

J B NAGAR CPE
STUDY CIRCLE
JOINTLY WITH
WICASA OF WIRC
OF
ICAI

IPCC – AUDIT
GROUP 2
PAPER 6

REFRESHER COURSE

21ST OCTOBER, 14

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Vouching and Verification

Q	Vouching	Verification
	i) It is examination of transactions	i) It is examination of balances
	ii) Checking of P/L items	ii) Checking of B/S items
	iii) It is conducted by checking documentary evidence	iii) Documental evidence + physical verification @ regular int.
	iv) Throughout the year	iv) End of the year
	v) Junior Staff	v) Senior staff or the auditor himself

Q. How to Vouch ?

1) V = Voucher

Auditor should check whether there are proper voucher (DE) in support of every transactions like Bill, Invoice, Agreement, Receipt, Contract, etc. Also check serial no, date, amt, signature, etc

2) O = Check whether the transaction has occurred over the current period of time

3) U = Check whether the transaction is made under proper competent authority

4) C = Check whether proper distinguish has been made between Capital and revenue expenditure / receipts

5) H = Check whether it has been recorded properly in BOA

6) Sec 227(1A) = Check whether the transaction is genuine and NOT Bogus

7) Sec 227(1A) = Check whether personal expenses are not charged to the Revenue P/L A/C

8) Sec 227(4A) CARO 2003 = Check whether there are any frauds, if yes qualify

9) Only for "INCOMES"

Check whether revenue is recognized as per requirements of AS -9 = "REVENUE RECOGNITION" on accrual basis unless there is any uncertainty.

10) If question is on Borrowing Cost/Interest, then additional point :

Check whether the treatment for Borrowing cost has been done as per the requirements of AS-16 = "BORROWING COST"

REFERENCE POINTS FOR VERIFICATION**1) AS -1 : “ Disclosure of accounting policies”**

- a) Consistency : Valuation policy is followed on a consistent basis
- b) Going concern : whether sale or destruction has affected the going concern

2) AS -2 (Revised) : “Inventories”

Check whether inventories are valued at cost or NRV, whichever is less

3) AS-3(Revised) : “Cash Flow Statement” → x**4) As-4 : “ Contingencies and Events occurring after Balance Sheet Date”**

→ Check whether



Amounts can be estimated

Cannot be estimated



Whether provisions has been made

whether disclosure is made by way of NOTE

5) AS-5 = x**6) AS-6 : “Depreciation”**

Check whether depreciation is provided as per the requirements of AS-6 “ Depreciation”

7) AS-7(Revised) : “ Construction Contract”

Check whether the construction contracts are valued as per %age completion method only

8) AS-10 : “Fixed Assets”

Check whether the fixed assets are valued as per the requirements of As-10

→ For Goodwill, check whether the decision for write – off is proper i.e. it is written off over 5 years or a longer period if justified

9) AS-11 : “Accounting for Fluctuation in Foreign Exchange

→ If any asset is purchased in foreign currency, check whether any fluctuations have been properly adjusted

10) AS-12 : “Government Grants”

If any govt grant is received for a depreciable asset; check whether the treatment, is done properly i.e. s per the requirements of AS – 12

11) AS-13 : “Investments”

Check whether long term investments are valued at cost

12) AS-14 : Accounting for “Amalgamation”

Check whether GOODWILL is shown in the BOA only if it is purchased

13) AS-16 : “Borrowing Costs”

If any asset is constructed, then check whether borrowing cost, if any have been capitalize as per the requirements of AS-16

*** REVISED SCHEDULE VI REQUIREMENTS :****1) SHARE CAPITAL**

- Any shares issued for consideration other than cash should be separately disclosed
- Any calls –In-arrears due from directors should be shown separately
- Forfeited shares amount originally paid up should be disclosed

2) RESERVES AND SURPLUS

→ Dr. Balance of P/L shall be shown as a -ve figure under the head ‘Surplus’. Similarly the ‘balance of ‘Reserves & Surplus’, after adjusting –ve balance of surplus, if any shall be shown under the head ‘R&S’

3) SHARE APPLICATION MONEY PENDING ALLOTMENT

→ It appears as a separate category after the heading ‘Shareholders Funds’

4) NON –CURRENT LIABILITIES

- Long term borrowings, long term provisions, deferred tax and other non-current liabilities come under this head
- Security provided for loans should be disclosed

5) **CURRENT LIABILITIES**

→ Short term borrowings, trade payable, short terms provisions and other current liabilities comes under this head

6) **FIXED ASSETS**

→ NON CURRENT ASSETS and Non Current Investments will be shown under fixed asset

→ Net Block and depreciation provided should be disclosed

7) **CURRENT ASSETS**

→ Investments according to revised schedule VI should come under this head. Market value should be disclosed.

→ Debtors : O/S for more than 6 months and others should be disclosed separately

→ Bank : Balance with Scheduled Bank and others should be disclosed separately

→ Other Loans & Advances will come under this head

8) **MISC EXPENDITURE**

Q : VERIFICATION OF ASSETS

How to verify tangible assets ?

V = Check whether the valuation is done as per the requirements of relevant accounting standards

Also check whether the depreciation is charged as per the requirements of AS-6

E = Check whether the asset is in existence by conducting physical verification towards and of the audit

R = Check whether the asset is a right of the company

- a) If asset is purchased → Check the invoice/agreement / contract
- b) If the asset is self constructed check costing records/certificates from technical persons
Also check whether borrowing cost if any incurred during construction period has been accounted as per the requirements of AS-16

I = Check whether there is any charge on the asset, if yes, check whether it is disclosed as per the requirement of revised Schedule VI

Also Check whether it is registered with the ROC

F = Check whether relevant revised Schedule VI requirements are followed

Y = Yo!

Q : VERIFICATION OF LIABILITIES

- 1) Check whether valuation is done as per AS-4 i.e. if the amt can be estimated check whether it has been provided & if it cannot be estimated, check whether it is disclosed
- 2) Check whether the liability is an actual obligation of the company i.e. obtain certificate from the management
- 3) Check whether the revised Schedule VI requirement is followed

Q : VERIFICATION OF GOODWILL

- 1) Valuation → As -10 AS -14
- 2) Right → Check whether it is the right of the company by checking the agreement purchased consideration
- 3) I → Charge → check whether charge ?
If ✓ → disclosed ? , ROC ?

