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AUDIT, INVESTIGATION AND DUE DILIGENCE

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ABSTRACT

This paper explains the approach to an investigation is different from that followed in an audit. An investigation involves a more detailed examination of the selected areas than what is required in an audit.

An investigation seeks substantive and in some case even conclusive evidence as compared to audit which mainly relies on persuasive evidence.

Over a period of time, audit and investigation have converged in to a relatively newer concept namely, Forensic audit. With the number of fraudulent activities and ambiguous financial activities have been accelerating all over the world. Consequently, businesses are exposed to risks of fraudulent activities

Keywords: Investigation, financial activities, Evidence, Forensic audit.

INTRODUCTION

An audit is a systematic and independent examination of books, accounts, statutory records, documents and vouchers of an organization to ascertain how far the financial statements as well as non-financial disclosures present a true and fair view of the concern. It also attempts to ensure that the books of accounts are properly maintained by the concern as required by law. Auditing has become such a ubiquitous phenomenon in the corporate and the public sector that academics started identifying an "Audit Society". The auditor perceives and recognizes the propositions before them for examination, obtains evidence, evaluates the same and formulates an opinion on the basis of his judgment which is communicated through their audit report. Audits provide third party assurance to various stakeholders that the subject matter is free from material misstatement.

An investigator does not accept a stated fact as correct until it is substantiated. An auditor, in the absence of suspicious circumstances, relies on stated facts or figures. An auditor must see whether the method of valuation and other accounting policies have been properly made in the financial statements or not. An investigator, however, is not bound by accounting conventions, policies and disclosure requirements.

Due Diligence on the other hand refers to a comprehensive appraisal of a business undertaken by a prospective buyer/investor, specifically to establish its assets and liabilities and ascertain its commercial potentiality. It is a term that is often heard in the corporate world these days in relation to corporate restructuring. The term 'corporate restructuring' normally includes internal reconstruction, amalgamations, spin-offs, divestiture, mergers, joint ventures, splitoff, etc. Certain corporate restructuring exercises are not within the group (also known as external corporate restructuring exercises), for example, a joint venture between two parties where one party hives off an existing unit or division into another company into which the joint venture partner then acquires an interest or has acquired an interest.

OBJECTIVES

To obtain an understanding of the approach for investigation, audit and due diligence, the steps, techniques in Investigation and audit and the types of due diligence.

To determine whether audit, investigation and due diligence in theory and in practice are similar or not.

HYPOTHESIS

H0: Audit, investigation and due diligence does not have identical meaning, objective, approach and purpose.

H1: Audit, investigation and due diligence has identical meaning, objective approach and purpose.

SCOPE

The working class population who are actively involved in the field of study, in particular the chartered accountants aspirants, qualified chartered accounts, graduates, post graduates, were selected for sending the questionnaire. Mumbai being considered as financial capital of the country is witnessing increased numbers of professionals in all streams but in particular in courses such as Chartered Accountants, Company Secretary, Cost Accountant, Masters in Finance and Accountancy, to name a few.

The professionals as mentioned above having their career in the field of study were part of the study and provide their views on various points put before them to enable the people who are relatively new and naïve for this topic to obtain a proper understanding of the matter of study. Also, the study covered the period from 12th

September 2018 to 23rd December 2018 for primary and secondary data collection. During this period the questionnaire were distributed amongst all the professionals mentioned above.

LIMITATIONS OF THE STUDY

Since, the respondents were professionals involved in assignments related to the subject and the questionnaire were sent to them in the month of September as well as December, which happens to be the due date for and half yearly reporting, filing annual reports, month closures tax deadlines etc. many respondents did not give their responses.

SIGNIFICANCE OF THE STUDY

Collection of the data was an experience in itself. The dedicated professions were ready to give responses and share their experiences. Some of them appreciated the efforts taken by the learner. The respondents were of the opinion that the study would be enable the new entrants in the profession to obtain an understanding of approach for investigation, audit and due diligence , the steps, techniques in investigation and audit and the types of due diligence and thus help them taking an informed decision for their career path.

SAMPLE SIZE AND DATA COLLECTION

The learner decided to carry out the study on samples basis considering the vast population size of professionals. The learner decided to select 50 samples randomly and sent them the questionnaire via google forms. 37 amongst the sample size selected responded to the questionnaire.

DATA COLLECTION

Primary data - The primary data was collected through questionnaire sent via google forms.

Secondary data - This data was collected from internet on various websites, articles, books, journals, etc.

LITERATURE REVIEW

Developing an Overall audit strategy sets the scope, timing and direction of the audit, and guides the development of the more detailed audit plan. The auditor shall establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. The process of establishing the overall audit strategy assists the auditor to determine, subject to the completion of the auditor's risk assessment procedures, such matters as:

- The resources to deploy for specific audit areas, such as the use of appropriately experienced team members for high risk areas or the involvement of experts on complex matters;
- The amount of resources to allocate to specific audit areas, such as the number of team members assigned to observe the inventory count at material locations, the extent of review of other auditors' work in the case of group audits, or the audit budget in hours to allocate to high risk areas;
- When these resources are to be deployed, such as whether at an interim audit stage or at key cut-off dates; and
- How such resources are managed, directed and supervised, such as when team briefing and debriefing meetings are expected to be held, how engagement partner and manager reviews are expected to take place (for example, on-site or off-site), and whether to complete engagement quality control reviews.

