

Audit of Stock Brokers

Presented by :

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Hosted by:

JB Nagar CPE Study Circle

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Agenda

Legal Framework

ICAI Code of Conduct for CA

Jargons in Stock Broking Industry

Auditing Aspects

Various Certifications

Legal Framework

Legal Framework

SEBI Act, 1992 & Rules framed there-
under

Securities Contract (Regulation) Act, 1956
& Rules framed there-under

Rules, Regulations & Bye laws of
Respective Stock Exchanges

Income Tax Act, 1961

Legal Framework

Companies Act, 1956

Indian Stamp Act and Relevant State Laws

Finance Act, 1994 – Service Tax


Other Labour Laws

- e.g. P.F., E.S.I.C., Gratuity etc.

Legal Framework



Accounting Standards (AS 1 to 31)
issued by ICAI



Standards on Auditing (SA 1 to 34)
issued by ICAI (Knowledge of the
Business, sampling, frauds & Errors etc.)



Standards on Internal Auditing issued
by ICAI

ICAI Code of Conduct

ICAI Code of Conduct

Whether the Statutory Auditor can be appointed as Internal Auditor

Whether statutory auditor of holding company be appointed as Internal Auditor

ICAI Code of Conduct

Whether peer review is applicable for internal audit of stock broker (whether internal audit of stock broker is an attestation function)

Whether tax auditor can be appointed as Internal Auditor

ICAI Code of Conduct

Whether internal auditor can undertake consultancy assignments of the broker where he is also an internal auditor

Is there any cap/ restriction on the value/ fees of the consultancy assignments that could be undertaken by internal auditor

ICAI Code of Conduct

Whether Tax auditor/ internal auditor can represent the clients before statutory authorities like Income tax, SEBI etc. Would it be considered as conflict of interest

Jargons in Stock Broking Industry

Jargons

- Valan / settlement - Rolling Settlement
- Jobbing/ Arbitrage/ Own Trading
- Sub Broker / Remisier / Authorised person
- UCC/ KRA
- Client Bank / Own Bank / Settlement Bank / Expense Bank
- Pool A/c / Beneficiary A/c
- Pay-in/ Pay-out
- BRK / Trade files

Audit Aspects

Financial Audits

Applicable Accounting Standards:

AS no.	Accounting Standards	Applicability
AS 1	Disclosure of Accounting Principles	Yes
AS 2	Valuation of Inventories	Yes
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	Yes
AS 9	Revenue Recognition	Yes

Applicable Accounting Standards:

AS 13	Accounting for Investments	Yes
AS 18	Related Party Disclosures	Yes
AS 22	Accounting for taxes on income	Yes
AS 23	Accounting for Investments in Associates in Consolidated Financial Statements	Yes

Applicable Accounting Standards:

AS 30	Financial Instruments: Recognition and Measurement	Yes
AS 31	Financial Instruments: Presentation	Yes
AS 32	Financial Instruments: Disclosures	Yes

CARO Requirement

- 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 and whether timely entries have been made therein; also whether the shares, securities, debentures and other investments have been held by the company, in its own name except to the extent of the exemption, if any, granted under section 49 of the Act;

