. [Paragraph .4(C) (ii)]

This requirement is similar to the requirement in respect of manufacturing mining or processing companies regarding unserviceable or damaged stores, raw materials and finished goods.
MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT IN CASE OF
FINANCE, INVESTMENT, CHIT FUND, NIDHI OR MUTUAL BENEFIT
COMPANY:

In case of a finance, investment, chit fund, Nidhi or mutual benefit
compny, the auditor is required to report these additional matters, as
are discussed below :-

i) Whether adequate documents and records are maintained in a
case where the company has granted loans and advances based
on security by way of pledge of shares, debentures and other
securities. [Paragraph 4(B) (ii)]

This requirement is confined to loans and advances which are
secured by way of pledge simples has the physical possession of
the security must be transferred to the company. This transfer can
be constructive a question may arise as to the exact meaning of
the term "other securities. The term "other securities" may be
constructed to mean bends or promissory notes issued by a
government or term-government authority. In a broad sense, it
can include any other assets, which is given as security for
repayment of a loan or fulfillment of an obligation. The auditor
has to report whether, adequate documents and records have
been maintained what records would be considered adequate
depends upon the nature of the security and the party to whom,
loan or advances is granted.
ii) Whether the provisions of any special statute applicable to chit fund, Nidhi, or mutual benefit society have been duly complied with [Paragraph .4(D) (iii)],

This is very wide requirement and taken literally would mean that the auditor has to ensure that the company complies with all the requirements of the relevant special statutes; obviously this cannot be the intention. A more rational interpretation would, therefore be that the auditors, has to satisfy him and report that the company has complied with all the provisions of the special statutes as far as they have application to the accounts. It is necessary that the audit report should clearly state the above interpretation.

iii) If the company is dealing or trading in shares, securities, debentures and other investments whether proper records have been maintained of the transactions and contracts. Whether timely entries have been made there is, also whether the stores, securities and debentures and other investments have been held by the company in its own name except to the extent of exemption if any granted under sec. 49 of the Companies Act, 1956 (1 of 1956) [Paragraph .4(D) (iv)]

This clause does not apply to companies which are not cleaning or trading in investment but which purchases investments with a view to hold such investment and earn income from dividend or interest there on. In deciding whether records have been properly maintained the auditor has to examine both, whether the form in
which records are maintained is adequate and whether the records themselves are properly written up and prescribed.

The auditor is required to examine whether timely entries are made in the records. The auditor’s is also required to report whether the investments are held in the company’s own name in respect of companies deal or trade investment. However section 4(a) (4) specifically exempt Companies whose principal business is buying or selling of shares or securities, from that requirements. It seems, therefore that the requirement to report will arise when the buying & selling of securities is not the principal business of the companies but it does such businesses along with some other business.

THE MANUFACTURING AND OTHER COMPANIES (AUDITOR'S REPORT)
ORDER 1988 (MAOCRO 1988):

The government of India has made some changes in the Maocro 1975 by revising it to the some extent. The Maocro 1988 came into force from 1.11.1988. The revised order seems to be galore of cosmetic changes and only give statutory recognition of existing guidelines of ICFAI. It would have been certainly better to evaluate the efficiency of the Maocro report before improving on its existing requirements. Some of the changes made in Maocro 1975 by introducing 1988 are as follows:-

i) Regarding the physical verification of the fixed assets, the word "reasonable internals" has been added.
ii) The other change is substitution of the words material discrepancies for the serious discrepancies.

iii) Regarding the valuation, the word based on this examination of stock word has been added the 1975 order did not contain the above word.

iv) A new clause has been added on loans given to interested parties and to companies under the same management 370(ii)

v) Order of 1988 has extended this review to include internal control procedures for the sale of goods also. The auditor will now be required to check this aspect also by use of internal control questionnaire on sale of goods and testing its adequacy and compliance.