Q : VERIFICATION OF ANY TANGIBLE FIXED ASSETS

- 1) Valuation → As -10 AS -6
- 2) Existence → Physical Verification
- 3) Right → purchased constructed + AS 16
- 4) Charge →
- 5) Check whether it is as Net Block
 $GB + P-S-D = \text{Net Block}$

Q : VERIFICATION OF LIVESTOCK

- 1) Valuation → NRV
- 2) Existence → Physical Verification
- 3) Right of the company
If purchased → check invoice
- 4) Charge
- 5) Any additions or deletions should be disclosed

Q : VERIFICATION OF INVESTMENTS

- 1) Valuation → AS -13
- 2) Existence
- 3) Right → purchased → invoice, share certificates, DEMAT statement, contracts receipts, investment register, etc

- 4) Charge
- 5) Schedule VI → Market value is disclosed

Q : VERIFICATION OF DEBTORS

- 1) Valuation
- 2) Obtain Schedules (list) from the mgmt. verify from BOA and also obtain independent confirmation
- 3) If a charge is created on the book debts
- 4) Schedule VI O/S 6 months or more
- 5) Check whether any B/R has issued or not

Q : VERIFICATION OF BANK BALANCES

- 1) Valuation → Obtain statement from clients verify from cash book & BRS and obtain independent confirmation in the form of Bank statements
- 2) Schedule VI requirements
- 3) Check costing, posting, etc

Q : VERIFICATION OF STOCK

- 1) Valuation → As per AS-2 (Revised)....
- 2) Existence
- 3) Right Purchased → invoices manufactured → costing records
If purchased → check invoice
- 4) Charge →
- 5) Schedule VI i.e ;stock of RM, WIP, FG should be shown separately

Q : VERIFICATION OF LOAN & ADVANCES

- 1) Valuation → Obtain schedule from the client, verify BOA, obtain independent confirmation in the form of Bank statements
- 2) Right → check the loan agreement
- 3) Check whether loans given are not shown as deposits → Sec 227(1A)
- 4) Sec 227(4A) → CARO'3 pays special attention to loans & advances given to the companies under the same management.

SPECIAL AUDIT

Q. Audit of government Co.

Ans : 1) Sec 619 Auditor of a government co. is appointed by C & AG

- 1) The CAG has the power to :
 - a) Gives instructions and directions to statutory auditor (SA) for carrying out the audit of Financial Statements of Govt. Co.
 - b) Conduct a supplementary audit or a test audit of FS of G CO either himself or by an authorized person , then it becomes the duty of management of company to provide information and explanation to such a person
- 2) The SA will submit his report to the CAG with the audit report as he likes

Q. Audit of Govt

Ans. : 1) Three components of Govt audit

- i) Audit of Receipts
 - ii) Audit of Expenditure
 - iii) Audit of Stores & Stocks
- 1) Govt audit is conducted by CAG

Q. Expenditure Audit

Ans.: 1) It is the most important component of Government audit

- 2) It is conducted by CAG
- 3) Components of expenditure audit

- i) Audit against Rules & Orders

The auditor needs to check whether every expenditure is according to the rules & regulations framed by constitution or any government authorities

- ii) Audit of sanctions

Auditor has to check whether every expenditure is booked by a general or special sanction by a competent authority

- iii) Audit of provision of funds

Auditor needs to check whether there is adequate provision for every expenditure and the fund is used only for the specific purpose

iv) Propriety Audit

Auditor needs to check whether the principles of prudence have been followed

- a) The govt. officials should use the government money as if it was their own money
- b) The govt officials should not abuse the authority
- c) The money should not be used on sections of the society

v) Performance Audit

The auditor should check whether the projects, schemes, and programmes are economical and yielding / producing the benefits. There should not be any wasteful expenditure

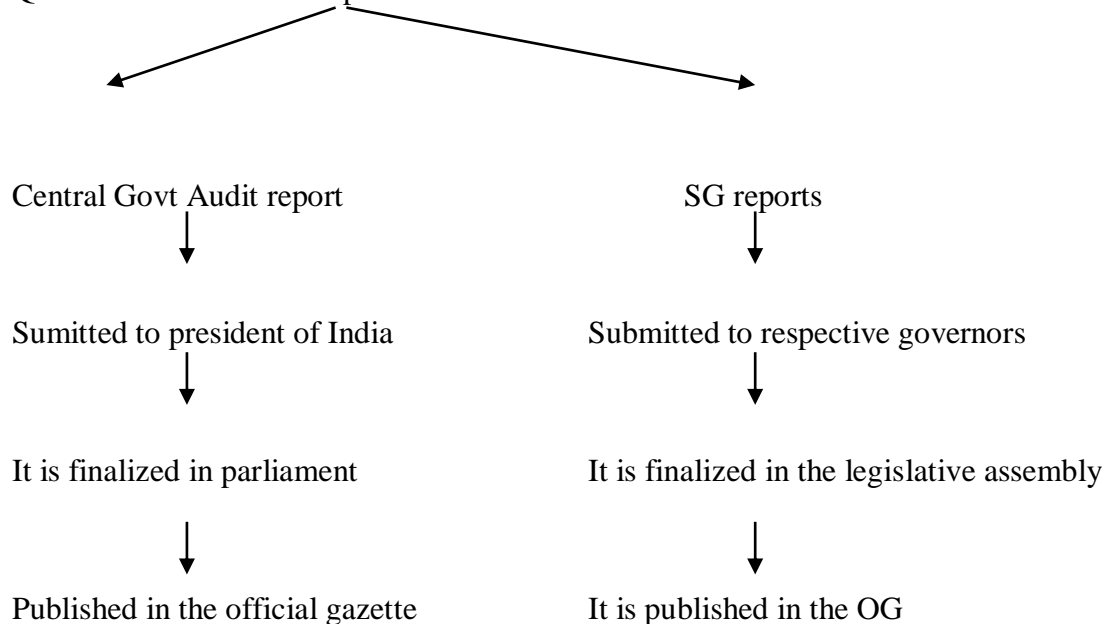
Q. Propriety Audit

Ans. : 1) Important component of expenditure audit

2) It is conducted by CAG

3) 3 principles of prudence....

