

STOCK & BOOK DEBT VERIFICATION (STOCK AUDIT)

STANDARD OPERATING PROCEDURE (SOP)

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Why Stock Audit !!!

- ❖ RBI Stipulation
- ❖ Bank Guidelines (Audit Committee Stipulation)

[Main Objective of Stock Audit is to do Independent verification of Borrower's factory sites and do analysis of borrower's Stock & Debtors Position vis-à-vis Drawing Power availed by the Borrower]

Step by Step Process

- ❖ Allotment of Stock Audit by Zonal Office/Regional Office/Branch
- ❖ Acceptance Letter to be send to respective department
- ❖ List of Documents send to Branch & Borrower
- ❖ Visit plan based on Factory Site Location
- ❖ Branch & Borrower document in depth Analysis
- ❖ DP Calculation Structure
- ❖ Draft Stock Audit Report share with Respective Branch (Optional)
- ❖ Report Finalized

List of Documents - Branch

- ❖ Latest Sanction Letter
- ❖ Last 3 Detailed Stock Statement Submitted to Bank
- ❖ Last 1 year Working Capital Account Statement and Term Loan Statement
- ❖ Last Inspection Report of Bank Official Visit
- ❖ Latest Quarterly Statement Submitted to Bank (QIS/QPR)
- ❖ Last Stock Audit Report
- ❖ Insurance Policy of Stock, P&M and Collateral Securities

List of Documents - Borrower

- ❖ Detailed Stock Statement as on Date of Visit
- ❖ Last 3 Detailed Stock Statement Submitted to Bank
- ❖ Provisional Accounts as on Last Stock Statement Submitted
- ❖ Provisional Accounts as on Date of Visit
- ❖ Month Wise Purchase & Sales Summary of Last 12 Months till date of Visit
- ❖ Last Tax Audit Report
- ❖ GST3B of Last 6 Months
- ❖ Sister Concern Ledgers of Last 6 Months
- ❖ Purchase & Sales Sample Bills
- ❖ Detailed Debtors Statement (Top 5 debtors) – Last 3 months

Factory Visit – Important Aspects (1 / 2)

❖ Verification of Stock – Able to Count

- Verified using Stock Sheet maintained at Factory
- Random Verification in case of Sizeable Quantity of Stock
- Communication with Store Keeper regarding Stock Register and Stock Taking Frequency
- Verification of Label/Expired Date/Old Stock/Non Usable Stock
- Obtained Stock position as on date of visit from Borrower (Will be used in depth analysis part later on)

Factory Visit – Important Aspects (2/2)

❖ Verification of Stock – Unable to Count

- Verification of Stock Sheet maintained at Factory
- Verification of Godown Capacity and actual availability of stocks
- Obtained Stock position as on date of visit from Borrower (Will be used in depth analysis part later on)
- Observe level of activity at factory such as no. of workers, machinery working, in-out register etc.

Branch document in depth Analysis (1 / 3)

➤ **Major points verify in Sanction Letter**

- Limit used (Fund, Non Fund, Sub Limit, Restriction of Limit, Peak, Non Peak Season Limit)
- Drawing Power Stipulations;
 - Margin on Stock & Debtors
 - Book Debts Days to be taken
 - Associate Book Debts
 - Accepted Level of Creditors
- Financial Position at the time Sanction and Financial Projection verification – Report in case projection are not achieve as on date of Visit and comment upon
- Verification of Special Conditions imposed and adherence thereto at the time of Stock Audit Report
- Collateral Security – Verify Valuation Date – Not more than 3 years at the time of Stock Audit Visit

Branch document in depth Analysis (2/3)

- **Stock Statement submitted to Branch** – Cross verify with Stock Statement submitted to us during Stock Audit and comment upon any difference
- **Verify Working Capital Statement**
 - Last 6 Months/1 year credit summation and compare with Sales during the period. Non-Bonafide entries to be ignored – such as month/quarter/year end full utilization of limit and reversal of amount in next working day
 - Average Utilization more than 95% - Early Warning Signals
 - Limit outstanding more than Drawing Power – Early Warning Signals
 - Frequent Cheque Bounce - Early Warning Signals
 - Last 3 months interest paid frequency to be verify
- **Verify Term Loan Statement**
 - Serving EMI on Regular or not
 - Penal Interest charged
 - Source of Payment of Term Loan EMI

Branch document in depth Analysis (3/3)

- **Verify Latest Inspection Report of Bank Official Visit**
 - Not more than 6 months old
 - Any adverse comments by Bank Official During Recent visit
- **Latest Quarterly Statement Verification**
 - Financial Figures Comparison of Actual vis-à-vis Projection
- **Last Stock Audit Report**
 - Any adverse comments by Previous Stock Auditor
- **Verification of Insurance Policy**
 - Stock has been insured (As per Sanction note)
 - Location of Risk and Hypothecation Clause verify
 - Validity of Insurance Policy

Borrower document in depth Analysis (1 /5)

