



**STOCK AUDIT POLICY : 2018-19**

**Version 8.0**

## DOCUMENT VERSION CONTROL

<b>Document Title</b>	Review of Stock Audit Policy 2018-19.
<b>Prepared By</b>	Senior Manager, Credit Audit & Monitoring Department
<b>Verified &amp; Recommended By</b>	Deputy General Manager, Credit Audit & Monitoring Department
<b>Approved By</b>	Board
<b>Board Approval Date</b>	
<b>Effective Date</b>	01/04/2018

### Document History

<b>Version No.</b>	<b>Date of Approval</b>	<b>Brief Description of Changes</b>
1.0	12.11.2007 ( Audit Committee Of Board )	<b>Newly Developed</b> <u>Conditions:-</u> Stock Audit should be completed within 30 days from the date of intimation sent to auditors as per schedule given below: Ø Commencement of audit work within 10 days from the date of intimation. Ø Conclusion of audit work within 10 days from the date of commencement. Ø Submission of audit report within 10 days from completion of audit.
2.0	30.01.2009 ( Board )	1. It should be ensured that there is no omission either in eligible accounts or in the area of coverage 2. The stock audit, post credit supervision etc., are carried out not simultaneously in a branch but within a reasonable time gap. 3. The Stock Audit for the eligible borrowers should be conducted once in a year.
3.0	26.07.2012 ( Audit Committee Of Board )	1. Stock Auditor is auditing only the stock and audit of receivables is not done. 2. In page 5, under the head “ 10. the appointment Letter “ change the word “ controller “ to “ in-charge “ so that the text would be read as “ The appointment order will be signed and sent only by the in-charge of the Credit Audit & Monitoring Department”.

4.0	28.10.14 ( Board )	The stock audit policy should be reviewed in the month of September every year.  <b>Modification: The period of review of Stock Audit Policy was changed from April to March of the every year from 2015-16.</b>
5.0	22.04.15 ( Board )	<ol style="list-style-type: none"> <li>1. The status of conduct of stock audit should be furnished to the Audit Committee of the Board periodically (quarterly).</li> <li>2. Conducting Stock Audit for all the borrowal accounts having working Capital limit of Rs 5 crores (both Fund based and Non based limits) has been reduced from Rs 5 crore to Rs 3 crore.</li> <li>3. Stock Audit may be conducted for the working capital limits below Rs 3 crores based on specific request of our Credit Department / Regional Office.</li> <li>4. NPA borrowal accounts having working capital limits of Rs 3 crore and above where the primary security of stock/ book Debts are available are also come under the purview of Stock Audit”.</li> <li>5. In Page No:8 Point No 14 to incorporate the condition that the Final Certificate should be submitted by the branches within one month from the date of receipt of the stock audit report by the concerned branch.</li> </ol>
6.0	10.05.16 (Board )	In Para no: 15 as below “ The Credit Audit & Monitoring Department should furnish the details to the Audit Committee of Board regarding the conduct of Stock Audits in the Bank Branches, on quarterly basis ie as on 31 <sup>th</sup> March/30 <sup>th</sup> June/30 <sup>th</sup> September/ 31 <sup>th</sup> December of every year.
7.0	28.02.2017 (Board)	Stock Audit Policy is to be placed before our Board for approval after getting approval of the drafted Stock Audit Policy from the Audit Committee of Board every year.
	04.05.2017 (Audit Committee of Board)	In Page No:6, Point No.8.6: The Concurrent Auditors can be appointed to conduct Stock Audit with a condition that they should not be the Concurrent Auditors for the same branch where they are appointed to conduct Stock Audit and there should not be any negative remarks on the Concurrent Auditors.

**Next Review Date: 31.03.2019. The document should be reviewed every year.**

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**TAMILNAD MERCANTILE BANK LTD., HEAD OFFICE, THOOTHUKUDI.**  
**CREDIT AUDIT & MONITORING DEPARTMENT**  
**STOCK AUDIT POLICY (2018-19)**

**1. INTRODUCTION**

In the context of rapid growth of credit, effective supervision & monitoring of advances have assumed considerable importance. In case of working capital finance, one of the measures that is deployed by the lenders for ensuring the end use of funds and monitoring the borrowal account is the system of periodical Stock Audit by the independent qualified Stock Auditors.

The Stock Audit system was first introduced in our Bank in October'2002 to monitor the borrowal accounts enjoying working capital limits of Rs.5.00 Crore & above.

