

**RECENT AMMENDMENTS TO
THE COMPANIES
(AUDITOR'S REPORT)
ORDER
CARO 2020**

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CARO 2020

- Central Government Notification under Section 143(11) of Companies Act, 2013 dated 25th February, 2020
- Deferred – now applicable for F.Y. 2021-22
- Auditor to consider materiality while reporting
- Auditor needs to exercise judgment whether main report needs to be qualified. Give reasons for qualification in CARO

CARO 2020

- Indicate why unable to express opinion
- Indicate the information and explanation not available
- Management explanation to unfavorable comment need not be included unless warranted
- Use sample paragraphs drafted for CARO reporting in GN

Common Clauses in Schedule III and CARO 2020

- Benami Property Holding
- Wilful Defaulter
- Quarterly Returns and Statements to Banks to be in Agreement with the Books of Accounts
- Transactions not recorded in the books surrendered or disclosed as Income during the year in Tax Assessment

Auditing Standards, GNs and Technical Guides on Audit

- ❖ GN on Audit of Investments
- ❖ GN on Audit of Loans and Advances
- ❖ GN on Audit of Liabilities
- ❖ Technical Guide on Audit of NBFCs
- ❖ GN on Audit of Internal Financial Controls over Financial Reporting

INVENTORY

- ❖ Auditor to comment on discrepancy of 10% or more in the aggregate for each class of Inventory noticed on physical verification
- ❖ No separate materiality to be considered
- ❖ Apply 10% threshold on net basis after adjusting excesses and shortages within each class
- ❖ Auditor needs to exercise his professional judgment to determine the materiality and the relevance of discrepancy to the users

INVENTORY

- ❖ If not dealt with in the books of account, the extent of the discrepancies and its impact on the Financial Statements need to be reported
- ❖ Annual reconciliation of opening inventory, purchases and consumption as co-related to production is required if no inventory records maintained
- ❖ Sanctioned working capital limit in excess of Rs.5 Crores any time during the year only require comment on quarterly returns to Bank to be in Agreement with Books of Accounts

Loans, Investments, Guarantees and Securities

- ❖ Includes any advances in the nature of loans
- ❖ Secured or unsecured
- ❖ Granted to related parties and others
- ❖ State whether terms are prejudicial
- ❖ State whether schedule of repayment stipulated and observed
- ❖ State overdue more than 90 days and reasonable steps to recover the amounts

Loans, Investments, Guarantees and Securities

- ❖ Loans falling due renewed or extended or fresh loans granted to settle over dues of existing loan given to same parties need to be covered
- ❖ Aggregate amount and percentage to the total loans or advances in the nature of loans to be stated
- ❖ Granting of loan and advances in the nature of loan, either repayable on demand or without specifying terms or period of repayment along with percentage to total loans and percentage to related party to be stated
- ❖ Comment only on transaction during the year

Loans, Investments, Guarantees and Securities

- ❖ Controls and procedures including purpose, permissibility as per applicable law, terms, person authorised etc. to be seen
- ❖ Ensure compliance with Section 179, 180, 185, 186, 187 and of the Act and Rules there under
- ❖ Only Financial Guarantees to be considered for reporting
- ❖ Examine minutes books of Board and General Meeting, Schedule V to SEBI LODR Regulations

Loans, Investments, Guarantees and Securities

- ❖ Loans given and squared-up during the year also to be commented
- ❖ Consider rate of Interest, Security, Terms and period of repayment, ability to lend, borrower's Financial Standing, Credit Rating, etc
- ❖ Check prior approval of Financial Institutions, rate of interest of prevailing yield of Government securities closest to tenor of the loan
- ❖ Check Register as per Form MBP-2

Utilization of Funds

- ❖ Whether term loans are applied for purpose for which loans were obtained, if not, Amount and purpose for which used
- ❖ Funds raised on short term basis utilised for Long Term purposes
- ❖ Current maturities of Long Term loans included in current liabilities are to treated as Long Term Sources of Fund
- ❖ Repayment or redemption of long term loan/debt is application for long term
- ❖ Report only if significant differences exist

Borrowing of Funds

- ❖ Reporting required if funds borrowed from any person or entity to meet obligation of subsidiaries, associates and joint ventures
- ❖ Loans taken and squared-up during the year to be also reported
- ❖ Raising of loans during the year on pledge of securities held in the subsidiaries, joint ventures and associate companies to be reported alongwith defaults
- ❖ Creation of charge u/s 77 to be verified