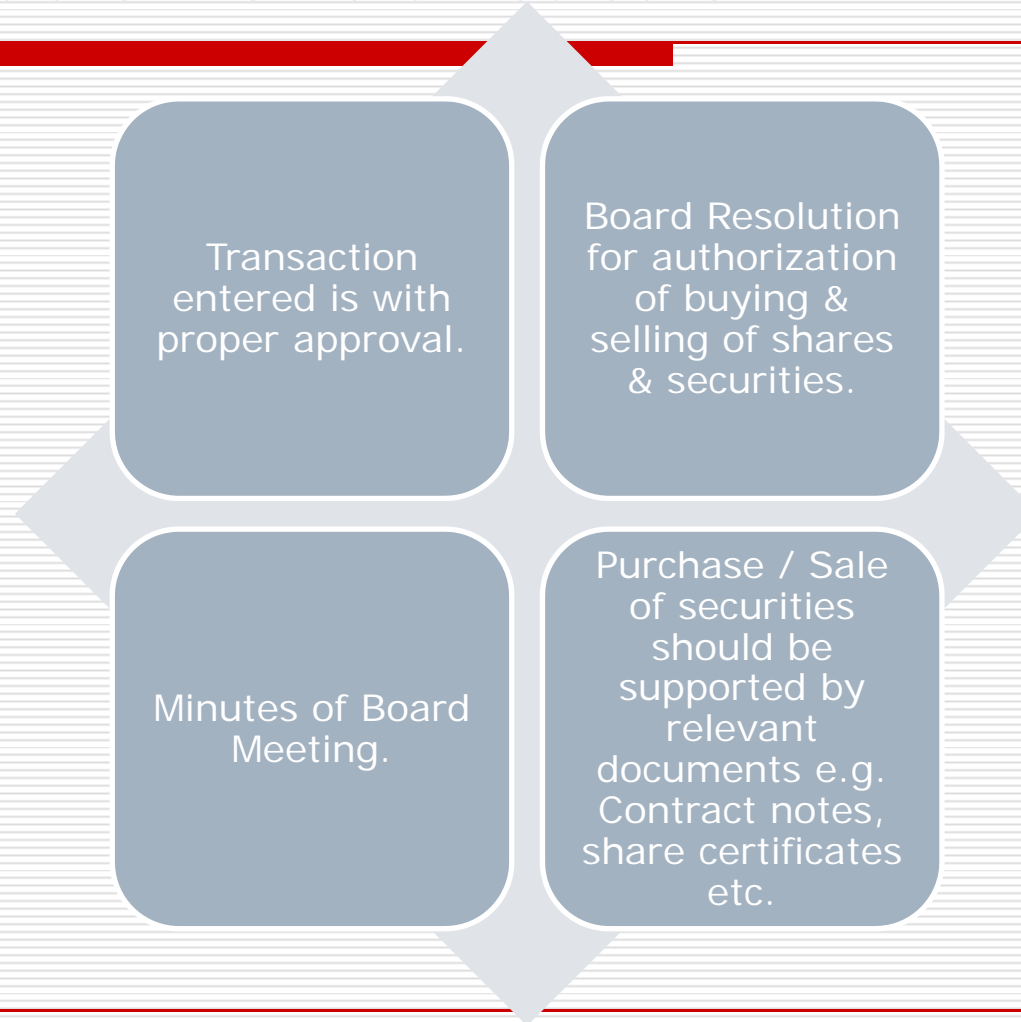
CARO Requirement

- whether the funds raised on short-term basis have been used for long term investment and vice versa; If yes, the nature and amount is to be indicated.
- whether any fraud on or by the company has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated.