Our present Bank's Loan policy stipulates as hereunder:

"Stock Audit should be conducted by appointing Chartered Accountants, who are in our panel as Stock Auditors, for Working Capital Limits of ` 3.00 Crore & above (both Fund based and Non Fund based Limits) where the primary security is hypothecation of Stock and/or Book Debts once in a year".

In order to have uniform procedure and practice and to regulate the system of stock audit process, a Policy document on Stock Audit was considered necessary and first such Policy was drafted and adopted in our Bank in the year 2007.

**2. THE POLICY:**

This document termed as "Stock Audit Policy", codifies the policy and the procedure involved in the Stock Audit function. This has been compiled after taking into account changes that have taken place in the lending scenario and monitoring systems.

**3. OBJECTIVES:**

The main objective of stock audit is to ascertain whether the security (borrower's stock and debtors) against which working capital finance has been made is safe and is valued correctly. It is the duty of the Stock auditor to verify the physical existence and absolute ownership of inventory / movable property charged to the bank and to examine the genuineness of the Sundry Debtors list submitted by the borrower.

The various purposes expected to be achieved through stock audit may be summarized as follows –

- Ø To physically verify the value of paid Stock (by excluding the total value of unpaid stock with reference to the level of Trade Creditors and the total value of stock procured under the Non Fund based credit limits viz., FLC / ILC / BG) available in the borrower's location and confirm the same together with the eligible Book Debts are sufficient to cover the total amount outstanding in the Working Capital Limits (Fund based) along with the required level of margin.
- Ø To verify whether the value of stock (procured under Non fund based limits) available on the date of physical verification along with the eligible Book Debts emanated from the sale of such goods is sufficient to cover the total amount of Bill Liability under the Non fund based limits including Bank Guarantee Limit for Supply of Goods.
- Ø To verify related records / registers / Books of accounts such as Stock Register, Purchase Register, Sales Register, Purchase Invoices, Sales Invoices, Credit Notes, Debit Notes etc., maintained by the borrower.
- Ø To carry out physical examination of stock to ascertain the quality, value and age of the inventory thereby identifying whether there exist any obsolete stock & if yes, whether it has been segregated & written off and excluded while arriving the drawing power.
- Ø To ensure proper preservation / storage and handling of stock.
- Ø To ensure the stock under hypothecation have not been hypothecated to other Banks.
- Ø To examine the end use of the funds and verify whether any diversion of funds, interlocking of funds among sister concerns.
- Ø To verify the operation of the accounts such as cash withdrawal, cheque returns, Clearing Cheque outstanding, Number of times the account remained overdrawn, adjustment of returned discounted cheques, PCL overdues, LC devolvement, Invoked Bank Guarantees etc.,
- Ø To confirm whether all the sanction conditions are complied.

- Ø To verify whether the stock is adequately and properly insured against fire and other natural calamities (in appropriate cases against other risks like theft, burglary, marine, riots etc. as per sanction) and kept in secured manner.
- Ø To ascertain whether physical stock tally with the stock statement submitted to the banker.
- Ø To ascertain whether hypothecated stock is realizable.
- Ø To confirm that stock is owned by the borrower and finance is made against value of paid stock only.
- Ø To examine the age wise debtors outstanding as per books and as per statement submitted by the borrower, steps taken for recovery of long pending debtors and likely instances of debtors turning bad, if any.
- Ø To ensure the timely submission of Stock / Book Debts statement, QIS statement etc.,

#### **4. Authority for issuance of Policy and process guidelines:**

The Credit Audit & Monitoring Department is responsible for drafting of Stock Audit policy and also for periodical review of the relative policy and processes.

#### **5. Stock Audit coverage & applicability:**

The borrowal accounts having **working capital limits of `3.00 Crore & above (both Fund based and Non Fund based Limits)** where the primary security is hypothecation of Stock and / or Book Debts come under the purview of Stock Audit. In exceptional cases, Stock Audit may be conducted for the working capital limits below `3.00 Crore based on the specific request of our Credit Department/ Regional Office.

Moreover, in case of NPA borrowal accounts having Working Capital limits of Rs.3.00 crore and above where the primary security of stock and/ or Book Debts are available are also come under the purview of Stock Audit.

