

Regulations on Audit and Accounts, 2007

Under section 23 of C&AG's (DPC) Act 1971, C&AG is authorized to make Regulations for carrying out into effect the provisions of the Act in so far as they relate to the scope and extent of audit including laying down for the guidance of the Government Departments the general principles of Government accounting and broad principles in regard to audit of receipts and expenditure. While the general principles of Government accounting and broad principles in regard to audit of receipts and expenditure were included in C&AG's Manual of Standing Orders (Accounts) and MSO (Audit) respectively, but these were by nature meant for the use only within the IA&AD for guidance. And further, the scope and extent of C&AG's audit was not explicitly defined anywhere. However, both the understanding of the Act and the standing convention has been that it is the sole prerogative of the C&AG to determine the scope and extent of audit. This principle has been in practice for last so many years since the promulgation of the Act and even before that. This is also considered in conformity with the provisions of the Act as held by distinguished constitutional and legal authorities from time to time.

However, this is also a fact that the issues concerning scope and extent of C&AG's audit have been raised on a few occasions by the Executive. Some of these have been narrated in the previous chapters in this History. To recall those that happened during the period covered by this book, there was the case of non production of records to Audit by the Ministry of Urban Affairs in 1995 on the ground that audit of allotment of Government houses was a matter beyond C&AG's jurisdiction because no financial

implications were involved. A more recent case is, where the Ministry of External Affairs showed its implicit reservation about authority of C&AG to carry out the Performance Audit of their passport, visa and consular services in missions abroad on the ground that an inter-ministerial group was looking into the performance audit aspects. Even more serious was the executive instruction of September 1976 precluding C&AG from having access to confidential files—this is discussed in chapter on Developments in Auditing. In first two cases, the intervention of the incumbent Prime Ministers settled the matter in favour of Audit. In the third case, the new Government annulled the orders of the previous Government. In fact, arising from Ministry of External Affairs case, the Government issued an OM dated June 2006 clarifying that Performance Audit was well within the scope of C&AG's audit jurisdiction. Thus, in all three cases, the authority of the C&AG to carry out audit in an unfettered manner was acknowledged and established.

The non-issue of Regulations in terms of section 23 of the Act even after so many years of the promulgation of the Act may have had its own reasons. Perhaps, questioning the C&AG's jurisdiction was a rare exception and hence, it was ignored. But surprisingly, there is nothing on record to suggest that the subject of issue of regulations in terms of Section 23 of the Act even after so many years of its promulgation has ever been debated in any serious forum like AG's Conference etc. There is a mention of this subject in the 'Foreword' to R.K. Chandrasekharan's Analytical History of the Comptroller and Auditor General of India (Volume I) by the then C&AG T.N. Chaturvedi where he clarified that 'such regulations are not subject to approval of either the executive Government of the day or of Parliament'. The C&AG 'has the discretion to regulate the scope of his audit'. In support, C&AG's 'Foreword' has quoted the Administrative Reforms Commission Report which had upheld not only C&AG's right to carry out efficiency-cum-performance audit but emphasized that this discretionary form of audit is even more important from the view point of accountability in the comprehensive sense. Despite these assertions, the two instances cited above could be considered as questions being raised about authority of C&AG. In this context, it was a very timely decision by the present C&AG to issue regulations codifying the scope and extent of audit as well as principles of accounting and auditing. The C&AG, realizing the importance of discharging this responsibility provided under

section 23, started consultations in early 2006. He also realized the necessity of issuing such Regulations for yet another reason. Audit, as a profession, was getting shaped by very significant changes in technology as also public policies. A look at the 1983 National Audit Act of UK makes this point very clear. The 1983 UK model became a benchmark for many countries to reform their audit systems and policies specially those countries which modelled their Constitution after UK. In nutshell, the C&AG rightly concluded that time had come to discharge the functions of the C&AG under section 23 of the Act and issue Regulations on Audit and Accounts. Eventually, in early 2006, the C&AG decided to commission the autonomous entity functioning under his aegis, the Institute of Public Auditors of India, to nominate a retired person from the IA&AD to provide the initial draft of these Regulations. This task was assigned to a distinguished retired IAAS officer Dharam Vir who made the basic structure of the draft Regulations. These were widely circulated and debated within the Department. All the Accountants General (or their equivalents) were given the draft for their comments and in the Headquarters all the DAIs and ADAIs and some DG level officers were given a copy of the draft for their views and feedback. The process of consultation on the draft Regulations took about a year. Personal involvement and direction of the C&AG in reaching the final draft is evidenced by the fact that he took several meetings with his top team on the feedbacks received from the various offices and the senior officers of the C&AG on the initial draft of the Regulations and made a number of important changes in the Draft Regulations by including a number of new regulations or by omitting some included in the initial draft or by altering or modifying some others.

