Annexure – 5a

TERMS OF REFERENCE
FOR
STATUTORY AUDIT

I. BACKGROUND

1. The World Bank is providing assistance to Integrated Coastal Zone Management (ICZM) project being implemented by the Government of India (GoI) and the State Governments of Gujarat, Orissa and West Bengal.

2. GOI's Ministry of Environment & Forests (MoEF) will have the lead responsibility for project implementation and ensuring that the project development objectives are met. The Department of Forest & Environment (DoFE) of each of the three participating states will be the key partners of MoEF in project implementation. Each of these four partners have set up special purpose vehicles in the form of registered societies (National and State level PMUs), to exclusively lead and coordinate project activities on a full time basis and directly implement some of the project sub components.

3. National Project Monitoring Unit (NPMU) and each State Project Monitoring Unit (SPMU) will have multiple line departments as Project Executing Agencies (PEA) who will also incur expenditure under the project. Each office responsible for incurring expenditure under the project is an Accounting Center (AC). Hence NPMU & PEA under NPMU as well as SPMU and PEA under SPMU will be the Accounting Centers under the project. Each AC will be subject to the normal financial supervision under the project including timely reporting, compliance with project Financial Management (FM) guidelines as documented in the Financial Management Manual (FMM), audit etc. Each PEA has designated a senior officer as Nodal officer of that department. Nodal officer of each PEA is the person primarily responsible for implementation of sound FM guidelines for the ACs under him..

4. The financial policies & accounting procedures adopted by NPMU & SPMUs are guided by Financial Management Manual (FMM) approved by the World Bank.

5. The Project accounts (books of account, documents & records) provide the basis for preparation of Internal Unaudited Financial Reports (IUFRs) and Project Financial Statements (PFS) and are established to reflect the financial transactions in respect of the project as maintained by the PEAs of various SPMUs and NPMU.

6. The accounting entries of the project will be made at various ACs and these will need to be consolidated at SPMU and subsequently at NPMU to get financial information for the project as a whole.

II. OBJECTIVE

7. The essence of the World Bank audit policy is to ensure that the Bank receives adequate independent, professional audit assurance that the proceeds of World Bank loans were used for the purposes intended, that the annual project financial statements are free from material misstatement, and that the terms of the loan agreement were complied with in all material respects. The objective of the audit of the Project Financial Statement (PFS) is to enable the auditor to express a professional opinion as to whether –

   a) The PFS present fairly, in all material respects, the sources and applications of project funds for the period under audit examination,
   b) The funds were utilized for the purposes for which they were provided, and
   c) Expenditures shown in the PFS are eligible for financing under the relevant loan or credit agreement.

   In addition, the auditor will express a professional opinion as to whether the Financial Management Reports submitted by project management may be relied upon to support any applications for withdrawal.

   The books of account that provide the basis for preparation of the PFS are established to reflect the financial transactions of the project and are maintained by the NPMU, SPMU and PEA in their respective office.

8. Standards

The audit will be carried out in accordance with the Auditing Standards promulgated by the Comptroller and Auditor General of India. The auditor should accordingly consider materiality when planning and performing the audit to reduce audit risk to an acceptable level that is consistent with the objective of the audit. Although the responsibility for preventing irregularity, fraud, or the use of loan proceeds for purposes other than as defined in the legal agreement remains with the borrower, the audit should be planned so as to have a reasonable expectation of detecting material misstatements in the project financial statements.

9. Scope[1]

The audit will be conducted for the entire project, i.e., NPMU & SPMU. In conducting the audit, special attention should be paid to the following:

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[1] *In response to identified project risks, the scope may be expanded to include a report or the expression of an opinion on specific aspects of the operation such as internal controls, compliance with Bank procurement policies, or efficiency and effectiveness in the use of loan proceeds.*

(a) All external funds have been used in accordance with the conditions of the relevant legal agreements and only for the purposes for which the financing was provided. Relevant legal agreements include the Financing Agreement, the Project Agreement, Grant Agreement and the Minutes of Negotiations;

(b) Counterpart funds have been provided and used in accordance with the relevant legal agreements and only for the purposes for which they were provided;

(c) All necessary supporting documents, records, and accounts have been kept in respect of all project transactions including expenditures reported via IUFR where applicable. Clear linkages should exist between the books of account and reports presented to the Bank; and

(d) The project accounts have been prepared in accordance with consistently applied Government Accounting Standards[2] and present fairly, in all material respects, the financial situation of the project at the year end and of resources and expenditures for the year ended on that date.

10. Project Financial Statements

The Project Financial Statements should include-

A. Statement of Sources and Applications of Funds: The formats of PFS are set out in Annexure 1.

B. Reconciliation of Claims to Total Applications of Funds. The PFS include reconciliation between expenditure reported as per the Statement of Sources and Applications of Funds and expenditure claimed from the World Bank through report based methods of reimbursement. The formats are outline in Annexure 2.