vi) Order of 1975 required and the enquiry to be restricted to stores and raw materials. The 1988 order has now extended to finished goods also.

vii) The 1988 order require the auditor to state the nature of contraventions in acceptance of deposits u/s 58A read with the rule framed there under.

viii) Under 1975, order adequacy of internal audit was to be commented upon only where the paid capital of the company exceeds Rs.25 lacks. The 1988 order requires this reporting even in cases where the average annual turnover of a company exceeded Rs.3 Crores in the three case entries years immediately preceding the financial year concerned.
ix) A new question included in 1988 Order. Whether any undisputed amount payable in respect of income tax, wealth tax, sales tax, custom duty or Excise duty were outstanding as at the last day of financial years. For a period of more than six months from the date become payable, if so the amount of such outstanding dues should be reported.

x) Another new question in the 1988 order is whether the personal expenses have been changed to revenue account of to, the details there of should be reported.

Under the manufacturing and other companies (Auditor's Report) order 1975 and subsequent revised order 1988 issued under section 227(4A) of the Companies Act 1956 the auditor has to make a statement in his audit report on some additional matters. This is merely a statutory recognition of what were already recognized as standard auditing practices. However, this order has now definitely enlarged the scope of statutory audit and increased auditor’s responsibility.

Previously the company auditor's were merely concerned with the reporting of the working results and the financial conditions of the company, which may be termed as "verification audit" as it was mainly concerned with arithmetical accuracy of the financial statements and their compliance with the Companies Act 1956. Now the auditor has to prove into the financial transactions, judgment on systems, policies and is required to comment that the same are not prejudicial to the interest
of the company. In other words, it may be stated that auditor is now required to review the "Commercial Prudence of Transactions".

The introduction of Sec. 227(1A) of the companies Act 1956, Extends the vision of the Company auditor, elightly beyond verificatory audit by requiring him to inquire whether certain transactions were prejudicial to the interests of the company. Thus under section 227(1A) of the companies Act 1956 the auditor was required to offer his comments, on certain transactions of the companies. The order under section 227(4A) extends the scope of audit still further. The order under section 227(4A) seems to be that the auditor's report should be explicit on the soundness of certain specified transactions of the company.

When this order was promulgated, it was claimed that "regulatory social audit" was being introduced and the main object of this order was to ensure social objectives of the companies in grater measure considering the fact that under present conditions. Companies have to sub serve public interest rather than purely private gain of inventors it seems that these claims are largely exaggerated. Though the order has been oriented towards "diagnostic" or property", audit but still it falls very much short of what may be called "Social Audit".

However some additional comments have to be included in auditor’s report under section 227(4A) which cost an onerous responsibility on the auditor to enable to discharge this responsibility satisfactory the company administration need to be improved considerably from within Internal control and Internal Audit will go a beg way in this direction.
AUDIT UNDER SECTION 233(B) RELATING TO COST AUDIT:-

In any manufacturing concern or in service organization often it is felt essential that costs price the goods and or services. Produced rendered should properly computed so as to maintain the market partly in the supply price and keep the firm prepared to face the cut throat competition. It is not only that the costing records are kept for the products and goods sold out, but the record and materials in stock and work in progress are also prepared. Valuation of stock in progress is also felt necessary because almost invariably certain goods are purchased or manufactured during the accounting period with in which the goods are sold. The main object is that the profit should be credited only when the goods are sold during this year, but purchased during the previous year and manufacturing also during the previous year. Therefore, the cost of the goods sold or goods already lying in stores have to be valued at the cost price at the end of the previous year. Keeping in view all these complications in the costing process and structure it has been felt necessary that the costing records should be properly audited and checked by a properly qualified and trained professional.

In India, cost audit was introduced in the statutory form in Oct. 1965 through amendment in different sections (209 and 233) and others of the companies Act 1956, to bring certain categories of companies under cost audit. Companies engaged in the production processing, construction and in mining work have been declared liable for getting their cost records audited under section 233(b) of companies Act 1956
under this the central Government in the prescribed form and send a copy of the report to the company.