➤ Drawing Power Calculation – Method I – Reversal Method

Sr. No.	Particular	Amount
1.	Value of Stock (as on Date of Visit)	(A) XXXX/-
2.	<u>Add: Cost of Goods Sold during (Last Stock Statement Submitted till Date of Visit)</u>	
	Sale during the period (I)	XXX/-
	Gross Profit @ % (II) – <u>GP to be taken of Based on Average of last 2 Years</u>	XXX/-
	Cost of Goods Sold (I-II)	(B) XXXX/-
3.	<u>Less: Purchase during (Last Stock Statement Submitted till Date of Visit)</u>	(C) XXXX/-
4.	Value of Stock (as on Date of Last Stock Statement Submitted) (A+B-C)	XXXXXX/-

- Compare the Value of Stock arrived by us with Stock Statement Submitted. Comment in case major variation observed – Early Warning Signals
- Acceptable Level – **10 to 15% variation.**

Borrower document in depth Analysis (2/5)

- Drawing Power Calculation – Method II – Gross Profit Method

Particulars	Amount
Sales	XXXX
GP @ % GP to be taken of Based on Average of last 2 Years (A)	XXXX
Actual GP shown (B)	XXXXX
Difference C= (B-A)	XXXXXX
Stock as per Stock Statement (D)	XXXXXX
Difference of stock as above C (E)	XXXXXX
Actual Stock as per GP method F = (D-E)	XXXXXXX

- Compare the Value of Stock arrived by us with Stock Statement Submitted. Comment in case major variation observed – Early Warning Signals
- Acceptable Level – **10 to 15% variation.**

Borrower document in depth Analysis (3/5)

➤ Provisional Account & Audit Report Verification

- Achieving Projection, Top Line Variation, Bottom Line Variation, Dilution of Equity including Quasi Equity, Other Lenders Debt
- Comparison of Creditors & Debtors Reported as per Stock Statement vis-à-vis Provisional and Comment upon any major variation
- Diversion of Funds
- Serving of Outside Liabilities and Penalty and Interest Paid verify from profit and loss and comment upon
- For Stress Borrower – Obtain last 6 months utility bills

Borrower document in depth Analysis (4/5)

➤ **GST data verification**

- Comparison of Month Wise Sales & Purchase with GST Return Submitted
- Verify any Interest or Late Fees imposed
- Check from GST Portal regarding frequency of GST return filled during last 1 year and comment upon

➤ **Sister Concern Ledgers verification**

- Random verification for transactions are done on Arm's Length price
- Loans given or not and comment any adverse entries specially related to diversion of funds
- Debtors to be exclude in DP calculation (if stipulated in Sanction Note)

➤ **Sample Bills verifications**

- Verify Latest Purchase & Sales bills of major products
- Raw Material Unit rate as mentioned in Stock Statement to be align with Latest Purchase bills
- Finished Goods Unit rate as mentioned in Stock Statement to be align with Latest Sale bills (after giving effect of GP)

Borrower document in depth Analysis (5/5)

➤ **Detailed Debtors Statements verification of Last 3 Months/6 Months**

- Age wise debtors are reported in Stock Statement. However we need to cross verify if it is genuine figures or not! - Based on Debtors Statement Verification
- Opening Balance before 3/6 Months – Sales During 3/6 Months – Collection During 3/6 Months
- FIFO method to be used for collection of dues – Arrived at Age wise outstanding based on our working and compare with Age wise debtors submitted by Borrower in Stock Statement. Comment upon any adverse observations.

DP Calculation Structure

PARTICULARS		Amount
Stock of Raw Material		
Less : Creditors		
Stock in Process		
Stock of Finished Goods		
Net Paid Stocks		XXXX
Less : Advances From Customers		
Less : Margin (As Per Stock Statement)		
Value of Stock for D.P.	A	XXXXX
Eligible Debtors (Below 90/180 Days)		
Less : Book Debt from Sister concern		
Less : Margin (As Per Stock Statement)		
Value of Debtors for D.P.	B	XXXXX
Drawing Power as per audit	A + B	XXXXXX
Drawing Power as per borrower	C	XXXXXX
Balance Outstanding as on Last Stock Statement Submitted	D	XXXXXX
Shortfall in Drawing Power	D-(A+B)	XXXXXXX

- **Bank wise DP Calculation Method will be different.**
- **Proper Care to be taken for Preparing DP Calculation Sheet (as it is Considered to be Heart & Brain of Stock Audit Report)**

Finalization of Reports

- Based on early warning signals report to be finalized
- Drawing Power Calculation be backed with perfect justification
- Clarify with Bank Official and Borrower in case of any doubt
- Give Reasonable Opportunity in case there is shortfall in Drawing Power
- All Major Observations compile at the end of report and the same will be backed with perfect justification

PRATICLE APPROACH



**DISCUSS DOUBTS & SHARING PRATICLE
EXPERIENCE**

DSKHTP & ASSOCIATES LLP



Thanking You
Suggestions are appreciated

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