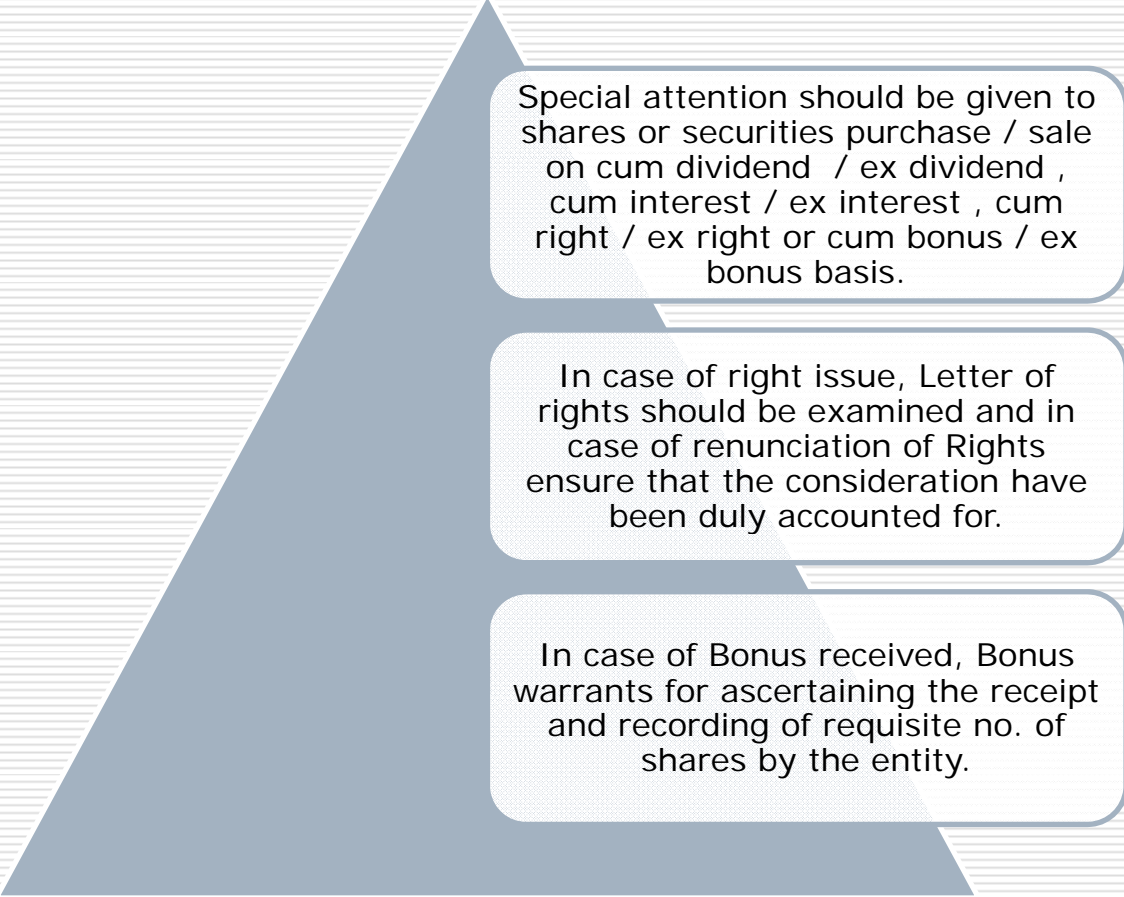
Classification of Investments

- Investment should be disclosed as current & long term Investment distinctly in its financial statement.

Verification of transaction



Verification of transaction



Special attention should be given to shares or securities purchase / sale on cum dividend / ex dividend , cum interest / ex interest , cum right / ex right or cum bonus / ex bonus basis.

In case of right issue, Letter of rights should be examined and in case of renunciation of Rights ensure that the consideration have been duly accounted for.

In case of Bonus received, Bonus warrants for ascertaining the receipt and recording of requisite no. of shares by the entity.

Verification of transaction

In case of Merger, Demerger, Split, Buy Back whether transaction are properly Accounted for with supporting Documents

Also verify the price paid / received for purchase / Sale of share and securities with the market price of that Day.

Verify whether Investment Register is maintained & Updated with each Transaction of Investment.

Revenue Recognition

As per AS-9

- Revenue arising should be recognized only when no significant uncertainty as to measurability or collectability exists.

Revenue on Interest

- Recognized on time proportion basis taking in to account the amount outstanding and the rate applicable.

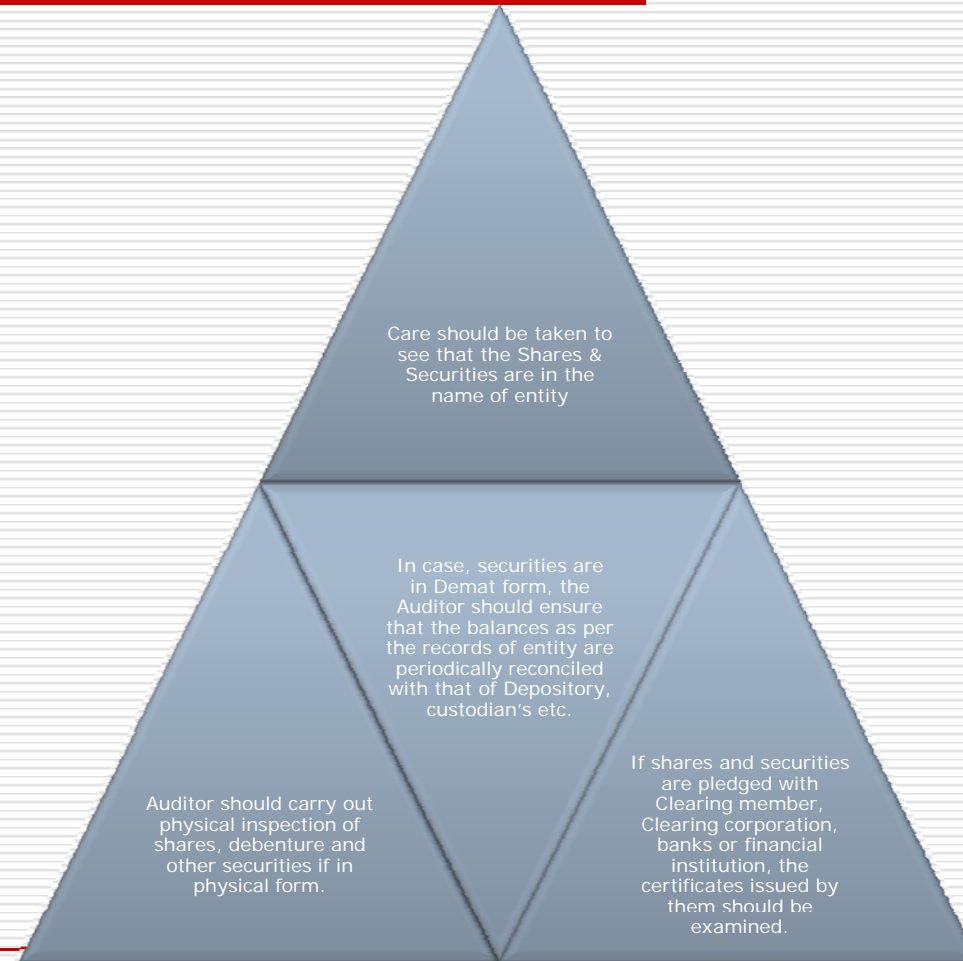
Dividend from Investment in Shares

- Recognized when the owner's right to receive payment is established.