**COST AUDIT**

Before taking up the legal terminology of defining the cost Audit, let us know the meaning of cost. The cost is made up of-

a) The value of goods purchased for resale or in the manufacture or assembly of finished goods.

b) Expenses directly carried forward in the stock instead of being charged against current revenue.

Cost Audit means the verification of the correctness of cost accounts and to the adherence to the cost accounting plans. Cost Audit is a system and accurate recording of detailed transactions and operations of manufacture controlling, extracting, transporting, supplying etc. to show the actual cost of each individual piece of work service or separate process of the business.

**OBJECTIVES OF COST AUDIT:-**

The main objects of cost audit are as follows:-

1. To detect any errors or fraud, this might have been committed intentionally or otherwise

2. To watch whether the cost accounting procedure prescribed by the management have been followed strictly
3. To examine that the cost accounts have been properly maintained according to the principles of costing employed in the industry concerned

4. To check whether each item of expenditure involved into the relevant components of the goods manufactured or produced has been properly incurred

5. Whether the internal cost audit system is being employed in the industry or not

**PROVISIONS OF COMPANIES ACT:-**

If 233(A) on companies act provides that, the control government engaged in the production, processing, manufacturing or mining activities. The Government may also direct that the audit of cost accounts if a company shall be conducted in such a manner to obtain a true and fair view of the state of affairs of the company has cost audit records. In such circumstances, the proper books of accounts would include such particular relating to utilization of materials or labour records.

Cost audit is also very helpful from the point of view of the government for the following reasons:-

i) To make a comparative study of cost and expenditure of identical types of industrial units and operations

ii) To fix prices of the goods in favour of consumers after having a study of different aspects of cost expenditure

iii) It also helps the authorities is consideration of protection policy
iv) It helps in taking decisions that whether differential pricing policy will be proper in that particular business.

**OUTLINES OF COST AUDIT:**

Under the companies Act the procedure by which the cost audit is to be conducted has been laid down. It also clearly states as to what cost auditor is expected to do and what time by which the cost audit should be completed. The cost auditor should study the following records carefully for the purpose of effective cost audit.

(i) Records of material and stores
(ii) Labour Records
(iii) Depreciation
(iv) Work in progress
(v) Records of overhead
(vi) Stores and spare parts records

1. **RECORDS OF MATERIAL AND STORES:**

   The cost auditor should in connection with the records of materials and stores keep the following points in mind:-

   (i) **Material Budget:** Cost auditor should see whether there is proper control on material budget or not, whether actual expenses are compared with the budgeted or not, if unfavourable variances are there reasons should be located and remedial measures be taken.

   (ii) **Adequacy of inventory levels:** Cost auditor should check properly the inventory level in respect of minimum, maximum
and re-ordering levels keeping in view the production programme and the rate of consumption of materials, whether economic order quantity has been decided or not.

(iii) **Comparison of stores requisition with bin cards:** - Stores requisition slips are to be posted on the Bio cards at the time of issue of materials or receipts of materials. Auditor should compare whether there exists a few fictitious entries in the Bin cards.

(iv) **To enquire about over stocking:** - The cost auditor should enquire whether management has fixed the maximum quantity of raw materials which can remain in stock at any time to avoid over stocking and thus locking up of the funds and consequently increasing the cost of production.

(v) **Verification of the pricing of the issued materials:** - The auditor should see that the materials issued for production are valued properly or not. He should also examine whether valuation method is followed properly or not.

(vi) **Verification of Waste:** - Cost auditor should see whether proper standards have been fixed for waste or not, what steps have been taken to detect the actual waste and standard waste. He should also examine whether absolute materials is sold properly or not.