Q. Government Audit Reports



Q. Audit of Government receipts

Ans. : 1) It is an important component of the govt audit

2) It is conducted by CAG

3) He checks whether the receipts are properly realized assessed and credited to consolidated fund of India

Q. Audit of Stocks & stores

Ans. : 1) It is an imp component

2)

3) The auditor checks whether :

i) Valuation is done properly and the write – offs, if any, are sanctioned by a competent authority

ii) The stocks are in existence by conducting physical verification

iii) whether the stocks are the right of the govt by verifying invoices, bills, agreements, etc

iv) If there is any change whether it is properly disclosed

Q. Duties of CAG

Ans. : 1) Compiled & submit accounts of CG (union) and SG (states)

2) Conduct audit of receipts

3) Conduct audit of expenditure (i.e. 5 components)

4) Conduct audit of stores of stock

5) Conduct audit of grants & loans

6) Audit of govt companies & corporations

Q. Special status of CAG

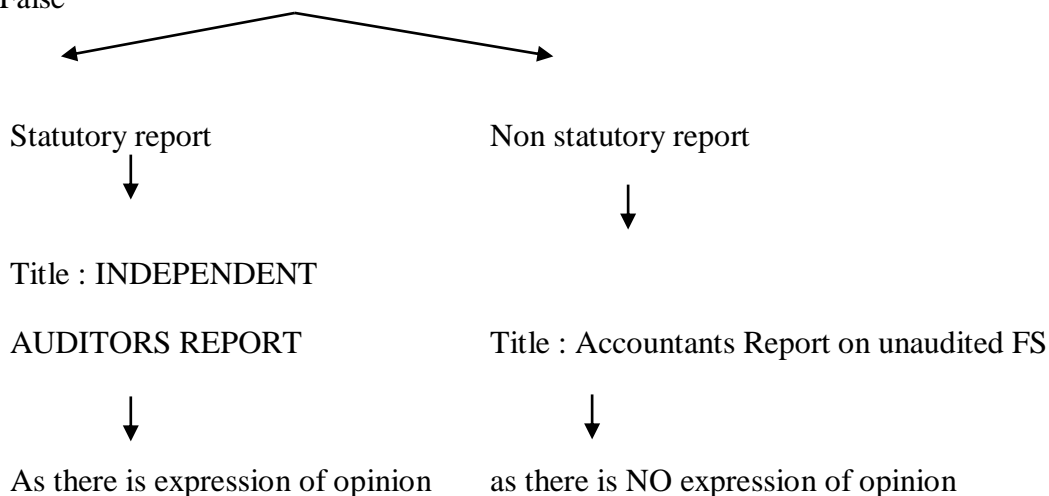
- Ans. : 1) He is appointed by president of India
- 2) His terms & conditions are fixed by POT
 - 3) He has a fixed term of service of 6 years of 65 years whichever is earlier.
 - 4) His salary is equivalent to the salary of judge of supreme court

Q. Audit of sole proprietor/firm

- Ans. : 1) Such Audit is not statutory
- 2) The scope of audit is decided mutually between the clients & the auditor in the letter of engagement
 - 2) The title of audit report is “ACCOUNTANTS REPORTS ON UNAUDITED FINANCIAL STATEMENTS”
 - 3) The auditor clearly mentions that they have confirmed that the P& L and B/S are in agreement with BOA. They have not audited the same & ∴ express No opinion

Q. The title of audit report is always Independent auditors report

Ans.: False



Q. Audit of incomplete records

Ans.: 1) Incomplete records may be there in the following circumstances :

- i) records are kept on single entry basis
 - ii) records are kept on double entry basis but some records are destroyed or seized by authorities
- 2) Role of statutory auditor

Situation (i) he should direct the management to convert BOA into double entry basis

Situation (ii) he will/should direct the management to complete or reconstruct the records

Q. Steps for audit of NPO's

Ans.: I) General Points :

- i) Check the constitution i.e set of rules & regulation & bye laws
- ii) Obtain certificates from the mgmt
- iii) Evaluate the ICS

II) Assets

- i) Check whether the valuation is done properly depreciation if any is reduced properly
- ii) Check whether the assets are in existence by conducting physical verification
- iii) Check whether the asset is the right of the organization by checking bills, invoices, agreements, controls, etc
- iv) Check whether there is any charge, if yes, Check whether it is properly disclosed
- v) Check whether investments are valued properly
- vi) Check whether stocks like are valued properly

III) Liabilities

- i) Check whether valuation is done properly
- ii) Check whether it is an actual obligation of the organization
- iii) Check whether the surplus has been added to the corpus fund and deficit has been reduced to corpus fund

IV) INCOMES & EXPENSES

5 points of VOUCH

V) Certain special points

- i) Check whether grants, donations, legacies, have been utilized for specific purpose only
- ii) Check whether there is corresponding car-marked investment for car marked funds
- iii) Check whether accounting is done properly for receipts & payments of special programmes & events

COMPANY AUDIT -1

What are the Qualifications of an auditor?	Sec. 226(1)
<ul style="list-style-type: none"> • Individual = Auditor = * CA + COP by ICAI • Firm = Auditor = <u>all</u> Partners = * • Appointment = firm name • Audit = any practicing partner • Firm → even if one partner * × Firm × 	

Disqualification of an auditor	
Sec. 226(3)(a) to (e)	Even if * <ul style="list-style-type: none"> (a) body corporate (b) officer / employee of body corporate (c) partner / employee of body corporate (d) debtor / guarantor > ` 1000 (e) person holding equity shares (security carrying voting rights) after 13.12.2001
Sec. 226(4)	If holding Co × Subsidiary Co × & vice – versa.
Sec. 226(5)	After appointment Sec. 226(3) & (4) is attracted then auditors is DEEMED TO HAVE VACATED HIS OFFICE.

Ceiling on No. of Co. Audits		Sec. 224(1B)
• Individual	10 Cos.+ <i>Max.</i> 10 Cos. = 20 public Cos. <small><i>PUSC<25L</i> <i>PUSC≥25L</i></small>	
• Firm	<ul style="list-style-type: none"> ▪ limit is applicable per partner ▪ except a partner who is in employment elsewhere. 	
<ul style="list-style-type: none"> • Limit is NA to Pvt. Cos, Branches, Foreign Cos, Tax audit, Audit of Co-Op Societ, trusts, corporations, Internal Audit, Guarantee Co without Share Capital • Joint Audit and Sec 25 Cos should be included • An auditor can accept maximum of 30 Cos <u>including</u> the audit of Private Cos (Notification issued by ICAI) • If Sec 224(1B) ×, then Auditor = Guilty of Professional Misconduct (GPM). 		

