

TERMS OF REFERENCE
FOR
INTERNAL AUDIT
OF
JAGDULLA HYDROPOWER COMPANY LIMITED
FOR THE PERIOD 2078/79

1. Background

Jagdulla Hydropower Company Limited (JHCL) is a hydropower company in Nepal established aiming for the development of hydropower projects. JHCL is developing Jagdulla Hydroelectric Project (JHEP) of 106 MW. The project site is located 750 KM west of Kathmandu on Jagdulla river of Dolpa district.

2. Scope and Objectives of Internal Auditing

Internal auditing activities include one or more of the following:

- a) Assess whether proper internal control system are operating effectively and efficiently.
- b) Verify the extent of compliance of policies and procedures laid down by the management.
- c) Ensure that all the items of income and expenses are within the delegated authority, properly accounted, correct in amount and consistent with organization policy.
- d) Determine that assets are adequately safeguarded and liabilities are properly disclosed.
- e) Examine the records and documents and various operational level and also to ensure that they are properly accounted and documented.
- f) Determine that the records of the bank are complete and adequate and that transaction is properly and timely recorded in the accounts.
- g) Compare the actual figure with the budget and find out the cause for deviation, if any.
- h) Review and follow up of last reports.
- i) Carrying out any other responsibility assigned by the management from time to time.
- j) Coverage of effectiveness and efficiency of accounting practice followed by company, fund management and financial reporting.
- k) Coverage of effectiveness and efficiency of Information technology and Communication system, Asset and Inventory Management System, Human

resource management System, HR policies, manual, Procurement plan process and control system of company.

- l) Review of Strategic risk, Business Risk and operational risk and specific to the company.
- m) Coverage of effectiveness and efficiency of Contract management system, corporate governance, legal compliance and statutory reporting of the company.
- n) Assessment of efficiency and effectiveness of business operation, detection and prevention of errors/ fraud/theft, Safeguard of assets, Accuracy and completeness of accounting data, Compliance with legal requirements, MIS, Administrative process, document control system Adherence to policies and plans of the company.

3. Overall Approach and Methodology

Internal audit shall be carried based on the following overall approach in the following Phase:

Phase	Overall Approach
Desk review of the reports and other related documents	<ul style="list-style-type: none"> ▪ Desk review of existing documents, audit reports (Internal/External), and other relevant documents; guidelines and memo issued by JHCL.
Risk Assessment Procedures	<ul style="list-style-type: none"> ▪ Based on the experience, desk review, reports of the internal/external auditors, budget areas, and Risk Assessment procedures shall be carried out accordingly. ▪ The risk areas shall be finalized in consultation with the management.
Review of Operation - Field Visit	<ul style="list-style-type: none"> ▪ Based on the desk review and risk assessment process, internal auditors shall perform field work.
Reporting	<ul style="list-style-type: none"> ▪ Reportable Issues shall be discussed and draft management letter shall be issued to the management. ▪ Final management letter to be issued after incorporating the management comments.

4. Planning of the internal audit

The auditor shall adequately plan the internal audit engagement well in advance of the work and ensure the execution of the internal audit of highest professional quality in an economical and efficient manner and within the agreed timetable.

On the basis of the information received during the planning phase, including his/her review risk assessment, the auditor shall determine:

- the type of transactions to be reviewed and the review method (full or random sample);
- the type of physical verifications and the sites to be selected;
- the site visits to be planned (if any)

The auditor undertakes to ensure continuity in the review approach of the internal audit engagement and the review team, even if there is a change in the leader of the review team from the prior year

5. Detailed internal audit procedures

Appropriate review procedures are to be applied by the auditor in order to form a professional judgement on the matters outlined below. These procedures applied, either on a full scope or random basis may include: controls, checking, evaluation, inspection, interview, analysis and other review techniques. When selecting the review procedures, the auditor shall give consideration to the results of his review risk assessment (during planning stage and during the course of the review work).

Accordingly, the auditor must define and carry out suitable review tasks in order to obtain an overview of the aforementioned aspects before s/he assesses the individual findings and reaches a final independent decision on the review.

The auditor is expected to select and apply any other review procedures that he may consider necessary in the professional execution of the internal audit engagement.

6. Additional work

If management required specific task to be performed not covered above, time and fees for such tasks shall be agreed mutually prior to undertaking the task.

7. Principles

Specific examples of possible review procedures are mentioned hereunder:

7.1 Principles of orderliness (financial regularity)

Project related matters:

- a) Authorizations/approvals of expenditures and validity with supporting documents,
- b) Physical existence and movements of the goods representing the property of the project (fixed assets, inventory items, current assets),
- c) Allocation of expenditures in conformity with the agreed budget(s),
- d) Conformity of local contracts with local legislation currently in force,
- e) Disposition and implementation of observations, adjustments and recommendations resulting from previous internal audit reports.