**Fund Based limits:**

Fund Based Limit includes all types of Working Capital Limits sanctioned such as Cash Credit (Stock), Cash Credit (Book Debts), Overdraft, Term Loan / Demand Loan (For Working Capital purpose), Bill limits Packing Credit Limit, Key Loan, Ware House Receipts Loan etc.

**Non Fund Based limits**

Non Fund Based Limits sanctioned for Working Capital purposes such as Bank Guarantees, ILC (DA terms / FLC (DA terms), STTC, etc., for the supply of goods on credit terms.

**Advances under Consortium / Multiple Banking arrangement**

In case of advances coming under Consortium / Multiple Banking arrangement, the Bank may fall in line with the Leader of the Consortium or Highest lender, as the case may be.

**Stocks which are not easily verifiable:**

In certain industries, business activities and projects, by the very nature of the business model, the primary security charged to the Bank is though tangible, not easily verifiable. In such cases, the Stock Audit should be conducted by outsourcing Stock Auditor who is having special/ specific knowledge about the nature of goods, which is discussed in para No. 9 of this policy.

**6. Periodicity of Stock Audit**

Stock Audit should be conducted for the eligible borrowal accounts once in a year. It should be ensured that there is no omission either in the eligible accounts or in the area of coverage. It should be arranged in such a way that stock audit, post credit supervision etc., are carried out not simultaneously in a branch but within a reasonable time gap.

**7. Appointment of Stock Auditors:**

The Stock Auditor has to apply to the Regional Manager in whose jurisdiction his office is situated for empanelling him as Banks' Stock Auditor. The Regional Manager has to recommend his request to Credit Audit & Monitoring Department after satisfying the criteria mentioned in Point No.8 of this policy.



A consolidated list will be prepared by Credit Audit & Monitoring Department and put up to the Committee of Executives for empanelling them as our Banks' Stock Auditors at regular interval. The permitted list will be placed before our Managing Director & Chief Executive Officer for his approval who was authorized in this regard by the Board of Directors.

Our Credit Audit & Monitoring Department will select the Stock Auditor from the available panel every year for conducting Stock Audit. The Credit Audit & Monitoring Department submits the list of Stock Auditors along with the borrowal accounts allotted to them to the Managing Director and Chief Executive Officer for his prior permission.

It is the responsibility of Credit Audit & Monitoring Department to review the Stock Auditors who are in the Bank panel every year by placing a review note to Managing Director & Chief Executive Officer.

#### **8. Criteria for appointment of Stock Auditor:**

The following general criteria is applied while selecting the Stock Auditors :-

- 1) The firm of the Stock Auditor shall contain at least two Chartered Accountants of which one of the partners should have at least three years experience. If the Chartered Accountant is an individual or Sole proprietary concern, he should have at least five years experience.
- 2) The Chartered Accountant firm / proprietor / individual should have conducted any Bank Audit in any Commercial Bank at least for a period of two years.
- 3) The Chartered Accountant firm / proprietor / individual should have an office as far as possible at the centre where the Bank's Branch is located for which the Stock Audit is to be conducted.
- 4) Specialized Auditors i.e. auditors having knowledge / expertise of the industry should be considered to the extent possible so as to achieve efficient and effective stock audit mechanism.
- 5) It should be ensured that the Auditor who has appointed to conduct the Stock Audit for the particular borrowal account is not the Auditor for the same borrower.

- 6) The Concurrent Auditors can be appointed to conduct Stock Audit with a condition that they should not be the Concurrent Auditors for the same branch where they are appointed to conduct Stock Audit and there should not be any negative remarks on the Concurrent Auditors.**

#### **9. Outsourcing of Stock Auditors:**

Stock Auditors are appointed taking into the consideration of the firm's constitution, experience etc. Some of the stock / goods may be graded depending on the composition, durability and other technical specifications which cannot be assessed by layman. Chartered Engineer who is technically / professionally qualified, may be engaged by Stock Auditors with prior permission. In such cases, if the Stock Auditor engages the services of a Chartered Engineer who is registered with The Institution of Engineers (India), such engineers should possess special knowledge / practical experience about the stock/ product such as chemicals, oils etc., in which the borrower is dealing with. Before engaging the services of such outsourced personnel, clearance should be obtained from our MD & CEO.

The outsourced Chartered Engineer will accompany Stock Auditor during Unit / Godown visit. The outsourced Chartered Engineer will certify the quality of product and also provide the market rate (per unit) for the stock/ goods to the Stock Auditor. Based on the rate provided by the Chartered Engineer, the Stock Auditor will ascertain the quantity of stock and arrives at the total value of stock available.