Appointment of first auditor	Sec. 224(5)
<ul style="list-style-type: none"> • FA = Appointment by BOD < 1 m from D. O. Inc. • If BOD × (after 1m) then SHS ✓ • Valid app: Mtg. (BOD/SHS) + Ordinary Resoln • Mere mention in AOA is not enough • Mtg + Resoln is required for valid apt. • FA app. By BOD = Removed by SHS • FA = auditor till 1st AGM <p><i>[However intimation should not be sent to ROC but however it is preferable in E-Form 23B.]</i></p> <ul style="list-style-type: none"> • Sec 224(7) → For removal of FA • Authority = SHS - Permission of CG is not required 	

Ref: **Que.:** Appt. of FA then **Ans.:** Sec. 224(5)

Que.: Removal of FA then **Ans.:** Sec. 224(5) & Sec 224(7)

Appointment of Subsequent Auditor	Sec. 224(1)
<ul style="list-style-type: none"> • Subs A = appointed by SHS @ AGM • valid app = Mtg (AGM) + Ordinary Resoln + Acceptance to ROC in E-FORM 23B within 30 days of receipt of notice • subs A = Auditor till next AGM • Sec 224(7) → For removal of subs A before expiry of his term • authority = SHS . Permission of CG is reqd, Spcl Notice = Not Reqd • For removal of subs A/ First Auditor @ AGM • authority = SHS . Permission of CG is not reqd, Spcl Notice = Reqd • If question is silent, CG × 	

Ref: **Que.:** Appointment of sub = A, then **Ans.:** Sec. 224(1)

Que.: Removal of sub = A, then **Ans.:** Sec 224(1) & Sec. 224 (7)

Reappointment of Retiring Auditor	Sec. 224(2)
<ul style="list-style-type: none"> • Re-app = AGM by SHS. ∴ VA = Mtg + Resoln + Accp. To ROC • Re-app × if : <ul style="list-style-type: none"> ▪ limit of Sec 224 (1B) ▪ auditor is disqualified ▪ auditor = written notice of unwillingness ▪ Resoln ✓ for his removal ▪ If the proposed auditor could not be app due to his death, disqualification, incapacity , the retiring auditor cannot be deemed to be reappointed. • If AGM is not held within time limit u/s 166, auditor shall continue in his office because auditor holds office from AGM to AGM 	

Appointment of an Auditor by CG**Sec. 224(3)**

- If the auditor is not appointed / re appointed / appointment is VOID then the CO = notice to CG within 7 days of conclusion of AGM
- On receipt of notice, CG = appoint auditor

Casual Vacancy**Sec. 224(6)**

- **Meaning:** Vacancy caused due to death, disqualifications, insanity, insolvency, resignation, dissolution of firm etc. It is caused after the auditor was validity app. & the app. was accepted.
- **Sec 224(6):** Filling up of CV
- It depends upon the reason — *Resignation* → SHS; *Others* → BOD
- Auditor will hold office till the concl. of next AGM.
- Refusal to accept app does not create a vacancy as there was no app. at all. In such a case, auditor would be app. only by CG.

Appointment of Auditor by SR**Sec. 224A**

- In certain cases, app/ re-app of auditor = SR only
- If **Sec 224A** is contravened, then **224(3)** → app = CG
- **Sec 224A × Sec 224 (3)** ✓
- Co. in which ≥ 25% of subscribed sh. cap is held singly/ jointly by



PFI
GCo.
CG
SG



Nationalized Bank
Insurance Co. doing
General Insurance



Co. in which ≥ 51% of SSC is held
by the SG

- should app / re-app the auditor only by a SR.
- Clarification by DOCA
The imp date is the date of AGM ie the date on which the Sp. Resolution is to be passed. If the share holding is < 25% on date of issuing notice but it is ≥ 25% on date of AGM then co= adjourn the mtg, issue fresh notice & pass the SR @ adjourned mtg.

CASE: X Ltd. has following SHS –

Particulars	%
ICICI	2
A Ltd in which 60% PUSC = GOI & GOMA	3
B Ltd which is subs of A Ltd	2
GOI	3
GOMA	2
SBI	3
P Ltd. Ins. Co. — Life Ins. Buss.	5
Q Ltd. In which 40% PUSC = GORA	10

Case	Ans.
Auditor should be app. by which Resoln?	Sec 224(A) ↑ effective sh = 15% ∴ OR
What if GORA held 60% of SSC in Q Ltd?	Then SH = 25% ∴ SR
On the date of sending notice ICICI = 24% of SSC in X Ltd on date of AGM → 25% Resoln?	Sec 224(A) ↑ Clarification by DOCA ∴ OR

Remuneration to Auditors	Sec. 224(8)
<ul style="list-style-type: none"> • If appointed by members → Members / Any other manner determined in GM • If appointed by BOD → BOD • If appointed by CG → CG • If appointed by CAG → Members / Any other manner determined in GM • In case of Re-app: If new Resoln x assumed to be the same as previous appt. • Exps paid to auditor = part of remuneration • Rem is generally fixed in the mtg. of appt. However, it could also be fixed in the next gm. • Extra fees for additional services like tax matters, consultancy is fixed by the BOD & is incl. in Rem. • Revised Schedule VI of Co's Act, 1956 requires disclosure of Auditors Rem. As fees, exp paid for 	

- services as:
- Auditor’s Remuneration:
 - (a) Audit Fees (b) Others

Procedure of Removal	Sec. 224(2) & (3)
<ul style="list-style-type: none"> • The Co = notice of removal = auditor • Rights of Auditor:- <ul style="list-style-type: none"> ▪ To be heard orally ▪ Make a representation ▪ To get his representation circulated amongst members • Duties of Company: <ul style="list-style-type: none"> ▪ Send a copy or representation to members ▪ State the fact of representation having been made in notice • If a copy is not sent by the Co, the auditor shall read out at the meeting • Intervention can be done by CLB on an application is made by CO or any aggrieved person if CLB is of the view that representation is needless publicity for defamatory matter. 	

Rights of an Auditor
<p>Rights of Auditor are given by Law to perform his duty and express opinion on FS.</p> <p>(1) Sec 227(1): Right of access to BOA & Vouchers (a) All BOA i.e. financial, costing, statutory, drafts (b) All places i.e. HO & Branches (c) All times i.e. usual business hrs Voucher = any documentary evidence in support of a transaction eg bills, invoices, receipts, agreements, contracts * If Sec 227(1) = denied = ROSA = AQAR</p> <p>(2) Sec 227(1): Right to obtain Information & Explanation from the officers/ employees / management related to audit *.....</p> <p>(3) Sec 228(2): Right to visit branch & check BOA of branch *</p> <p>(4) Sec 231: Right to receive notice + attend + be heard</p> <p>(5) Right of Lien can be exercised on the clients’ books & records provided it is exercised in a lawful manner.</p>

Duties of an Auditor	
Sec. 227(1A)	Auditor enquires into 6 areas but report only if he unsatisfied <div style="text-align: center;">↓</div> LT DIES

Sec. 227(4A)	CARO, 2003 — Auditor reports on all 21 points whether satisfied or not ↓ Audit report chapter
Sec. 227(3)	6 points of Opinion Para of the audit report ↓ Independent Auditors Rep.