(vii) **Enquiry about important records of books of the company:** - Cost auditor should properly enquire whether the tenders or quotations being invited by the purchase department are properly considered and the order is placed at the competitive
prices and for favourable terms. He should also see that the authorized officials of the company place the orders. Entries in the stores ledger and job ledger should be checked with the help of material received note, material Requisition note, material returned note, and material transfer note. The possibilities of pilferage in the Production Department shall be checked and a reconciliation statement is prepared with the cost sheet. As certified by the management and the stores ledger should be done for the total cost period or for different time intervals.

2. **LABOUR RECORD:**

The cost auditor should see whether efficient budget control exists regarding labour costs, he should also see that labour cost is based on job study, material study and time study standards labour costs is compared with the actual labour cost and for variance remedial measures to taken. He should also review the employment & training programme of the workers. He should also compare the attendance register of the regular and casual workers along with the operational staff with the records being maintain at the gate of the factory. The supervisors’ attendance records should also be checked and compared with the gates Attendance register. Auditor should also enquire whether extra payments are made by way of incentives in the form of bonus if such incentives payments are genuine or not. He should also enquire as to who sanctioned such payments and what the
relevant records of their incentive claims are. The cost auditor should also enquire the budget allocation of wages and salaries for each department and compare it with actual payments. The system of overtime payments should also be thoroughly examined. Workers are normally paid the double of the routine wages for their overtime duties, hence the auditor is required to see that workers should not usually be asked to put in overtime work unless there is urgent need of overtime for the completion of the contract.

He should compare the piecework cards of the workers with the stock register and wages sheets if wages are paid on piece rate basis. He should see if the proper record is kept of their work done. He should also see the allocation of records of the direct and in direct labour for various jobs. He should check the posting of the jobs tickets with the cost and time summaries along with the attendance cards and job ticket while observing the labour records. The auditor must find the reasons for the idle time are not satisfactory. He should disclose their facts in his report.

3. **DEPRECIATION:**

The auditor should sincerely with that rate of depreciation maintained throughout almost the same in the cost records or if any other method is, being adopted them the same should be continued while going through the assets records he should see the following points carefully:

(i) Cost of each asset.
(ii) Date of acquisition of each asset and its life.
(iii) Additions in assets during the year
(iv) Rate of depreciation
(v) Total amount of depreciation so far written off
(vi) Obsolescence value of the assets

If some abnormal expenses are incurred on special repairs renovation of an asset then these should be added to the value of the assets, Auditor should check the basis of allocation of expenditure. However, if it is not done properly, the cost auditor can ask specifically the concerned officer of the company if he finds no satisfactory answer, then he can get these incorporated in his report. Thus, the management may be kept informed about the irregular practice of recording depreciation.

4. **WORK IN PROGRESS**

The cost auditor should enquire into the principles of allocation of overhead charges to the work in progress may be defined as the work, which has not been completed on the date on which final accounts were prepared. Treat this incomplete work or when the work is nearly at completion on the date of balance sheet the amount as work in progress.

The basis of valuation of work in progress should also be checked. He should also see that there is no practice of under valuation or over valuation of W.I.P. He should test check some items of overhead charges and should examine them properly. According
to cost sheet, see whether allocation has been done correctly. In the case, the auditor finds that the value of W.I.P. is not separated from finished goods he can ask for an explanation and he can mention this fact in the cost audit report.

5. RECORD OF OVERHEAD CHARGES:-

The auditor should examine overhead expenses like power consumed rent, salaries etc. He should also compare the actual overhead with the Budget overhead. He should also see whether overhead expenses are allocated properly or not. In order to find out accuracy of overhead charges, and their allocation to different jobs, the cost audit or should enquire in to the principles of allocation of overhead charges. He should also see as to which method of absorption and under absorption of overheads. If the practice has prevailing what steps, the management to stop over absorption or under absorption is adopting. If marginal costing is being used by company the auditor should see whether different overhead classified as fixed and fluctuating overhead is proper or not and the distribution is made on fair basis. The auditor should also see the ratio of overhead expenses to sales. He should compare them with the last year expenses, to find out that they are not increasing, excessively. If they are increasing what steps are being adopted by the management to control them or minimize them cost auditor is expected to see whether the overheads are related to manufacture administrative, selling and distribution activities and these be distinguished from each other
because he is to certify that the allocation of overhead charges have been done properly & correctly.