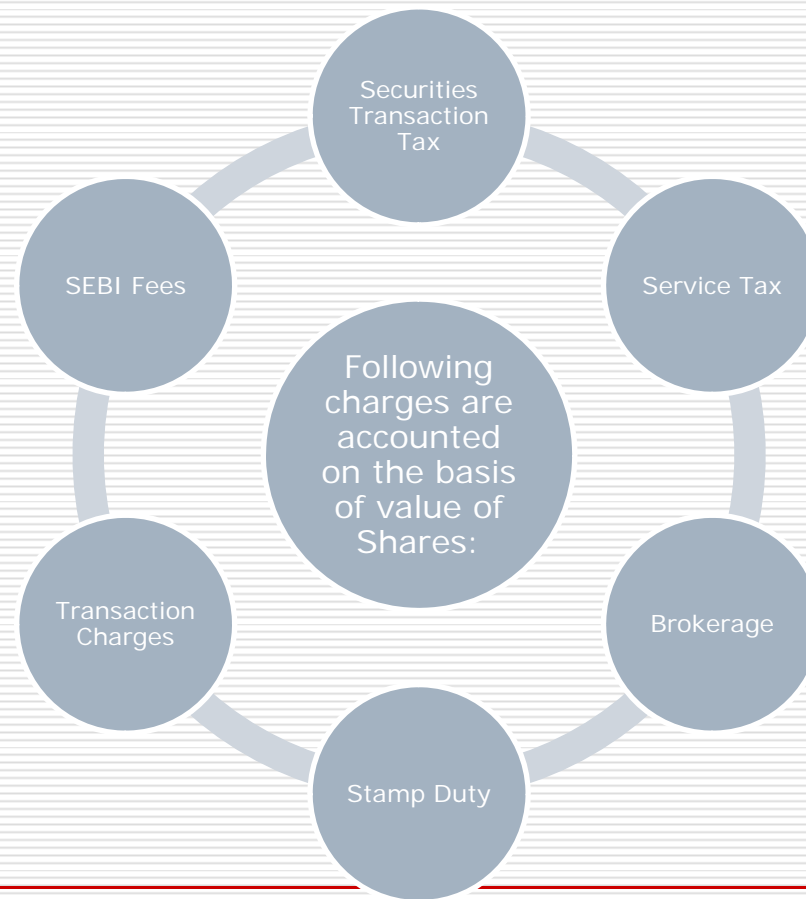
Brokerage Income

- Disclosed at Gross Figures and should not be netted off with payments made to Sub-brokers