Report on specified enquiries or Duty under Sec. 227(1A)	
<i>Auditor = duty = enquiry into all 6 areas. However, he shall report only if he is not satisfied. If he is not satisfied, he shall qualify his report. [Areas: LT DIES]</i>	
Loans	Security is proper? Terms & Conditions are proper? It should not be prejudicial to the interest of members (PTIM)
Transactions	Transactions: genuine / not bogus i.e. only book entries It should not be PTIM
Deposits	Loans & adv given by the co should not be shown as deposits. It should not be PTIM
Investments	Investments should be sold @ proper price i.e. market price
Expenses	Only those personal exps should be charged to the P/L which are as per the contractual obligations
Shares	Issued for Cash/COTC should be disclosed in the FS

Branch Auditor		Sec. 228
Qualification	BA = Statutory Auditor/ Any other person as per Sec 226 * = If Branch = foreign country, then he should be qualified as per the foreign law	
Rights of SA	Visit the branch & check BOA of the branch	
Appointment	SHS / SHs may authorize the BOD to app the BA in consultation with the SA	

Remuneration	SHS/ BOD
SA & BA	Same rights and duties

Exemption from Branch Audit based on Quantum	
The exemption is available only if <i>Step2 < Step 3</i>	
Step 1	Calculate Quantum of Activity: [Whichever is Higher] <ul style="list-style-type: none"> • Aggregate value of goods produced/manufactured/processed at branch • Aggregate value of goods sold and service rendered by branch office • Aggregate value of expenditure whether revenue or capital by the branch office
Step 2	Calculate Average Quantum of Activity: By taking average of 3 FY's immediately preceding the relevant FY
Step 3	Calculate Highest of the following: <ul style="list-style-type: none"> • ₹ 2 Lacs or • 2% of Avg. Turnover of the company including all its branch(3 years)

Exemption on other factors	
CG may exempt a Branch from audit requirements on following factors:	
<ul style="list-style-type: none"> ▪ Arrangements made by company itself; ▪ Availability/non availability of branch auditor at reasonable cost; ▪ Any other factor as per CG opinion 	

Special Audit (Re-audit)		Sec. 233A
Circumstances	It is directed by CG when — (a) Co: unsound busi. principle (b) Co: danger of insolvency	
Qualification	Sp. Auditor = company auditor / any other CA who may be not in practice	
Appointment	By CG	

Remuneration	By CG
Sp. Auditor	Same rights & duties as SA
Ep. Auditor	→ SAR → CG ∴ any action = CG

Cost Audit	Sec. 233B
Cost Audit	verification of costing records for Cos notified by CG
Sec. 209(1)(d)	Such cos → P2M2 production, processing, manufacturing, mining cos are required to maintain costing records if prescribed by CG such cost audit u/s 233B is in addition to the final audit.
Qualification	He should be a cost & works ACC
Appointment	BOD + approval of CG
Cost Auditor	same rights as SA
Cost Auditor	→ CAR → CG & @ same time he has to forward a copy to the co.

CARO REVISION – SHORT NOTES

Question 1

Non Applicability of Companies (Auditor's Report) order, 2003 (CARO, 2003)?

Ans

CARO'03 = NA to follⁿ Cos

B = Banking Co

I = Insurance Co

P = Private Co

S = Sec 25 Co (Charity Co)

C₁ = PUSC & Res ≤ 50 L

& C₂ = O/S loan ≤ 25 L

& C₃ = TO ≤ 5 CR

Ref. : Even if one C x

CARO = appl

21 points of CARO '03 (FIDA Tere DIL Says Saif ,Dumbo Abhishek Cute Rani Great Pair for Shaadi, Aish Salman Enemies Forever)

1) F = Fixed Assets

Auditor should check whether

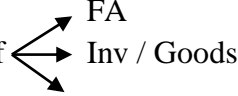
- Proper quantitative details are maintained?
- Proper physical verification is conducted by the management at regular intervals & any diff is adj properly in the BOA.?
- Whether going concern is affected by sale/disposal of asset?

2) I = Inventory

- ↑
- ↑
- Whether procedures are adequate?

3) D = Debts → 301

- Whether details of loans with Cos u/same management = properly recorded in the register reqd u/s 301
- Whether security and other terms & condition are not PTIM
- Whether repayment is regular
- If O/S amt > 1 L whether steps for recovery have been taken

- 4) **A = Adequate Internal Control**
 a) Whether adequate I.C.S exists for purchase & sale of 
- 5) **Tere = Transactions → S 301 (Pur/ sales)**
 a) Whether details of transactions with Cos u/same management = properly recorded in the register reqd u/s 301 provided the amount > 5 Lacs.
 b) Whether the transaction are made at proper price i.e. 'market price'
- 6) **D = Deposits**
 Whether the following are complied by the Co
 D = Directives iss by RBI
 P = provisions of the Co's Act
 O = Orders of the CLB (Co Law Board)
- 7) **I = Internal Audit**
 Whether Int. Audit is reqd if :
 a) PUSC + Res > 50 L OR b) Avg T/O of last 3 yrs > 5 CR
- 8) **L = Legal Provⁿ → S 209(1) (d) i.e for P² M² = Costing records are maintained if prescribed by CG**
- 9) **Says = Statutory Dues**
 a) Undisputed SD like PF, IEPF, I-Tax, S. Tax, Service Tax, Customs duty, Excise duty, ESI, any other case O/S for more than 6 ms should be reported
 b) Disputed amts = amts & the authority with which the case is filed should be reported
- 10) **Saif = Indicator of Sick Co**
 a) Co. regd in India min 5 yrs
 b) Accumulated losses \geq 50 % (Net Worth)
 c) Cash Losses → CY / PY
- 11) **Dumbo = Default in dues to Banks / FI/ Deb. Holders**
- 12) **Abhishek = Adequate records for pledge → maintained ?**
- 13) **Cute = Chit Fund Cos**
 a) Whether Company has complied with prudential norms
 b) Procedure for credit appraisal should be verified
 c) Repayment schedules should be as per the repayment capacity of the borrower.
- 14) **Rani → Whether all investments are regd. In the name of the Co.**
- 15) **Great → Guarantee**
 Guarantees given by the Co / PTIM