C. Other Statements or Schedules as may be applicable in particular circumstances and as specified in the relevant legal agreements, such as:

- A statement showing appropriate major heads of expenditure. (say by Project Component/Sub-components)
- A summary of cumulative expenditures by category of expenditure such as buildings, equipment, furniture, vehicles, major rehabilitation of canals etc

D. Management Assertion: Management should sign the project financial statements and provide a written acknowledgement of its responsibility for the preparation and fair presentation of the financial statements and an assertion that project funds have been expended in accordance with the

[2] *Until such time as the pronouncements of the Government Accounting Standards Advisory Board are accepted and prescribed by the Ministry of Finance, the accounting standards followed by the Government of India will be defined by the General Financial Rules, PWD codes, Treasury codes and similar financial rules and codes as are in effect and applicable to the operations of the project.*

intended purposes as reflected in the financial statements. An example of a Management Assertion Letter is shown at Annexure 3.

11. Financial Management Reports

In addition to the audit of the PFS, the auditor is required to audit all Financial Management Reports (FMRs) for withdrawal applications made during the period under audit examination. The auditor should apply such tests as the auditor considers necessary under the circumstances to satisfy the audit objective. In particular, these expenditures should be carefully examined for project eligibility by reference to the relevant financing agreements. Where ineligible expenditures are identified as having been included in withdrawal applications and reimbursed against, these should be separately noted and qualified by the auditor.

12. Audit Report

An audit report on the project financial statements should be prepared in accordance with the Auditing Standards[3] promulgated by the Comptroller and Auditor General of India. Those standards require an audit opinion to be rendered related to the financial statements taken as a whole, indicating "unambiguously whether it is unqualified or qualified and, if the latter, whether it is qualified in certain respects or is adverse or a disclaimer of opinion."[4] In addition, the audit opinion paragraph will specify whether, in the auditor's opinion, (a) with respect to FMRs, adequate supporting documentation has been maintained to support claims to the World Bank for reimbursements of expenditures incurred; and (b) except for ineligible expenditures as detailed in the audit observations, if any, appended to the audit report[5], expenditures are eligible for financing under the Loan/Credit Agreement.

The project financial statements and the audit report should be received by the Bank not later than 6 months after the end of the fiscal year. The auditor should also submit two copies of the audited accounts and audit report to the Implementing Agency.

The audit report is issued without prejudice to CAG's right to incorporate the audit observations in the Report of CAG of India for being laid before Parliament/State or UT Legislature.

13. Management Letter

In addition to the audit report on the project financial statements, the auditor may prepare a management letter containing recommendations for improvements in internal control and other matters coming to the attention of the auditor during the audit examination.

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[3] *Relevant CAG Auditing Standards are reproduced in Annexure 5.*

[4] *See relevant portions of Auditing Standards of the Comptroller and Auditor General of India as applicable from time to time.*

[5] *A sample audit report wording for an unqualified audit opinion is shown at Annexure 4.*

Where a management letter is prepared by the auditor, a copy of the same will be supplied to the Bank. Else, a written advice may be made that no management letter was prepared together with the audit report on the project financial statements.

III. KEY PERSONNEL

14. The list of key personnel required for the audit is as under:

S.No.	Key Professionals	Description of Services to be provided	Experience	No. of persons	Total Man months per year per person
1	Partner	Overall coordination, & planning, team leadership, reporting, liaison with client	Qualified Chartered Accountant with at least 15 years experience as a partner with expertise in statutory audit of external aided projects, its planning, execution and reporting	1	0.5
2	Audit Manager	Coordinating & planning, reporting & liaison with client	Qualified Chartered Accountant with at least 7 years experience with expertise in statutory audit of external aided projects	1	1
2	Audit Team Leader	Responsibility to lead the audit teams in the field, planning and execution of the audits, discussion with SPMU / PEAs and report writing and finalization.	Qualified Chartered Accountants with at least 5 years experience in statutory audit of external aided projects, with ability to lead and team and interact with senior level govt officials	4	2
3	Team Member	Field level audit of works departments - (mainly relating to civil works)	Person with experience in works accounting & audit procedures and PWD codes etc	1	2

4	Team Member	Field level audit of line departments including community groups and sample physical verifications of activities/ assets.	CA Inter with experience in internal audit and report writing.	8	2

IV. FACILITIES TO BE PROVIDED BY THE NPMU / SPMU

15. The auditor will be given access to all legal documents, financial management manual, operations manual, government orders/ circulars, World Bank Procurement Guidelines correspondence, monthly financial statements, Project Financial Statements, IUFRs and any other information associated with the project and as deemed necessary by the auditor.
16. The auditors will also be given access to all the assets selected for physical verification by the auditors.
17. No services other than those specifically mentioned in this TOR shall be extended to the auditor. The auditors shall make their own conveyance arrangements.
18. No expenditure on traveling/ boarding/ lodging expenses (TA/DA etc) will be borne by the NPMU/ SPMU separately and the consultant shall include such cost in his proposal.