The reimbursement to such outsourced Chartered Engineer will be fixed by the concerned Regional Office after consultation with the Stock Auditor. The fees may vary from product to product and also depending upon the availability of testing centre / equipments etc. However, the decision of the Bank in this regard is final and binding on all the parties.

#### **10. Appointment Letter :**

The appointment letter will be signed and sent only by the in-charge of the Credit Audit & Monitoring Department to ensure audit independence and integrity. The appointment letters will contain the name of borrower unit(s) to be inspected and the details of tasks to be performed such as carrying out physical verification of stock and to ascertain existence, ownership, quantum, value of different items of inventories such as raw materials, work in progress and finished stocks as per standard accounting practices and pointing variances, if any and verification of debtors etc.

The Auditors will be furnished with necessary guidelines issued by the Bank and expected to have adequate knowledge of regulatory requirements.

**In the appointment letter, the Auditor will be advised to take up his assignment within 30 days of intimation. If not another auditor/s may be appointed in his/their place and the same auditor should not be considered for next/subsequent audit.**

The appointment letter should also contain a suitable confidentiality clause to the effect that the Auditor should not divulge any information / statements / particulars furnished to him by the bank and maintain them in strict confidence.

### **11. Period of appointment:**

The appointment of Stock Auditor shall be upto three years. The Stock Auditor should be appointed before the month of June every year. Any additional appointment / refusal / cancellation of Stock Auditors should be after obtaining prior permission from the Managing Director & CEO as and when needed. There should be a cooling period for Stock Audit of at least one year and thereafter they can be shifted to another branch. Rotation of Stock Auditors should be made in such a way that the same auditors should not generally audit the same unit / sister / associate units next time or repetitively. The number of accounts to be allotted to a Stock Auditor should be done on fair basis without any discrimination based on previous experience.

### **12. Remuneration of Stock Auditors:**

The remuneration / fees and other expenses payable to Stock auditors depend upon the location of units / godowns visited and the number of days spent by them. The fees structure (as existing now) along with other terms and conditions for payment of fees are provided in the **Annexure** to this Policy.

### **13. Completion of Stock Audit**

The Stock Audit should be completed within 30 days from the date of intimation to the Stock Auditor as per the schedule given below:

1. Commencement of Audit work - Within 10 days from the date of intimation.
2. Conclusion of Audit - Within 10 days from the date of commencement.
3. Submission of Audit Report - Within 10 days from completion of Audit.

**14. Reporting System & Submission of Final Certificate:**

The Stock Auditor should verify the borrower's unit/ godown as to their position on Stock / Book Debts and submit the report immediately in quadruplicate (4 copies) two copies to Credit Audit & Monitoring Department, one copy to the respective Regional Office through the Branch and one copy to the branch.

The Final Certificate should be submitted by the branches within one month from the date of receipt of the stock audit report by the concerned branch. The concerned Regional Office should verify the full compliance and obtain Final Certificate from the respective Branches and submit the same to Credit Audit & Monitoring Department. The entire process till the obtention of the Final Certificate from the respective Regional Office is being monitored at the Credit Audit & Monitoring Department.

**15. Reports to Audit Committee of the Board:**

The Credit Audit & Monitoring Department should furnish the details to the Audit Committee of Board regarding the conduct of Stock Audits in the Bank Branches, on quarterly basis i.e. as on 30<sup>th</sup> June, 30<sup>th</sup> September, 31<sup>th</sup> December and 31<sup>st</sup> March of every year.

**16. Review of Stock Audit Policy**

This policy will be in force upto March 2019 and it will be reviewed once in a year.

**17. Stock Audit Policy for Approval**

Stock Audit Policy is to be placed before our Board for approval after getting approval of the drafted Stock Audit Policy from the Audit Committee of Board every year.

**Dated:** 15.02.2018.

**Place:** Thoothukudi.

## ANNEXURE

### FEE STRUCTURE FOR CONDUCTING STOCK AUDIT

#### Stock Auditor Fees (per account)

**I) Local (without going to outstation):**

**A) Metro Centre**

(in ` )

	Days						
	1	2	3	4	5	6	7
a) Fees	1000	2000	3000	3500	4000	4000*	4000*
b) Fixed lump sum Amount	2500	2500	2500	2500	2500	2500	2500
Total	3500	4500	5500	6000	6500	6500	6500

\* Fees should not exceed maximum of `4,000/- irrespective of the no of days taken for Audit.