- 16) **Pairs** = Purpose
Check whether term loans are used for proper purpose
- 17) **Shaadi** = Short term / Long term
Check whether STL are not used for LT purpose & vice-versa
- 18) **Aish** = Preferential Allotment → S 301
- Whether details of preferential allotment with Cos u/same management = properly recorded in the register reqd u/s 301
 - Check whether the issue proper price = mkt price & not PTIM
- 19) **Salman** = Security
Check whether proper security is provided to Deb holders
- 20) **Enemies** = End use of Public Issue Money
- ↑ = reports to SEBI - Quarterly Statements
 - Details = Estimated / Actual Exp along with variance and reasons should be reported
 - ↑ may not be audited
 - ↑ submitted to SEBI till the Co. has accounted for end use of public issue money
- 21) **Forever** = Frauds
Nature & amount should be reported.

Revision of CARO

Not applicable to:- (i) Banking Company. (ii) Insurance Company (iii) Company U/s 25 (iv) Private Limited Company (at only point of time) whose

- Paid up Capital + Reserves \leq 50 lakh &
- Loan o/s $<$ 25 lakh &
- Turnover \leq 5 crore Rs.

Turnover

- Trade discount deducted
- Sales Tax / Excise duty deducted if credited separately to A/c
- Commission to IIIrd parties not deducted
- Sales returns deducted (even if of prior years).

Reserve

{(Capital Reserves + Revenue Reserves + Revaluation Reserves) – (Debit Balance of P/L Account + Misc. Expenses not w/o)}

Loans :- In aggregate from Banks or F.I. is to be taken.

BARE CARO!

- **Matters to be included in the auditor's report** - The auditor's report on the account of a company to which this Order applies shall include a statement on the following matters, namely–
- (i) Whether the company is maintaining proper records showing full particulars, including quantitative details and situation of fixed assets;
 - Whether these fixed assets have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account;
 - If a substantial part of fixed assets have been disposed off during the year; whether it has affected the going concern;
 - (ii) Whether physical verification of inventory has been conducted at reasonable intervals by the management;
 - Are the procedures of physical verification of inventory followed by the management reasonable and adequate in relation to the size of the company and the nature of its business. If not, the inadequacies in such procedures should be reported;
 - Whether the company is maintaining proper records of inventory and whether any material discrepancies were noticed on physical verification and if so, whether the same have been properly dealt with in the books of accounts;
 - (iii) has the company granted any loans, secured or unsecured to companies, firms or other parties covered in the register maintained under section 301 of the Act. If so, give the number of parties and amount involved in the transactions.
 - Whether the rate of interest and other terms and conditions of loans given by the company, secured or unsecured, are prima facie prejudicial to the interest of the company;
 - Whether receipt of the principal amount and interest are also regular
 - If overdue amount is more than one lakh, whether reasonable steps have been taken by the company for recovery of the principal and interest;
 - Has the company taken any loans, secured or unsecured from companies, firms or other parties covered in the register maintained u/s. 301 of the Act. If so, give the number of parties and the amount involved in the transactions.
 - Whether the rate of interest and other terms and conditions of loans taken by the company, secured or unsecured, are prima facie prejudicial to the interest of the company.
 - Whether payment of the principal amount and interest are also regular.
 - (iv) is there an adequate internal control system commensurate with the size of the company and the nature of its business, for the purchase of inventory and fixed assets and for the sale of goods and services. Whether there is a counting failure to correct major weaknesses in internal control system.
 - (v) Whether the particulars of contract or arrangements referred to in section 301 of the Act have been entered in the register required to be maintained under the section.
 - Whether the transactions made in pursuance of such contracts or arrangements have been made at prices which are reasonable having regard to the prevailing market prices at the relevant time; (This information is required only in case of transactions exceeding the value of five lakh rupees in respect of any party and in anyone financial year).
 - (vi) in case the company has accepted deposits from the public, whether the directives issued by the Reserve Bank of India and the provisions of sections 58 A and 58AA or any other relevant

provision of the Act and the rules framed there under, where applicable, have been complied with. If not, the nature of contraventions should be stated; If an order has been passed by Company Law Board or National Company Law Tribunal or RBI or any Court or any other Tribunal whether the same has been complied with or not?

- (vii) in the case of listed companies and / or other companies having a paid-up capital and reserves exceeding Rs.50 lakhs as at the commencement of the financial year concerned, or having an average annual turnover exceeding five crore rupees for a period of three consecutive financial years immediately preceding the financial year concerned, whether the company has an internal audit system commensurate with its size and nature of its business;
- (viii) where maintenance of cost records has been prescribed by the Central Government under clause (d) of sub-section (1) of section 209 of the Act, whether such accounts and records has been made and maintained;
- (ix) is the company regular in depositing undisputed statutory dues including Provident Fund, Investor Education and Protection Fund, Employees' State Insurance, Income-tax, Sales-tax, Wealth Tax, Service Tax, Custom Duty, Excise Duty, cess and any other statutory dues with the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated by the auditor.
 - In case dues of sales tax 1 income tax 1 custom tax 1 wealth tax 1 excise duty 1 cess have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending may please be mentioned.
(A mere representation to the Department shall not constitute the dispute).
- (ix) Whether in case of a company which has been registered for a period not less than five years, its accumulated losses at the end of the financial year are not less than fifty percent of its net worth and whether it has incurred cash losses in such financial year and in the immediately preceding financial year.
- (xi) Whether the company has defaulted in repayment of dues to a financial institution or bank or debenture holders? If yes, the period and amount of default to be reported;
- (xii) Whether adequate documents and records are maintained in cases where the company has granted loans and advances on the basis of security by way of pledge of shares, debentures and other securities; If not, the deficiencies to be pointed out.
- (xiii) Whether the provisions of any special statute applicable to chit fund have been duly complied with? In respect of nidhi/ mutual benefit fund / societies;
 - Whether the net-owned funds to deposit liability ratio is more than 1 : 20 as on the date of balance sheet;
 - Whether the company has complied with the prudential norms on income recognition and provisioning against substandard 1 doubtful / loss assets;
 - Whether the company has adequate procedures for appraisal of credit proposals 1 requests, assessment of credit needs and repayment capacity of the borrowers;
 - Whether the repayment schedule of various loans granted by the company is based on the repayment capacity of the borrower.
- (xiv) If the company is dealing or trading in shares, securities, debentures and other investments,

whether proper records have been maintained of the transactions and contracts and whether timely entries have been made therein; also whether the shares, securities, debentures and other securities have been held by the company, in its own name except to the extent of the exemption, if any, granted under section 49 of the Act;