Accounting related matters:

- o) Arithmetic exactitude of the accounts, supporting documents and financial statements and reports,
- p) Correctness of the accounting entries,
- q) Timeliness of recording economic events and transactions in the general ledger accounts,
- r) Financial statements and report information in agreement with the general ledger accounts,
- s) Assessment of accounts receivable and advances; justification for overdue/unpaid amounts in excess of one month,
- t) Reconciliation of balances of cash in hand and in banks with the general ledger accounts,
- u) Disposition and implementation of observations and recommendations as well as adjustments and recommendations resulting from previous external/internal audit and/or audit reports.

7.2 Existence, adequacy and effectiveness of the Internal Control System (ICS)

- a) Adequacy of the internal organization (structures, functions, tasks, authority, responsibilities, methods, procedures, segregation of duties etc.),
- b) Effectiveness of project and financial accounting and reporting processes,
- c) Adherence to applicable laws, regulations and instructions,
- d) Physical safeguard of assets,

- e) Prevention of accounting errors and financial fraud,
- f) Adequacy and completeness of information and financial reporting system.
- g) Existence and application of adequate measures in the internal control system (ICS) in respect of the utilization of committed resources;

7.3 Conformity with the project objectives and adherence to the contract conditions

- a) Agreement of transactions, expenditures and receipts by comparison with the basic project documents (project description, programs of activities, contracts, terms of reference, budgets etc.);
- b) Verification that goods purchased with allocated funds are utilized within the defined objectives and are still available or have been disposed/sold in conformity with the procedures defined in the project agreement/contract;
- c) Verification whether the clauses of the project agreement/contract have been respected;
- d) Verification that the expenditures correspond to the agreed budgets. Analysis of deviations between budgeted and actual expenses and substantiation of major budget variations (+/- 10 % of the budget).

7.4 Economical conduct of business and effective use of financial resources

- a) Financial resources are utilized optimally for the activities, as stipulated in the agreement, contract with the consultant/implementer and terms of reference, always ensuring an appropriate level of cost and benefits (value for money);
- b) Application of management procedures relative to the various project transactions. In particular, adequate segregation of duties for vital functions and processes, like entering commitments, authorizing and accounting of expenditures, reconciliation of cash on hand and in banks, follow-up on long outstanding debtors and creditors, physical control over inventories, etc.);
- c) Expenditures are in line with the agreed budget positions;
- d) Any deviations of actual expenses from the agreed budget are reasonably explained and adequately documented by the project management
- e) Existence of adequate bid and purchasing procedures. e.g. best cost/benefit ratio for materials and services, conformity of price offers with local practices and cost levels;
- f) Confirmation that prices and rates are subject to regular verification and that the accounting system in use is adequate to the requirements of a management tool, particularly as it concerns cost analysis;

- g) Review and substantiation of expenditures of local and foreign experts/consultants (rent, travel expenses, accommodations, allowances etc.);
- h) Review and substantiation of expenditures related to national staff (gross salary, social and pension contributions, income taxes etc.);
- i) Existence of the vehicle logbook and verification that private use of vehicles has been invoiced and paid;
- j) Verification that private use of mobile and fix net phones by members of the staff has been invoiced and paid.

7.5 Others

- a) Advice on policy related issues.
- b) Tracking of improvement observation over quarters.
- c) Submit quarterly/ annual report to audit committee, specifying the major highlight of the observation and improvements in the process/control/mechanism.

Findings and recommendations

In the internal audit report, the auditor is expected to

- explain and quantify any adjusting and/or reclassification entries including compliance issues; and
- Formulate recommendations for the improvement of the internal control system (ICS) as well as of project and accounting procedures.

8. Findings and recommendations

In the internal audit report, the auditor is expected to

- explain and quantify any adjusting and/or reclassification entries including compliance issues; and
- Formulate recommendations for the improvement of the internal control system (ICS) as well as of project and accounting procedures.

9. Closing meeting

After the completion of the internal audit engagement, but before leaving the project or the premises, the auditor shall hold a closing meeting with the appropriate level of management, process owners and the staffs responsible for accounting and reporting.

The meeting shall address the results of the project review, discuss major weaknesses in the project, administrative and financial management (including the deficiencies of individual staff members) and propose recommendations to improve the project management, the accounting procedures and the internal control system (ICS) which shall be later communicated through management letter.

10. Internal audit report

The review report of the auditor shall explicitly be responsive to the overall principles applicable to the review engagement, as stated under 6 above.

11. Frequency

The frequency of internal audit shall be carried out on quarterly basis. The schedule of internal audit shall be agreed in consultation with JHCL. The internal audit is to be seen as an independent examination to review whether the internal control measures are compatible with JHCL's internal policy as well as with generally accepted accounting principles.

Financial Proposal- The financial proposal should mention:

- The quarterly lump sum remuneration payable by the company.
- Basis of reimbursement of actual expenses incurred by the auditors (IF Any)

Annex- II

Eligibility Criteria for Firm

All practicing Chartered Accountancy Firm meeting following additional criteria may submit its proposal till 2078/07/23 for audit for F/Y 2078/79:

- At least 5 years of experience in Auditing;
- Not less than 3 years exposure of auditing Hydropower Project Companies.
- Profile of the manpower currently working with the Firm.
- Not having any relatives working in JHCL.



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