**B) Non Metro Centre**

(in ` )

	Days						
	1	2	3	4	5	6	7
a) Fees	1000	2000	3000	3500	4000	4000*	4000*
b) Fixed lump sum Amount	2000	2000	2000	2000	2000	2000	2000
Total	3000	4000	5000	5500	6000	6000	6000

\* Fees should not exceed maximum of `4,000/- irrespective of the no of days taken for Audit.

**For example:** If the Stock Auditor and godown are in the same place

<b>Metro Centre:</b>	If 6 days are taken in a Metro centre for inspection of the godowns situated at the same place, then the total amount of fees paid will be `6,500/- (Fees `4,000/- + Fixed Lump sum amount `2,500/-).
<b>Non Metro Centre:</b>	If 6 days are taken in a Non metro centre for inspection of the godowns situated at the same place, then the total amount of fees paid will be `6,000/- (Fees `4,000/- + Fixed Lump sum `2,000/-).

**II) For Outstation works:**

**A) Metro Centre**

(in `)

	Days						
	1	2	3	4	5	6	7
a) Fees	1000	2000	3000	3500	4000	4000*	4000*
b) Fixed lump sum Amount	2500	2500	2500	2500	2500	2500	2500
Total	3500	4500	5500	6000	6500	6500	6500

\* Fees should not exceed maximum of `4,000/- irrespective of the no of days taken for Audit.

**B) Non Metro Centre**

(in `)

	Days						
	1	2	3	4	5	6	7
a) Fees	1000	2000	3000	3500	4000	4000*	4000*
b) Fixed lump sum Amount	2000	2000	2000	2000	2000	2000	2000
Total	3000	4000	5000	5500	6000	6000	6000

\* Fees should not exceed maximum of `4,000/- irrespective of the no of days taken for Audit.

**c) Boarding and Lodging expenses for outstation works:**

1. Metro Centre - `1,000/- per day for 2 persons
2. Non Metro Centre - `850/- per day for 2 persons

**d) Boarding expenses during Travel:**

	For Metro Centre Per day	For Non Metro Centre Per day
Boarding Expenses (Each person)	<b>`250/-</b>	<b>`225/-</b>

e) Traveling expenses will be reimbursed for 2 persons (one qualified auditor + one assistant) on production of original tickets for one Up and Down Journey - Train A/c II Tier / Actual Bus fares are eligible.

**Total Fee Payable:**

Metro : II A a + b + c + d + e

Non Metro : II B a + b + c + d + e

**For example:** If the Stock Auditor and godown are at other places

<b>Metro Centre:</b>	If 6 days are taken in a metro centre for inspection of the godowns, then the total amount of Fees including Boarding & Lodging paid will be ₹13,500/- (Fees ₹4,000/- + Fixed Lump sum amount ₹2,500/- + Boarding & Lodging ₹6,000/- + Boarding expense during travel for 2 days for 2 persons ₹1,000/-) + Actual Train/Bus Fare for 2 persons.
<b>Non Metro Centre:</b>	If 7 days are taken in a Non metro centre for inspection of the godowns, then the total amount of Fees including Boarding & Lodging paid will be ₹12,850/- (Fees ₹4,000/- + Fixed Lump sum amount ₹2,000/- + Boarding & Lodging ₹5,950/- + Boarding expense during travel for 2 days for 2 persons ₹900/-) + Actual Train/Bus Fare for 2 persons.

**Conditions:**

- 1) Stock Audit should be made by any of the qualified Auditors, one assistant may accompany him.
- 2) Vehicle may be provided for godown inspection to the Stock Auditor.
- 3) Branch has to plan with the Stock Auditor for the sequence of the Stock Audit and number of days required and conducts the Audit accordingly.
- 4) The Stock Audit fees with eligible service tax if any, after deducting the TDS payable at the Branch by getting necessary sanction from the Regional Manager.
- 5) If the Auditor verifies stock of more than one account the expenses are to be shared equally to all the borrowal accounts.
- 6) The expenses for conducting Stock Audit should be informed to the borrowers well in advance.

**The branch should pay the stock audit fees and the eligible expenses by debiting the concerned Borrowal account(s) after obtaining approval and sanction from the Regional Office.**