- (xv) Whether the company' has given any guarantee for loans taken by others from bank or financial institutions; the terms and conditions whereof are prejudicial to the interest of the company;
- (xvi) Whether term loans were applied for the purpose for which the loans were obtained;
- (xvii) Whether the funds raised on short-term basis have been used for long term investment; if yes, the nature and amount is to be indicated;
- (xviii) Whether the company has made any preferential allotment of shares to parties and companies covered in the Register maintained under section 301 of the Act and if so whether the price at which shares have been issued is prejudicial to the interest of the company;
- (xix) Whether securities or charge have been created in respect of debentures Issued?
- (xx) Whether the management has disclosed on the end use of money raised by public issues and the same has been verified;
- (xxi) Whether any fraud on or by the company has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated.

COMPANY AUDIT – II**Q. FINAL DIVIDEND**

1) Proposed by BOD and declared by SHS at the AGM

2) Section 205 sources :-

- a) Free reserves i.e., reserves which are available for distribution of dividends.
- b) Current / previous or accumulated profits.
- (★) After providing depreciation
- (★) CG power = exempt
- c) Out of the moneys provided by the CG / SG if POD is guaranteed by government.

3) Compulsory transfer to reserve

- a) Before declaring dividend company should transfer certain % of current profits to a reserve.
- b) The % are minimum and therefore the company may voluntarily transfer more than minimum.
- c) The transfer depends upon the rate of dividend.

Rate of Dividend		% of Transfer
Upto 10%	→	NIL
10 to upto 12.5%	→	2.5%
12.5% upto 15%	→	5%
15% upto 20%	→	7.5%
More than 20%	→	10%

4) Time Limit → sec 205

Dividend is declared at the AGM . Any amount unclaimed after 30 days should be transferred to “ Unpaid Dividend A/c “ in a scheduled bank. Any amount o/s for over 7 years should be **transfer** to set up by the Cy o/s 205c.

Q. INTERIM DIVIDEND ?

1) It is proposed and declared by BOD.

2) sec 205 = Sources

Only out of current years profit after providing full years depreciation.

3) Compulsory Trf to reserves

----- Same as previous question.

4) Time Limit

----- Same as previous question.

Q. Balance in Security Premium A/c = **50** crs Only **5** crs is utilized for dividend.

Ans :- Acc to sec 78 , balance is Security premium can be utilized only for 5 purpose.

R 1) **Redemption** of Preference shares and debenturesP 2) Writing off **Preliminary** ExpensesIs 3) Writing off share and debenture **issue** expensesBindas 4) **Bonus** SharesBanda 5) **Buy Back** Shares.

Acc to sec 205 dividend can be declared and paid only out of divisible projects and Free reserves whether CY , LY , both or CG.

In the above case , it is contravention of sec 78 and sec 205 --- Qualify.

Q. POD out of CRR ?

Ans :- 1) sec 205 = Sources

2) sec 80 = Redemption of Preference shares →

Balance in CRR can be utilized only for issuing fully paid up bonus shares.

Therefore committed reserve.

In the above case , sec 205 X , sec 80 X.

∴ Auditor Qualify.

Q. POD out of DRR ?

Ans :- 1) sec 205 = Sources

2) sec 117 = Compulsory creation of DRR which can be utilized only for redemption of debentures.

∴ Committed reserve.

↑ ∴ sec 205X sec 117x.

∴ Auditor Qualify.

Q. POD out of Capital Reserve

Ans :- 1. sec 205 = Sources

2. only that port of capital reserve which is realized in cash can be utilized for POD i.e.,

Eg :- Profit on sale of fixed Asset ,

Profit on Re-issue of forfeited shares even if realized in cash can be utilized for payment of dividend.

↑ --- as the question is silent , CR is not realized in cash . It remains a committed reserve.

Sec 205X

∴ Auditor Qualify.

Ref :- Dividend Equalization Reserve = Free Reserve.

Q. POD out of investment Allowance reserve / Development Rebate Reserve.

Ans :- 1. Sec 205 = Sources

2. sec 205X Auditor qualify.

Q. POD out of balance in UNCLAIMED DIVIDEND A/C

Ans :- 1. Sec 205 = sources

2. 205 = Time Limit

205X

∴ Auditor Qualify.

Q. POD out of balance in UNCLAIMED DIVIDEND A/C where amount o/s is for 8 years

Ans :- 1. Sec 205 = sources

2. 205 = Time limit

Also requirements of CARO , 2004 , any statutory dues o/s for more than 6 months should be reported by the management to the shareholders.

↑ ---- 205X also duty under CARO, 2004 to qualify the report.

Q. INVESTOR'S EDUCATION & PROTECTION FUND (IEPF)?

Ans :- 1) IEPF is set up by CG o/s 205C

2) It is set up for the purpose of providing education and protection to investors.

3) 7 Sources

D - Unpaid dividends

A - o/s Application Money

D - Unpaid deposits

D - Unpaid debentures

I - Interest on Application Money , Unpaid deposits and

Debentures.

Is - Interest on Investment made out of IEPF.

Great - Grants and donations from CG / SG / Co's / Financial

Institutions.

4) Time Limit

5) Once the amount is transfer to IEPF , the liability recover anything from government.

Sec 208 :- Payment of interest on capital out of capital ?

CONDITIONS:-

P – Paid up Capital

L – Long Gestation Period

S – Special resolution by SHS

W – With sanction from CG .

A – Only if authorized be AOA

I – Interest rate → Max → 4%

T – Time limit max upto 6 months after construction is

Complete

_ - Financial Effect

Miscellaneous exp OR add to the cost of assets.

★ Payment of Interest will NOT be considered as a reduction in a capital.

Q. Maintenance of Books of ACCOUNTS & VOUCHERS = sec 209

Ans :- 209 (1) = BOA = Registered office , containing the details of :-

Clause (a) Income & Expenditure

(b) Purchase & sales

(c) Assets & Liabilities

(d) P^2M^2 Co = Costing records only if prescribed by CG.