6. **STORES & SPARE PARTS RECORDS:**
A detailed comprehensive checking of the items of stores and spare parts is also essential in the cost audit. Therefore, the cost auditor should make certain, enquires about this important record. The auditor should see whether the value of stores and spare parts has been debited to proper heads such as manufacturing repairs to plants and machinery, repairs to building etc. He should also check whether all changes up to the words or go down of the company e.g. - carriage, stores and spare parts.

7. **AUDIT OF STOCK:**
The cost auditor should also see whether proper stock of raw materials, stores and spare parts is being maintained or not, so that there is no disruption in production. He should also see that no excess stock is maintained so that there will not be a loss of interest of capital and wastages.

The cost auditor should also see that no excess stock of finished goods remains in the company, proper relation of production and sale is being maintained or not. He should also see that proper arrangements have been made for verification and valuation of stock, in the company. He should test check, some, items.
From the above descriptions, it is clear that in Indian companies Act, many aspects of social audit have taken place but the social audit is a voluntarily and not statutory. These provisions are inadequate considering the complexities of the companies act and the importance of social audit for public utility concerns are immense so social audit should be given its due place.

APPLICATION OF THE ABOVE PRINCIPLES:

(i) The companies under the study submitted positive comments. The companies were maintained proper a record showing full particular including quantitative details and situation of fixed assets, the frequency of verification is reasonable and no material discrepancies have been noticed on verification.

(ii) None of the fixed assets was revalued in any of the company under study.

(iii) The stock of finished and semi-finished goods and raw materials were physically verified in all the companies under study. The frequency of verification is reasonable in relation to the size of the company and the nature of the businesses.

(iv) The procedure of verification of stocks followed by the companies was reasonable and adequate in relation to the size of the company and nature of its business.

(v) The discrepancies noticed between physical stocks and books records were not material in respect of items rented and the same were properly dealt with in the books of accounts of the companies under the study.
(vi) All the companies have adequate internal control procedures commensurate with the size of the company and the nature of its businesses for the purchases of stores, raw materials including components, plants and machinery, equipment and other assets and for the goods.

(vii) The companies under the study, accepted deposit from the public under the provisions of section 58 (A) of the companies Act, 1956 and the companies Rules 1975

(viii) Reasonable records have been maintained by the companies for the sale and disposal of By Products and scrap in the companies under the study

(ix) It was reported that there was adequate internal audit system, commensurate with the size and nature of its business

(x) The book of accounts maintained by the company pursuant to the order made by central Government for the maintaining of cost records in respect of certain products under section 209 (i) (d) of the companies Act 1956

(xi) The companies under the study were regular in deposit in provident fund dues with the appropriate authorities employee’s state insurance scheme was not applicable

(xii) It was reported that there were no personal expenses of employees or directors changed to Revenue Account, other than those payable under contractual obligations or in accordance with generally accepted business practices
(xiii) The companies were not a sick industrial companies within the meaning of clause (a) of section 3 (1) of the sick Industrial Companies Act, 1985.

(xiv) It was reported that there was no damaged stocks under the company’s trading activity.

However, some additional comments have to be included about social impact of undertaking on the society. Whether it is the impact being made on the company’s work force of an affirmative action programme. The impact of safety and health programme on the health and safety of its employees the impact of on environmental control programme on the surroundings community or the impact of consumer affairs. Programme on the consumers themselves in the audit report, under section 227(4A) which casts or onerous responsibility of the auditors to enable to discharge responsibility satisfaction.