While a number of officers in the Headquarters contributed in framing of Regulations, special mention would be in order for Audit Wing especially of DG Audit¹. Arising from these long discussions and consultations, which were frequent, several major and substantive changes in the Regulations were brought out. A more important contribution from DG (Audit) was that as head of the policy making wing and concerned subject wing, it fell on her to not only efficiently discharge her overall functions of planning and coordinating the work of preparing Regulations, but contributions of more substantive nature were also made. These included putting a viable draft prepared on the basis of inputs of several persons who participated in the process (field offices, consultant, the senior officers in the Headquarters, the legal expert,

etc.) after 'merging of independent and sometimes divergent views'. An important fact was that DG (Audit) offered a number of suggestions and ideas for the consideration of DAI² and the C&AG and many of these were incorporated after their approval. In nutshell, during this one year period when the Regulations were under preparation, DG (Audit) and her team³ did commendable work in the finalization of the Regulations. In this, they were driven by the constant searching questions by the C&AG, who, as already pointed out, was personally involved in the framing of the Regulations ever since after initially conceiving the idea. As a result of these strenuous efforts, it became possible to finalise the Regulations. The Regulations look comprehensive. Only time will tell how effective these prove in their aim namely to sensitize both Audit and the Administration of their responsibilities under the C&AG's DPC Act. These, however, do make both Audit and auditable entities aware of their duties and responsibilities.

Essentially, these Regulations are in the nature of administrative instructions issued by the C&AG for use and practice by the audit professionals and for the guidance of Government Departments and other auditable entities in their relationship with audit department. These Regulations have the force of law and are binding in nature for all the concerned parties. These are transparent since these are meant not only for departmental circulation but are shared with all the auditable entities so that they are aware of what is Audit expectation of them and what are audit duties in relation to that. In other words, the Regulations indicate the responsibilities of auditee as well as of the auditor.

The Regulations have been notified in the official gazette of Government of India on November 20, 2007 and are, thus, available even to general public for reference.

Besides laying down the broad principles of audit of receipts and expenditure and general principles of government accounting, the Regulations spell out the basic obligations of the Executive in regard to facilitating audit work. The broad subjects covered by Regulations include:

- ❖ Scope and extent of audit
- ❖ Guiding principles of Auditing Standards
- ❖ Financial Audit
- ❖ Compliance Audit
- ❖ Performance Audit

Besides, it deals in four separate chapters- principles governing audit of bodies and authorities other than government establishment and companies, audit of government companies, role of the C&AG in audit of Panchayati Raj Institutions and Urban Local Bodies and audit in Information Technology Environment. A chapter is also devoted to audit evidence and one chapter is devoted to the conduct of audit, that is the process of inspection of auditable entities and how the audit will be conducted in these offices. It describes transparently the system of producing audit notes and inspection reports as also audit reports. One chapter is devoted to general principles of Government accounting and the final chapter deals with special provisions. The principles of audit with regard to the audit of various types that are detailed in the Regulations are generally in line with the principles laid down in the MSO (Audit) but with some changes.

A brief account of the more important and salient Regulations enshrined is given below:

The Regulations have laid down very clearly the broad objectives of Audit as 'to ensure legality, regularity, economy, efficiency and effectiveness of financial management and public administration ...'. The Regulations have classified audit systems through which these objectives will be assessed mainly into three, namely, Financial Audit, Compliance Audit and Performance Audit. The three terms are defined in terms of their broad objectives. The Financial Audit will assess whether financial statements are properly prepared, are complete in all respects and are presented with adequate disclosures; Compliance Audit will seek to assess if provisions of the Constitution, applicable laws, rules and regulations made thereunder and various orders and instructions issued by competent authority are being complied with. Performance Audit will assess the extent to which an entity, programme or organization operates economically, efficiently and effectively.

These three types of audit now constitute the basic framework for Audit Reporting also. For example Performance Audit Reports and Compliance Audit Reports are issued as separate volumes as far as Union Reports are concerned. State Audit Reports are mainly combined Reports, with occasional separate volume on Performance Audit. As regards Financial Audit Reports, C&AG brings out a separate volume on Financial Audit in case of Union but in the case of States, Financial Audit output is contained in chapter 1 and 2 of the Audit Report (Civil).

In the context of importance of independence of the Comptroller and Auditor General of India, the Regulations provide, what was hitherto known and understood by Audit that there is no power of direction by the executive in relation to the performance of audit mandate. In the event of any such directions from executive, the C&AG is not obliged to carry out such directions. It is made clear, however, that executive could always request C&AG proposing matters for audit even though decision on that shall finally rest with C&AG.