★ BOA

- Any place
- BOD
- India
- ROC

209 (2) Proper BOA should be maintained even for Branch Office.

209 (3) 3 Conditions for BOA

(i) True & Fair View

&

(ii) Accrual Basis

&

(iii) Double entry System

209 (4A) :- 8 years

BOA + Vouchers to be maintained for last 8 years.

If any of the above section X , then qualify.

Q. Costing records are not provided to the auditor by the management / are not maintained.

Ans :- 1) sec 227 (1) Right to check BOA and vouchers at all times , place and types.

2) sec 209 (1) (d) -----

3) CARO , 2004 if 209 (1) (d) X

Auditor has to qualify the report.

4) If costing records are not provided the auditor would not be able to complete this duties properly

∴ It is a restriction on scope of audit

∴ Qualify the report.

Q. UNDERWRITER'S COMMISSION ?

CASE :- X Ltd → BOD decide to pay 5% of issue price of shares as underwriters commission. However , the AOA allow only 2% . Can the company pay UWC out of the share capital?

Ans :- sec 76 → MARKED

M → Meaning

Special contract between company and underwriters where underwriters agree to subscribe for the shares themselves or obtain subscribers. For underwriting they undertake a risk for which they charge under writers commission .

A → Payment of UWC should be authorized by AOA

R → 5% of issue price of shares of 2.5% of issue price of debentures or as provided in AOA whichever is less.

K→ Copy of underwriters contract alongwith prospectus should be **filed** with ROC

E →Eligibility

I) Underwriters are eligible for commission even if they don't subscribe even to a single share or debentures. The UWC can be paid out of profits as well as share capital.

D → Details of underwriters like Name , Address , Number of shares and debentures underwritten should be stated in prospectus.

---- UWC should be paid at 2% and decision to pay UWC out of share capital is valid.

Q. Buy back ? sec 77A

Ans :- Sources :- 1) Free Reserves

2) Security Premium

3) Proceeds of Fresh Issue

★ However proceeds of earlier issue cannot be utilized .

CONDITIONS :-

- 1) Authorized by AOA
- 2) Special resolutions by SHS
- 3) only fully paid up capital
- 4) Only Equity share capital
- 5) Max. 25% of total paid up capital
- 6) Debt. Equity 2:1
- 7) SEBI regulation completed within 12m from the date of passing the resolution.

Q. The Dr. balance of P/L A/c is adjusted Security Premium balance

Ans :- Sec 78----

Schedule VI requirement , the Dr. balance in P/L A/C can be adjusted only against Free Reserve means only those reserves which are available for the purpose of **dist**ribution of dividend.

Above case 78 X , sch VI X ∴ qualify.

Q. Discount ?

Ans :- Sec 79 contains the conditions

- 1) D – Shares could be issued at discount by following below conditions
- 2) I – Issue details should be mentioned in the prospectus
- 3) S – SHS → OR
- 4) C – Sanction from CG
- 5) O – Over 1 year from date of commencement of business should have passed.
- 6) U – Shares should be of same / uniform class already issued.
- 7) N - Rate should not exceed 10% / CG
- 8) T – Issue must be within two months from the sanction / extended ---- as provided by CG.

Q. Sweat Equity Shares?

Ans :- sec 79A → some companies issue sweat equity shares at a discount or for consideration other than cash to their employees or directors in return of know how , value addition , intellectual property.

In this way, the employees or directors participate in the growth of the company.

Conditions :-

S – shares should be of a same class already issued.

W – When ? 1 year of commencement of business

E – Employee and directors details like no. of shares, current market price , consideration if any and class should be disclosed in the resolution.

A – Authorized by special Resolution by SHS

T – Terms and Conditions

Listed Co – SEBI , not listed – CG

Q. Redemption of Preference. shares ?

Ans : Sec 80 : Conditions

1) Only fully paid up can be redeemed

2) AOA - ✓ , Resolution by SHS - ✓

3) Sources

i) Free Reserves i.e only those reserves which are available for distⁿ of dividend

ii) Security premium

iii) Proceeds of Fresh Issue

* Proceeds of earlier issue cannot be utilized

iv) CRR – only for fully paid up bonus shares

Q. Rights Issue ?

Ans. : Sec 81 : whenever a co. goes for further issue provided it is after 2 yrs from the formation of the co. or 1 yr of the first allotment whichever is earlier then it is duty bound to offer the share first to the existing equity SHS. Therefore existing eq. shs have a pre-emptire right to subscribe for the shares.

The shares can be offered directly to outsiders if

1) Special Resolution by SHS

2) OR by BOD + CG

- 3) BOD should exercise this right in good faith
- 4) If issue is made within 2 yrs of the formation of the co. or 1 year of the 1st allotment

Time Limit :

Co. should send the notice specifying the nos of shares offered & time limit of min 15 days to communicate the acceptance

* If there is no communication it is deemed to have been declined

Q. Reserve Capital ?

Ans. : Sec 99 : It is that part of capital which can be called up only in the event of and for the purposes of winding up or liquidation of the Co.

Q. DIMINUTION OF CAPITAL

Sec 94

- i) Cancellation of unsubscribed capital
- ii) AOA ✓ OR → SHS enough
- iii) Sanction from court not required
- iv) The words ‘and reduced’ need not
Be added to the name of the company

REDUCTION OF CAPITAL

Sec 100

- i) Reduction of subscribed capital
- ii) AOA ✓. SR – SHS is a must
- iii) Required
- iv) Words ‘ and reduced’ should be added
for a period mention in the court order

Q. Debentures ?

Ans. : 117(A) - Agreement between Co & deb holders which will be called Debentures Trust deed

117(B) – A Board of Debenture fund & investments made out of it

117(C) – Compulsory creation of DRR which can be utilize only for redemption of Debentures

Q. P Ltd has 5 Lacs cash at bank which is disclosed in the B/S Yet Quality?

Ans. : Part I of Schedule VI disclosure requirement of B/S cash at bank should be disclosed separately as a) Balance with Schedule Bank & b) Others

Q.	Provision	v/s	Reserve
Ans :	1) It is a charge on profit		1) It is an appropriation on profit
	2) It is to be made whether there is a profit or loss		2) Amt. is transferred to reserve only when there are profits
	3) PFO, PFI, Provision for doubtful debts		3) CRR, DRR

! EDUCRAFTING YOUR FUTURE!

SEE YOU AT *FINAL'S, B THERE!!!*