INTERNAL AUDIT

FREQUENTLY ASKED QUESTIONS (FAQs)

1. To whom is Internal audit applicable?

All the stock brokers and clearing members, who have transacted or cleared even a single trade during the period of audit, are required to conduct the internal audit. It is applicable for Capital Market, Derivatives (F&O and CDS) and WDM segment of the Exchange.

2. When are the half yearly Internal audit report required to be submitted?

Members shall conduct Internal audit on a half yearly basis. For half year ending March 31st, audit reports along with management comments are required to be submitted by June 30th and for half year ending September 30th, same is required to be submitted by December 31st through ENIT only.

3. Who can conduct the Internal audit?

Internal audit can be conducted by Independent qualified Chartered Accountants, Company Secretaries, or Cost and Works Accountants, who are in practice and who do not have any conflict of interest with the member.

4. What is the scope of Internal audit?

Every half year Exchange stipulates minimum guidelines for Internal Audit. Scope of audit shall include areas such as:

a) Review of Order and Risk Management system.
b) Verification and review of Constituent Registration Documents.
c) Verification of systems for Margins collection from clients.
d) Verification/Review of Procedures and systems pertaining to dispatch of contract notes/Margin Statement/Statement of accounts.
e) Verification of systems and procedures in place for receipt/payments of funds/securities from/to clients.
f) Review of operations at branch and subbroker location.
g) Verification of internal controls of Terminal Operations at members office.
h) Review of documentation and implementation of Provisions pertaining to Anti Money Laundering (AML) Compliance.

i) Review/Verification of Systems in place to prevent and monitor code changes.

j) Verification and review of Investor Handling Mechanism etc.

k) Review of clearing activities in case of Professional Clearing member/ Members clearing trades of other trading members.

Guidelines prescribed by the Exchange does not limit the scope of Internal Audit.

5. Can Auditor verify any additional area other than defined in scope of Internal audit Report?

If in the opinion of the Auditor, it thinks that review is required for any other area it may undertake further examination for the same.

If any noncompliance is observed by the auditor, the same shall form part of the Internal Audit Report and commented under the head “Other Areas” as given in the format of Audit Report.

6. What is the format of the audit report?

The format for each half year is specified by the exchange in its circular for the respective half year. Such format/guidelines is updated/reviewed every half year by the Exchange. The report consists of Annexure I which is the Format of Audit Certificate and Annexure II which is the Format of Audit report. Annexures to the observations/adverse comments shall form part of the audit report. Member shall ensure that Management comments are given for adverse observations given by the auditor.

7. What should be the sample size to be adopted?

Internal Auditor has to atleast select minimum Sample size as prescribed under the guidelines issued by the Exchange. While conducting audit, wherever auditor feels appropriate it may take decision to increase the sample size.

8. What are the areas to be taken care of while finalization of Internal audit report?

While finalizing report certain basic areas to be taken care of are as given as under:

a. Each page of the Audit Report should be stamped by the auditors.
b. The Audit certificate should be on letterhead of the auditors containing the address and contact details of the auditors.
c. Minimum sample size should be adhered to and mentioned in the audit report.
d. The Audit Report must contain Management comments.
e. The Audit Reports should come through Members of the Exchange only (i.e. the audit report should be accompanied by a covering letter on the letterhead of the member).
f. The Audit Report should contain observations pertaining to the respective Exchange to which the report is submitted.
9. Is it necessary to indicate whether management accepts comments given by the auditor?

In case of any non–compliance, the management comments are necessary clearly specifying whether the management accepts the non–compliance or otherwise. Management is required to indicate the tentative timeliness to comply with the non-compliance reported by the auditor.

10. How to submit the Internal audit report?

Internal Audit report shall be submitted in Soft Copy through ENIT only. The same has to be in scanned pdf format / digitally signed by the member and shall form part of an attachment through ENIT. Detailed procedure for the same is explained in the Exchange circular no. NSE/INS/22076 dated November 6, 2012.

11. What is the maximum size of file upload on ENIT?

The members are required to upload the scanned copy of the complete internal audit report signed and stamped by the auditor along with all annexures and management comments in the PDF file in a zipped folder of the maximum file size of 10 MB.

12. On what grounds can the Exchange ‘Not Approve’ the reports submitted by the member?

The Exchange may reject or ‘not approve’ the reports of the members on the following grounds-

a) If the reports is not as per the format prescribe by the Exchange for that half year.

b) If the sample size of the audit report is not as per the minimum prescribed by the Exchange

c) If the management comments are not provided in the report for the questions where the auditor has pointed out non-compliance.

In the above cases the Exchange may reject the report and the members are required to make further/revised submissions to make good the deficiencies.

13. How to make any further submission on ENIT?

In case the request has not been approved by the Exchange, the request status will change to “Not Approved” and in order to make revised/ further submission the member needs to click on this request reference no. and browse and upload the fresh submission.

14. In case of Members having multiple branches/sub brokers, is it necessary to cover all branches/subbrokers for audit?

Auditor shall perform audit of branches/sub brokers on sample basis. Factors such as Volumes generated from such location (branch/sub broker), geographical coverage,
number of terminals allotted by the broker, number of years of operation, periodicity of last visit etc. may be guiding factors for sample selection.

15. What is the penalty for non-submission/delayed submission of Internal audit reports?

As per exchange Circular No. NSE/INSP/23196, dated April 11, 2013, following shall apply in case of non submission/late submission of Internal Audit Reports by due date.

<table>
<thead>
<tr>
<th>PARTICULARS</th>
<th>ACTION</th>
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<tbody>
<tr>
<td>Non submission of internal audit report to the Exchange within 3 months</td>
<td>Charges of Rs.100/- per day after the due date till the last day of 3rd</td>
</tr>
<tr>
<td>Non submission of internal audit report to the Exchange for more than 3</td>
<td>months from the due date till the date of submission of the report.</td>
</tr>
<tr>
<td>Non submission of Internal Audit Report to the Exchange beyond 6 months</td>
<td>Disciplinary action as may be decided by the relevant authority which</td>
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<td>from the due date of submission of the report</td>
<td>may also include withdrawal of trading facility.</td>
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16. Is there any action for non compliances pointed out by Auditor in Internal audit report?

Internal Audit Report received are analyzed and non compliances observed are monitored and placed before appropriate authority for appropriate action. Further Exchange has issued Circular No. NSE/INSP/2011/115 dated March 28, 2011 containing indicative list of penalties/actions to be initiated regarding audit observations in Internal Audit Reports. The penalties are indicative in nature and could undergo change in specific cases depending on frequency and gravity of violations.