Scope and extent of Audit: For the first time, the scope and extent of Audit has been laid down by these Regulations in a separate chapter. The Regulations have made it abundantly clear that within his mandate, the C&AG is the sole authority to decide the scope and extent of audit to be conducted by him or on his behalf. Within his mandate, the C&AG undertakes audits broadly categorized as financial audit, compliance audit and performance audit as elucidated in separate chapters in the Regulations. The overriding consideration in the exercise of his authority to audit any transaction, programme or entity will be fulfillment of his mandate and achieving the objectives of audit. Extent of Audit is defined as the quantum of audit including the period, the units of the auditee, the extent of test check and the boundaries of audit enquiry to be covered in an audit. This chapter also details instructions on conduct of audit and request for special audit including reporting the results thereof.

Guiding principles of Auditing Standards: A separate chapter details guiding principles of Auditing Standards and lays down that Auditing Standards issued by the C&AG 'shall be consistent' with the guiding principles of Auditing Standards as contained in the chapter. These guiding principles are benchmarked to international auditing standards.

Financial Audit: Financial Audit, Compliance Audit and Performance Audit are discussed in exclusive chapters for each one of them. The instructions in the chapter on Financial Audit spell out the requirements to be fulfilled by the Government departments like sending copies of orders of reappropriation and surrender of funds along with reasons for the same to be explained clearly. Similarly, at the end of the year, reasons for any excesses and short falls in expenditure beyond limits prescribed for this purpose vis-à-vis amounts provided need to be explained. There

is an exhaustive list of specific documents which the government departments and other agencies responsible for compilation of accounts and financial statements are to supply suo-moto to the Audit Officer. This makes a good beginning in the sense that Departments now will know beforehand all the essential documents that should be sent to Audit; in addition, they will also send any other documents demanded by Audit. The Regulations specifically emphasize about the responsibility of audit offices and agencies responsible for preparation and compilation of accounts to prepare an annual action plan for timely completion of certification of financial statements and its monitoring.

Compliance Audit: The Compliance Audit chapter essentially sets out the principles of audit of expenditure and receipts. In the case of audit of receipts, the Regulations have laid stress on the examination of systems and procedures and their efficacy with regard to a number of parameters listed. These also clearly stipulate the right of Audit to have access to assessment files and records and computerized data base. Such access shall be subject to any law in force at that time. Regulations significantly stipulate that the scope of audit of receipts includes examination of integrity of data, information and documents which form the basis of a policy.

Regarding data, information and documents obtained by the auditable entity from a third party, the Regulations clarify that Audit will have access to such information and documents as relied upon by the auditable entity in performance of its functions. If such third party evidence is found to be insufficient in Audit, additional information may be requisitioned by Audit from the auditable entity with prior approval of Accountant General.

These are very important provisions in the Regulations and have been prescribed for the first time.

Performance Audit: The chapter on Performance Audit is one which content wise may compare to the previous document namely MSO (Audit) but with very different exposition. The chapter has laid down all essential features of Performance Auditing as already enunciated in the Performance Auditing Guidelines. The basic criteria of Performance Audit namely assessment of economy, efficiency and effectiveness also remain the same.

The Regulations have a provision on timely access to data, information and documents to Audit. These will include documents classified as 'confidential' or 'secret' or 'top secret'. However, the

Regulations make it clear that these documents will be dealt with by Audit in accordance with the standing instructions of the Government for handling and custody of such documents. Regulations also specify that confidentiality of privileged or confidential information prohibited from general disclosure by law must be maintained by Audit. It elaborates that it should be ensured in such cases that the Audit Reports, Inspection Reports and the Audit Notes do not become a means of compromising such privilege or confidentiality of information.

What action is to be taken in case the departments failed to provide data, information and documents to Audit? The Regulations have dealt with this delicate subject with some good provisions. The Regulations say that cases of failure to provide data, information and documents shall be reported by audit office to the Controlling Officer and the concerned government for appropriate action and those authorities shall inform the audit office about the action taken within three months of such a report(s). It does not say beyond this as to what action would be taken if there is a failure to inform about the action within the stipulated time.

The Regulations have specifically made provision for acquiring specialized skills from external sources in carrying out an audit or accounts task if so required.

Regarding action on audit observations—another critical area in auditor- auditee relationship and which has a record that leaves much to be desired at present—the Regulations have demanded establishment and implementation of systems and procedures to ensure timely action on audit observations including recommendations of the Committees of the Legislature and follow up of Audit Reports of the Comptroller and Auditor General.