General

The auditor should be given access to any information relevant for the purposes of conducting the audit. This would normally include all legal documents, correspondence, and any other information associated with the project and deemed necessary by the auditor. The information made available to the auditor should include, but not be limited to, copies of the Bank's Project Appraisal Document, the relevant Legal Agreements, a copy of these Guidelines, and a copy of the Bank's Financial Management Assessment of the project entity. It is highly desirable that the auditor become familiar with other Bank policy documents, the Bank's internal guidelines on Financial Management that include financial reporting and auditing requirements for projects financed by the World Bank. The auditor should also be familiar with the Bank's Disbursement Manual. Both documents will be provided by the Project staff to the auditor.

Annexure 1

Statement of Sources and Application of Funds

TO BE INSERTED

Annexure 2

Reconciliation of Claims to Total Applications of Funds

TO BE INSERTED

Annexure 3

Example of a Management Assertion Letter[6]

(Project Letterhead)

(To Auditor) (Date)

This assertion letter is provided in connection with your audit of the financial statements of the _____ Project for the year ended _____. We acknowledge our responsibility for the fair presentation of the financial statements in accordance with the cash basis of accounting followed by the Government of India, and we confirm, to the best of our knowledge and belief, the following representations made to you during your audit:

- .....
  The project financial statements are free of material misstatements, including omissions.
- .....
  Project funds have been used for the purposes for which they were provided.
- .....
  Project expenditures are eligible for financing under the Loan/Credit agreement.
- .....
  There have been no irregularities involving management or employees who have a significant role in internal control or that could have a material effect on the project financial statements.
- .....
  We have made available to you all books of account and supporting documentation relating to the project.
- .....
  The project has complied with the conditions of all relevant legal agreements, including the Financing Agreement, the Project Agreement, the Project Appraisal Document, the Minutes of Negotiations, and the Borrower's Project Implementation Plan.

_____
(Project Director)

_____
(Senior Financial Officer)

[6] *This sample management assertion letter is based on ISA 580, "Management Representations," Handbook of International Auditing, Assurance and Ethics Pronouncements, International Federation of Accountants, 2007*

Annexure 4

Sample Audit Report—Unqualified Opinion[7]

Report of the Comptroller and Auditor General of India

Addressee[8]

Report on the Project Financial Statements

We have audited the accompanying financial statements of the _____ Project financed under World Bank Grant No._____, which comprise the Statement of Sources and Applications of Funds and the Reconciliation of Claims to Total Applications of Funds[9] for the year ended _____, these statements are the responsibility of the Project's management. Our responsibility is to express an opinion on the accompanying financial statements based on our audit.

We conducted our audit in accordance with the Auditing Standards promulgated by the Comptroller and Auditor General of India. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audit examines, on a test basis, evidence supporting the amounts and disclosures in the financial statements. It also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements present fairly, in all material respects, the sources and applications of funds of _____ Project for the year ended _____ in accordance with Government of India accounting standards.[10]

In addition, in our opinion, (a) with respect to FMRs, adequate supporting documentation has been maintained to support claims to the World Bank for reimbursements of expenditures incurred; and (b) except for ineligible expenditures as detailed in the audit observations, if any, appended to this audit report, expenditures are eligible for financing under the Loan/Credit Agreement. During the course of the audit, FMRs (each application no. and amount to be indicated) and the connected

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[7] *See relevant portions of Auditing Standards of the Comptroller and Auditor General of India as applicable from time to time for conditions where unqualified, qualified, adverse or disclaimers of opinion may appropriately be rendered.*

[8] *The auditor's report should be addressed to the person stipulated in the underlying loan agreement as responsible for providing audited project financial statements.*

[9] *Insert titles of other required statements and schedules included in or annexed to the project financial statements, if any.*

[10] *Until the Ministry of Finance prescribes adoption of the accounting standards pronounced by GASAB or other body such as IPSAS, the accounting standards followed by the Government of India shall be the cash basis of accounting applied with due regard to the General Financial Rules, PWD codes, Treasury codes and similar financial rules and codes as are in effect and applicable to the operations of the project.*

documents were examined and these can be relied upon to support reimbursement under the Loan/Credit Agreement.

This report is issued without prejudice to CAG's right to incorporate the audit observations in the Report of CAG of India for being laid before Parliament/State or UT Legislature.

[Auditor's Signature]

[Auditor's Address]

[Date[11]]

[11] *The report should be dated as of the date to which the auditor has become aware of and considered the effects of events and transactions. This is generally the final date of fieldwork, as opposed to the date of signing the audit report.*