STEPS IN INVESTIGATION

As investigation involves a variety of situations, it is not possible to lay down any standardized procedure. However, usually, an investigation requires the following steps in order of sequence:

1. Determination of objectives and establishment of scope of investigation: At the stage of acceptance of the assignment, the investigator should be clear about what is sought to be achieved by the investigation. If instructions from the client leave matters vague and non-specific, it would be proper for the investigator to have the matters discussed and obtain clearly written instructions covering the object and the scope of investigations and the issues incidental thereto.
2. Formulation of the investigation programme: It is not possible to draw up one programme to serve different types of investigations which a professional accountant is called upon to carry out, for their scope and content must be determined on a consideration of circumstances peculiar to each business or situation. The investigation programme should be drawn up having regard to the nature of the business, the structure of business, the instructions from the client embodying the objectives, the consequent scope and depth and the necessity to extend the investigation into books and records belonging to others.

3. **Collection of Evidence:** Through examination, the investigator would be gathering relevant evidence connected with the matters to be investigated. In the course of examination of the documents and records, the investigator may require obtaining oral explanations from various personnel of the concerned business. In case his client is a person external to the business, it may be necessary for the investigator to get the matter formally agreed to by the business through the client.
4. **Analysis and Interpretation of Findings:** Careful analysis and correlation of facts and figures will be necessary before the investigator can reach his conclusion. The conclusion should be well reasoned and backed by established facts and data. He must analyze the data objectively based on evidence gathered by him and should not draw conclusions according to pre-conceived notions. While interpreting the figures, the investigator must keep in mind various factors e.g. the political and economic considerations, competition faced by the business, historical pattern of the data, nature of the business, etc.
5. **Reporting of findings:** Like all other work of an accountant, an investigation results in a report. It is submitted and addressed to the party at whose instance the investigation has been carried out. The nature of the report is governed mainly by two factors. First, the instructions given by the client as regards the special aspects of the business which are required to be investigated; and second, the findings of the investigating accountant.

The important issues to be kept in mind by the investigator while preparing his report are as follows:

- The report should not contain anything which is not relevant either to highlight the nature of the investigation or the outcome thereof.
- Every word or expression used should be properly considered so that the possibility of arriving at a different meaning or interpretation other than the one intended by the investigator can be minimized.
- Relevant facts and conclusions should be properly linked.

GENERAL APPROACH FOR INVESTIGATION

The general approach for investigation under Sections 210, 212 and 213 of the Companies Act, 2013 is conditioned by the legal requirements in these regards. From the foregoing requirements of law, it is apparent that investigations under these requirements may encompass a wide field. The affairs of the company may include everything such as goodwill, profit and loss, contracts, investments, assets, shareholding in subsidiaries, decision making, etc. Also, the specific circumstances mentioned in these sections like fraud, mismanagement, oppression of any shareholder etc. come within the term "affairs of the company."

Understanding the differences between an audit and financial due diligence:

In the context of mergers and acquisitions, potential investors often feel a level of comfort when their investment target is audited. However, relying solely on a target's audited financial statements when making an investment decision may be shortsighted. An audit's purpose is to provide assurance that management has presented a true and fair view of a company's financial performance and position, but audited financials often do not identify significant issues likely to be of interest to a buyer or seller. The due diligence process typically covers a wide range of areas, including legal, information technology, operational, marketing and financial matters. Financial due diligence (often referred to as "accounting" due diligence) focuses on providing potential investors with an understanding of a company's

- sustainable economic earnings,
- Historical sales and operating expense trends,
- Historical working capital needs,
- Key assumptions used in management's forecast, and
- Key personnel and accounting information systems.

DATA ANALYSIS, INTERPRETATION AND PRESENTATION

A total of 19 questions were asked to the respondents covering their names, profession, various topics and aspects of the objective and the hypothesis of the project. All of these questions was filled up into google form and was sent to the respondents via various means which includes email, social media, etc. After this the responses received were directly converted into spreadsheet of google where the learner analyzed and interpreted the data and made pie diagrams, tables, column charts from the responses received. Before starting the actual questionnaire, the respondents were asked their names, qualifications and whether they work in the related field of study.

Q1. Is the ultimate objective of Audit and investigation or forensic audit same?

The response to this question was taken in yes or no format.

- 0 respondents gave their positive responses as yes.
- 17 respondents gave negative responses i.e. no.

Q2. Is the work of Investigation limited by rigid time frame like audit?

- 0 respondent gave their positive response as yes.
- 17 respondents gave negative responses i.e. no.

Therefore, it is to be interpreted that unlike audit, investigation has no rigid time frame. In audit, there are deadlines by which the audit must be completed. However, investigation is normally not subjected to limitation in time.

SUGGESTIONS

Audit forms part of most of the curriculum at the graduation and postgraduation level. Student who come out as graduates are very much familiar with audit in terms of theory as well as its practical approach. However there is relatively less understanding and familiarity with the terms such as forensic audit, statutory and nonstatutory investigation, due diligence. These terms are gaining demand due to various changes and events happening in corporate world which require the conduct of such assignments. Based on the study it was concluded that these are relatively different concepts in theory and practical approach. Hence, if these topics are included as a part of the curriculum at graduation and post-graduation level, then it will assist the students to familiarize themselves with these terms which will broaden the scope of finding a placement and give them an added advantage when they enter the corporate world.

CONCLUSIONS

Audit, Investigation and due diligence are three different disciplines with each topic having a different methodology, approach in execution. Each of the vertical has a different purpose for which it is undertaken and different situation or scenarios under which it is undertaken which is closely driven by the objective of its execution. Each of the topics are performed as a part of either statutory or no statutory requirement with different ultimate objective and the procedures and steps also would vary accordingly. Based on the study undertaken, analysis of the responses by the participants to the research study it can be concluded that Audit, investigation and due diligence are relatively different topics with wide difference between them in various aspects and thus they are different in theory as well as practical applicability

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