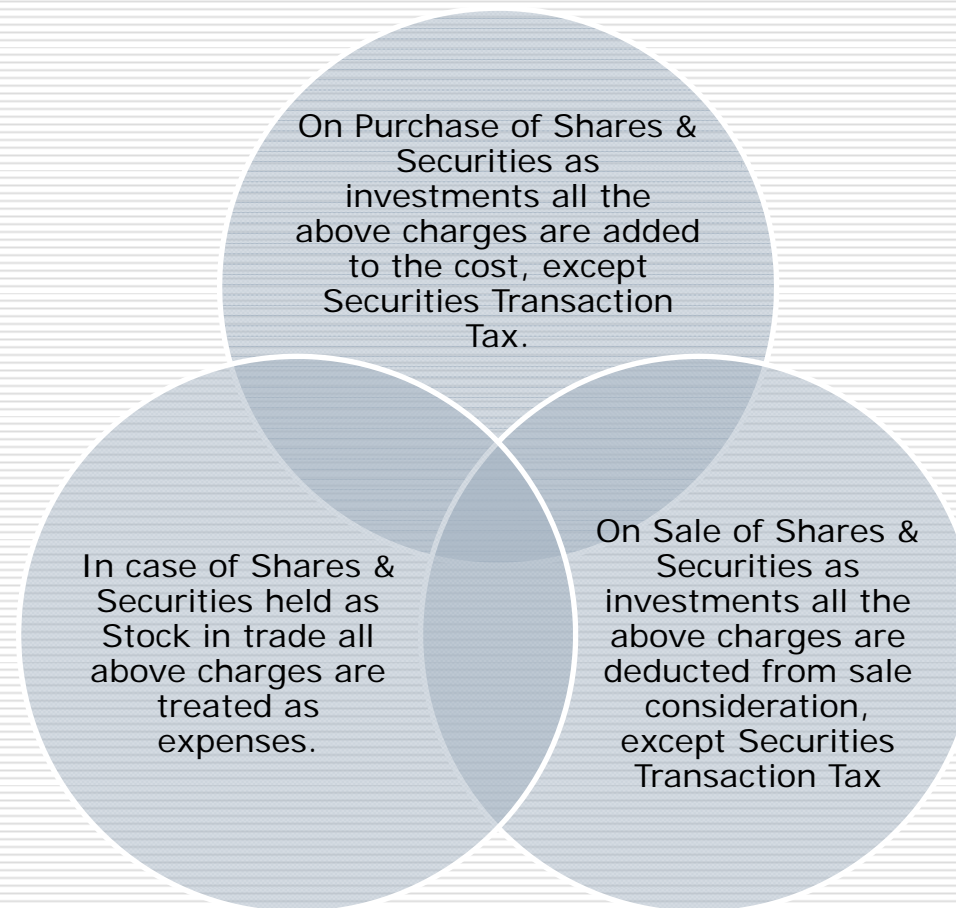
Physical Inspection



Accounting of Incidental Charges



Accounting of Incidental Charges



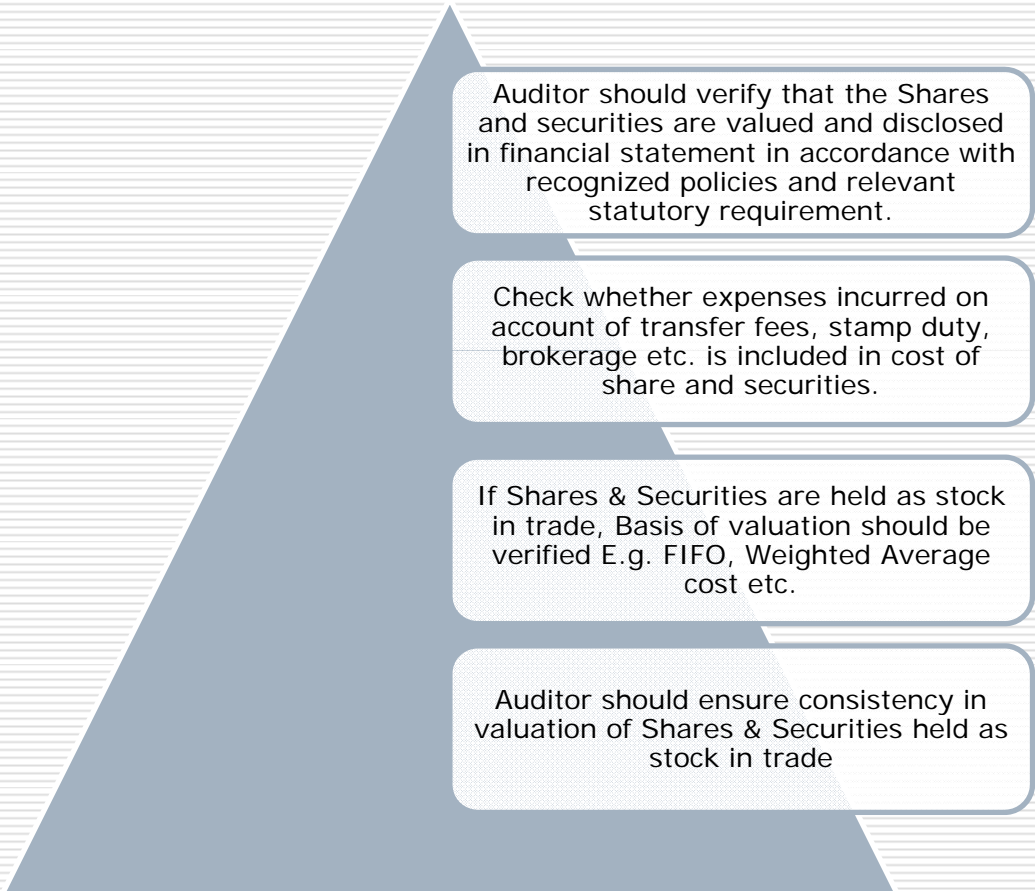
Carrying amount of investments

Initial recording of Shares & Securities Should be at cost.