Management Letters: The Regulations contemplate issue of two types of management letters to the Secretary to Government:

- (a) Intimation of major irregularities to the Government and heads of departments—To strengthen the responsiveness of the auditable entity, a provision has been made for communication of every instance of major irregularity detected in Audit, through a special management letter to the Secretary of the concerned department (with a copy to the Head of the department) within six weeks of the instance coming to the notice in Audit. The Department will respond first with a preliminary report confirming or denying the facts within six weeks. If not denied, a detailed report will come with action

taken within three months of preliminary report. This provision has been made based on recommendations of Administrative Reforms Commission accepted by the Government of India.

- (b) Significant audit observations to be communicated to Secretary—At the end of April every year, Accountant General may write to Secretary to Government of concerned department a management letter 'communicating significant observations and conclusions emerging out of audit during the preceding year'.

Annual Public Statement regarding pending audit observations: A very important provision made in the Regulations relates to making Annual Public Statement regarding pending audit observations by each Head of the Department each year interalia including number and gist of audit paras included in Audit Reports of the previous year; number and gist of major irregularities intimated by Accountant General (Audit) during the previous year; action taken by department on them and number of audit paragraphs incorporated in the inspection reports issued in the previous year and gist of paragraphs with substantial money value. This provision is also based on recommendations of the Administrative Reforms Commission accepted by Government of India.

The Regulations have incorporated provisions for establishment of Audit Committees by the Government for the purpose of monitoring and ensuring compliance and settlement of pending audit observations. Each committee so established shall comprise of a representative of administrative department, Audit and a nominee from the Finance Department besides, the head of the department of the auditable entity. Audit committee meetings shall have minutes recorded.

This provision has put the Audit Committees (which are already existing in many states) on some legal footing with a requirement of minutes being recorded. It is to be noted that the Audit committees are to be constituted by the Government. The Regulations seem to be placing great hopes on Audit Committees for compliance and settlement of pending audit observations. It would be interesting to watch how things shall be in this regard after the Regulations come in operation.

The Chapter dealing with Audit of Bodies and Authorities other than Government Establishments and Companies, had expanded the expression 'body' by including typical examples of corporate or incorporate 'bodies', like institution or organization set up as

an autonomous organization under a specific statute or as a society registered under the Societies Registration Act, 1860 or Indian Trusts Act, 1882, voluntary organization or non-government organization, urban or rural local self government institution, co-operative society, other society or clubs etc. The Chapter has now made very clear provisions regarding audit of these bodies and authorities which are easy to understand and follow. An important Regulation is that Government and heads of departments empowered to sanction grants and/or loans shall furnish to audit office by the end of July every year a statement of bodies or authorities to which grants and/or loans aggregating Rs. ten lakh or more were paid during the preceding year. The statement shall also mention the purpose of the loan/grant and the total expenditure of that body or authority. With the implementation of this Regulation, an important gap existing today viz. of correct data base of bodies and authorities falling under the audit of C&AG, shall hopefully be removed.

The chapter dealing with Audit Reports in Regulations has brought out many important features. For example, it stipulates clearly what should be the minimum contents of the written reply of the concerned Secretary to Government to the draft paragraph issued to him. It says that the reply shall state:

- a) whether the department accepts the facts and figures mentioned in the draft paragraph; if not, the reasons supported by the relevant documents and evidence duly authenticated;
- b) comments, observations and explanation of the Government on matters included in the draft paragraph;
- c) Government's response to suggestions and recommendations made in the draft paragraph;
- d) remedial action taken or proposed to be taken and
- e) any other observations or remarks of the department.

In this chapter, an elaborate system had been outlined for Action Taken Notes for PAC or COPU, Government's response on the recommendations of the PAC/ COPU and role of Accountants General (Audit) in these.

Under special provisions, the two noteworthy Regulations are: one, which clearly stipulates that these Regulations will not come in the way of acceptance of international assignments taken up or being taken up; two, the Regulations have also prescribed an interrelationship of various orders of the C&AG. Specifically, it has outlined the hierarchy of instructions of the C&AG as

Regulations, Standing Orders, Guidelines and Practice Notes in that order. It has clarified that Standing Orders, Audit Guidelines and Practice Notes need to be consistent with these Regulations.

NOTES: CHAPTER-21

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² C.V. Avadhani

³ DG (Audit) was assisted in this work by Kaushal Kumar Tripathi, AAO

GLOSSARY OF ABBREVIATIONS

UK	United Kingdom
OM	Office Memorandum
COPU	Committee on Public Undertakings