Whistle-Blower Complaints

- ❖ Complaints during the year only to be considered
- ❖ See applicability of whistle-blower mechanism under Companies Act and SEBI Regulations
- ❖ Whether the companies has whistle-blower process with adequate procedure to handle complaints and to accept confidential submission of concerned about questionable accounting, internal control or auditing matters to be verified

Whistle-Blower Complaints

- ❖ Auditor may consider principles of materiality while reporting
- ❖ Action taken by management on complaints to be considered
- ❖ Auditor to modify nature, timing and extent of audit procedures based on complaints received and management action

Internal Audit

- ❖ To verify whether company has an Internal Audit system commensurate with the size and nature of its business
- ❖ Refer Section 138 of Companies Act, 2013 with Companies (Accounts) Rules, 2014 for applicability of clause
- ❖ Consider adequacy of scope, functioning, periodicity and methodology along with adequate staffing for conducting Internal Audit

Internal Audit

- ❖ For external agency as Internal Auditor – evaluate competency, objectivity and Independence along with qualifications, experience and professional standing
- ❖ For Listed companies, refer presentation to audit committee by Internal Auditor along with minutes of ACB and Board
- ❖ Review Independence and effectiveness of Internal Audit function
- ❖ See whether Technical assistance provided to Internal audit Department
- ❖ Refer follow-up systems on the deficiencies pointed out

Cash Losses

- ❖ Reporting of Cash losses in the financial year and immediately preceding Financial Year
- ❖ Cash loss = Net Profit/Loss after tax + Non Cash items such as – Depreciation, amortization, impairment provision, deferred tax income/expenses, Foreign Exchange Gain Tax, Fair Value changes
- ❖ Adjustment for effect of qualifications in the respective audit reports to the extent of their quantification to be considered
- ❖ Do not use cash flow statement to determine cash loss
- ❖ If cash losses only for one year, comment on two years separately

Resignation of Statutory Auditor

- ❖ In case of resignation of Statutory Auditor during the year, the new auditor needs to consider the issues, objections or concerns raised by outgoing auditor
- ❖ Ethical issues and compliances with company law provisions to be verified
- ❖ Section 140(2) , Rule 8 of the Companies (Audit and Auditors) Rules 2014 and Form ADT-3 need to be considered
- ❖ Reading of Minutes of the Board, communication to Audit Committee and enquiry with the Management required

Resignation of Statutory Auditor

- ❖ Consider “Implementation guide on resignation/withdrawal from an Engagement to Perform Audit of Financial Statements”
- ❖ Consider SEBI Circular CIR/CFD/CMD1/114/2019 dated October 18, 2019 on “Resignation of Statutory auditors from listed entities and their material subsidiaries”
- ❖ The reasons for resignation should be considered, such as non-availability of sufficient appropriate evidence, while issuing audit opinion on the financial statements of the current year
- ❖ Obtain Management Representation that there are no concerns of outgoing auditor beyond those stated in NOC and resignation letter

Material uncertainty in Meeting Liabilities

- ❖ Consider Financial Ratios, ageing and expected dates of realization of financial assets and payment of financial liabilities, other information, auditors knowledge for Management Plans to understand whether the company is capable of meeting its liabilities as and when they fall due within a period of one year from the Balance Sheet date
- ❖ SA-570 – Going Concern – Whether material uncertainty exists about the entity's ability to continue as a Going Concern
- ❖ SA-560 – Subsequent Events

Material uncertainty in Meeting Liabilities

- ❖ Consider recoverability of Financial Assets based on Agreements, Contracts, Historical Trends and Correspondence with debtors and borrowers
- ❖ In case of support letter from Holding Company, Auditor to evaluate whether holding company has ability to discharge such liabilities
- ❖ Ratios need to be calculated on the balance sheet date and also on the date nearer to audit report

Material uncertainty in Meeting Liabilities

- ❖ Consider MIS for subsequent months, cash flow projection for 12 months and commitment and guarantees on behalf of other entities
- ❖ Auditor to give negative assurance in his report stating that he neither gives any guarantee nor any assurance that all liabilities falling due within a period of one year from the balance sheet date will get discharged by the company as and when they fall due

CARO for CFS

- ❖ Qualifications and adverse remarks in CARO by subsidiary auditors need to be indicated by way of details of the companies and the paragraph numbers of the CARO report containing such qualification or remarks.
- ❖ Does not include qualification or adverse opinion given as per SA-705
- ❖ If subsidiaries audits are not finalized, state the fact
- ❖ Include qualification / adverse remark given in parent companies standalone CARO report also
- ❖ Text of subsidiaries CARO report is not required
- ❖ Do not evaluate materiality from consolidation perspectives

Thank you