Investment classified as current investment are carried in the financial statement at the lower of cost & market price

Investment classified as Long term investment are carried in the financial statement at the cost, However provision for diminution should be made to recognise a decline, other than temporary in the value of for each Shares & Securities

Valuation



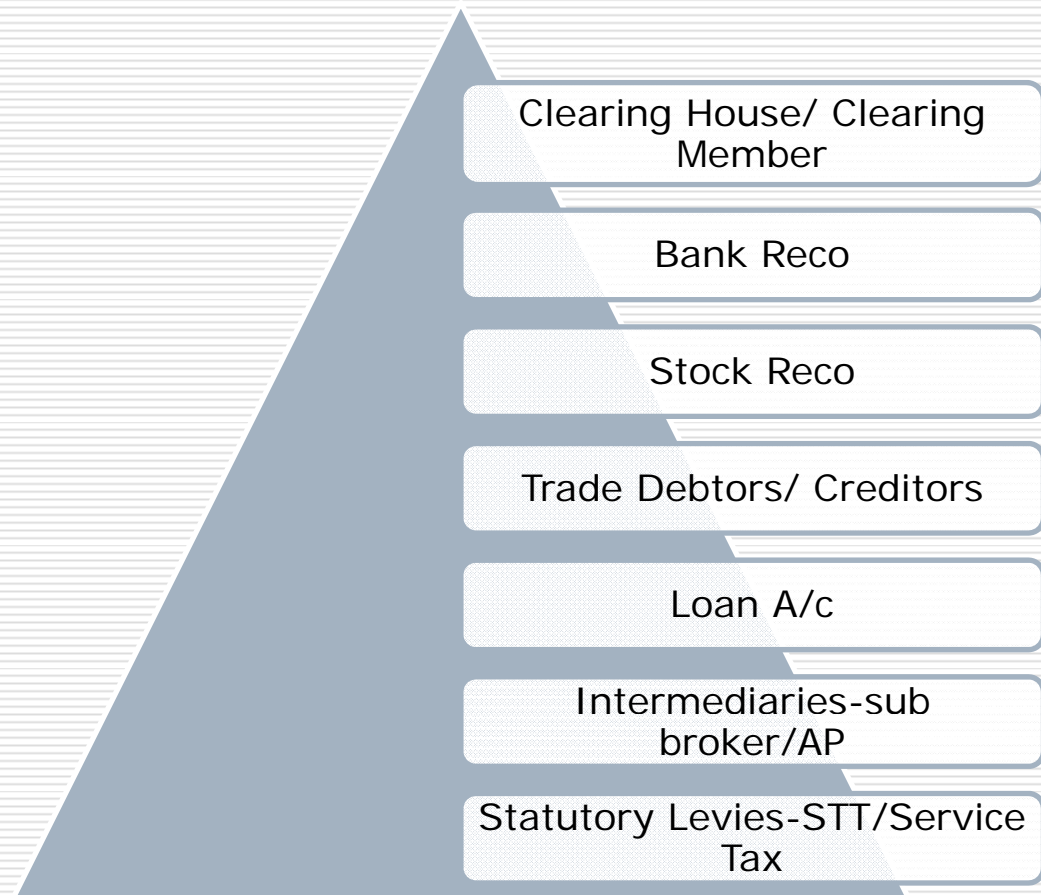
Auditor should verify that the Shares and securities are valued and disclosed in financial statement in accordance with recognized policies and relevant statutory requirement.

Check whether expenses incurred on account of transfer fees, stamp duty, brokerage etc. is included in cost of share and securities.

If Shares & Securities are held as stock in trade, Basis of valuation should be verified E.g. FIFO, Weighted Average cost etc.

Auditor should ensure consistency in valuation of Shares & Securities held as stock in trade

Reconciliations



Management representation

Obtain management representation in writing as to classification and valuation of Shares and securities for balance sheet purpose



However auditor is not relieved from his responsibility of performing the procedures to obtain sufficient appropriate audit evidence.

Disclosure

The Following should be disclosed in the Financial statement

- ❑ The Accounting Policies for determination of carrying amount of Shares & securities
- ❑ Significant restrictions on right of ownership, realisability of Shares & Securities or the remittance of Income & Proceeds of disposal

Disclosure

- ❑ The Aggregate Book Value of Quoted & unquoted Shares & Securities
- ❑ The Aggregate Market Value of Quoted & Unquoted Shares & Securities
- ❑ Requirements of Revised Schedule VI of The Companies Act relating to Shares & Securities
- ❑ Other Disclosures as specifically required by The Relevant Statute governing the enterprise.

Disclosure

Auditor should also ensure that the following minimum disclosures have been made In case of F&O Contracts:

- ❑ Category-wise quantitative data about derivative instruments that are outstanding at the balance sheet date.
- ❑ The purpose, viz., hedging or speculation, for which such derivative instruments have been acquired.

Disclosure

- ❑ In case where Bank Guarantees have been provided to Stock Exchange/ Clearing Corporation; necessary disclosures in contingent liability with respect to value of bank guarantee and the underlying collateral.
- ❑ In case where corporate guarantee has been provided for group companies; necessary disclosures should be provided in financial statements

Various Certifications

Exchange: BSE				
Sr. No	Document Type	Description	Certified By	Applicability
1	Annexure 1	Net worth Requirement & Method of Computation as per the type of membership	CA/ CS	All Members
2	Annexure 2	Net worth Certificate	CA/ CS	All Members
3	Annexure 3	Computation of Net worth (Exchange Prescribed)	---	All Members
4	Annexure 4	Computation of Networth (L.C.Gupta Format)	---	All Members
5	Annexure 5	Auditor's Report	---	All Members
6		Audited Balance Sheet & Profit & Loss Account	CA	All Members
Circular Reference: 20130604-25 dated 04 Jun 2013				

Exchange: NSE				
Sr. No	Document Type	Description	Certified By	Applicability
1	*Annual Accounts	Balance Sheet, P&L, Schedules & Notes to Accounts, Directors report & Auditors report	CA	For ALL Members
2	*C-1	Net worth Certificate along with the relevant computation	CA/ CS	For ALL Members
	**C-2	Details of Membership on other Stock Exchanges & Details of Listing	---	For ALL Members
	**C-3	Details of Directors/ Proprietors	---	Corporate/ Individual/ Banks/ PCM
	**C-6 For Partnership & C-7 Corporate & Banks	Details of Shareholding Pattern & Dominant Group of Corporate	CA/ CS	Corporate/ Partnership/ Banks

Exchange: NSE				
Sr. No	Document Type	Description	Certified By	Applicability
	**C-8	Undertaking for Relative Support to the Dominant Group	CA/ CS	Corporate/ Partnership
		OR		
3	C-10	Undertaking stating no changes in Documents C-2 to C-8	CA/ CS	For ALL Members
* Submission of these documents is mandatory for all the members.				
** With respect to the submission of documents C-2 to C-8 in following scenario 1 & 2, the member may submit document C-10 (Annexure No. 2.8) instead of submitting documents C-2 to C-8 as may be applicable:				
1. As per member's records, details of documents C-2 to C-8 as on March 31, 2013 are exactly the same as per the submissions of above documents made by the member as on March 31, 2012.				
OR				
2. Details of documents C-2 to C-8 as per the member's records as on March 31, 2013 are exactly the same as per records of the Exchange made available to the member as on March 31, 2013.				
Circular Reference: NSE/COMP/23669 dated 13 Jun 2013				

Exchange: MCX-SX

Sr. No	Document Type	Description	Certified By	Applicability
1	Annexure A #	Audited Financial Statement F.Y. 2012-13	CA	All Members
2	Annexure B	Net worth as on March 31, 2013	CA	All Members
3	Annexure C	Undertaking regarding status of details submitted	CA	All Members
4	Annexure D	Details of Directors/ Partners/ Proprietor	CA/ CS	All Members
5	Annexure E	Shareholding Pattern/ Partnership Pattern	CA/ CS	Individual/ Proprietor/ HUF/ Partnership/ Corporate/ Banks

Exchange: MCX-SX				
Sr. No	Document Type	Description	Certified By	Applicability
6	Annexure F	Details of Dominant Promoter Group/ Dominant Group of Partnership Firms	CA/ CS	Individual/ Proprietor/ HUF/ Partnership/ Corporate
7		Contact Details	---	All Members
8		Details regarding Membership of other Stock Exchanges	---	All Members
# Format not Available				
Circular Reference: MCX SX/MEM/1265/2013 dated 20 June 2013				

Depository: CDSL

Sr. no	Document Type	Description	Certified By	Applicability
1	Annexure D	Net worth certificate	Statutory Auditors	All Participants
2		Audited Financial Statement	Statutory Auditors	All Participants

Communiqué Reference: 945 dated 21, August 2007

Depository: NSDL			
Sr. no	Description	Certified By	Applicability
1	Audited Financial Statement	CA	All Participants
2	Networth Certificate	CA	All Participants
3	If DP is clearing member of the clearing corporation of any exchange, the details regarding any suspension/ termination or defaults or any disputes	---	All Participants
4	Number of Complaints received from Clients, their nature, status and manner of redresal, once every month	---	All Participants
5	Internal & Concurrent audit report	CA	All Participants
Reference: Handbook for NSDL Depository Operation Module, Chap 3- Business Partners of NSDL, Page 8			

Exchange: MCX				
Sr. No	Document Type	Description	Certified By	Applicability
1	ARI-1-3 for Individual/ HUF/ Proprietor/ Partnership ARC-1-4 for Corporate	Account and related statements	CA	For All Members
2	ARI-4 for Individual/ HUF/ Proprietor/ Partnership ARC-6 for Corporate	Networth Certificate	CA	For All Members
3	ARC-5	Schedule and Notes to the A/c submitted		Corporates
4	ARP- 5	Sharing Pattern	CA	Partnership Firm
5	ARC-7	Shareholding Pattern	CA	Corporates
6	ARI-6	Details of Proprietor/Individual/HUF	---	Individual/HUF/ Proprietor

Exchange: MCX				
Sr. No	Document Type	Description	Certified By	Applicability
7	ARP6 for Partnership & ARC-8 for Corporate	Details of Dominant Promoter Group (DPG)	CA	Corporate/ Partnership
8	ARC-9 for Corporate & ARP 7 for Partnership	Undertaking for Relative Support	CA	Corporate/ Partnership
9	ARC-10 for Corporate & ARP 8 for Partnership	Undertaking for Corporate Support along with Board Resolution for support	CA	Corporate/ Partnership
10	Individual/ Partnership/HUF/ Proprietor for ARI- 5, Corporate ARC-11 & ARP- 9 for Partnership	Details of other Exchange Membership in the Member Company / Sister Concern / Group Company And Details of Listing on Stock Exchanges	---	All Members

Exchange: MCX				
Sr. No	Document Type	Description	Certified By	Applicability
11	ARI6 for Individual/ HUF/ Proprietor ARC- 12 for Corporate & ARP 10 for Partnership	Details of Director / Society Member/ Partners/ Individuals/ HUF/ Proprietors	---	All Members
12	ARI 7 for Individuals/ HUF/ Proprietors, ARC- 13 for Corporate & ARP 11 for Partnership	Present contact details of the Member Entity	---	All Members
13	ARI 8 for Individuals/ HUF/ Proprietors, ARC- 14 for Corporate & ARP 12 for Partnership	Debarred and Suspended Undertaking	---	All Members

Exchange: MCX				
Sr. No	Document Type	Description	Certified By	Applicability
14	ARI 9 for Individuals/ HUF/ Proprietors, ARC- 15 for Corporate & ARP 13 for Partnership	Undertaking regarding status of documents submitted as on March 31, 2012	---	All Members
Documents to be submitted by Inactive Members				
1	ARI 10 for Individuals/ HUF/ Proprietors, ARC- 16 for Corporate & ARP 14 for Partnership	Declaration cum Confirmation from Inactive Members	---	All Members
2	ARI-4 for Individual/ HUF/ Proprietor/ Partnership ARC-6 for Corporate	Networth Certificate	CA	All Members
Circular Reference: MCX/MEM/335/2012 dated 28, September 2012				

Exchange: NCDEX				
Sr. No	Document Type	Description	Certified By	Applicability
1	Annual Accounts	Financial Statements (which includes Balance Sheet, Profit and Loss Account/ Income and Expenditure Account, Directors' and Auditor's Reports) duly certified by a Chartered Accountant (CA)	CA	For ALL Members
2	Annexure I (Balance Confirmation)	Balance Confirmation - Details of deposits with NCDEX outstanding as on March 31, 2012	CA	For ALL Members
3	C-1 and C-1A	Net worth Certificate along with computation sheet, duly certified by statutory auditors/CA.	---	For ALL Members
4	C-2	Details of other exchanges membership	---	For ALL Members

Exchange: NCDEX				
Sr. No	Document Type	Description	Certified By	Applicability
5	C-3	Details of Directors/Partners duly certified by CA/CS	CA/ CS	Corporate/ Partners
6	C-3A	Undertaking from Directors/Partners/ Proprietor	---	Corporate/ Partners
7	C-4	Details of Shareholding/Sharing Pattern duly certified by CA/CS	CA/ CS	Corporate/ Partners
8	C-5	Details of Dominant Promoter Group duly certified by CA/CS	CA/ CS	Corporate/ Partners
9	C-6	Undertaking from Relatives/Corporate entities supporting the Dominant Promoter Group duly certified by CA/CS	CA/ CS	Corporate/ Partners
10	D	Declaration of Members' Fidelity Insurance	---	For ALL Members
11	E	Declaration cum confirmation for Inactive Members (Applicable for Inactive Members only)	---	For ALL Members

Exchange: NCDEX				
Sr. No	Document Type	Description	Certified By	Applicability
12	F	Compliance Officer details	---	For ALL Members
13	G	Undertaking for Foreign Holding	---	For ALL Members
14	H	Member's Additional Details	---	For ALL Members
Circular Reference: NCDEX/MEMBERSHIP-004/2012/312 27, August 2012				

Open Forum



Thank You

Presented by CA. Kinjal Shah

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