



# **Changes in Accounts & Audit Rules**

## **Companies Act, 2013**

CA Chintan Shah

# Introduction

- Background
- Companies (Accounts) Rules, 2014-Rule 3 and Proviso to Rule 3(1)
- Companies (Audit and Auditors) Rules, 2014-Rule 11(g)

# Background

- Section 128 of the Companies Act, 2013
- Section 2 (13) “books of account”
- Sec 143(3)- Audit report – comment on books of accounts
- Notification dated 5 August 2022 - Rule 3 of the Accounts Rules w.e.f 11<sup>th</sup> Aug, 2022
- Global scenario
- ICAI – Implementation Guide

# Amendments in Rule 3

**Availability of books of accounts:** Rule 3(1) of the Accounts Rules has been amended to provide that the books of account and other relevant books and papers maintained in an electronic mode should remain accessible in India, **at all times** so as to be usable for subsequent reference.

**Maintaining of backups:** Rule 3(5) of the Accounts Rules requires every company to maintain proper system for storage, retrieval, display or printout of the electronic records as the Audit Committee, if any, or the Board of Directors may deem appropriate and such records should not be disposed of or rendered unusable, unless permitted by law. Additionally, companies are required to maintain the back-up of the books of account and other relevant books and papers in an electronic mode on servers physically located ***in India on a daily basis (earlier periodic basis)*** even in cases where such books are maintained at a place outside India.

# Amendments in Rule 3

- **Service provider:** Rule 3(6) of the Accounts Rules requires disclosure by a company to the Registrar of Companies (ROC) in case a service provider has been used for maintenance of books of accounts in an electronic form. The amendments require an additional disclosure relating to the name and address of the person in control of the books of account and other books and papers in India, where the service provider is located outside India.

The revised requirements to be disclosed to the ROC on an annual basis at the time of filing of financial statement are:

- The name of the service provider
- The internet protocol address of service provider
- The location of the service provider (wherever applicable)
- Where the books of account and other **books and papers** are maintained on a cloud, such address as provided by the service provider
- **Details of where the service provider is located outside India, the name and address of the person in control of the books of account and other books and papers in India.**

# Audit Trail- Proviso to Rule 3(1)

## Management's Responsibility

Provided that for the financial year commencing on or after the 1st day of April 2023, every company which uses accounting software for maintaining its books of account, shall **use only such accounting** software which has a feature of **recording audit trail** of each and every transaction, **creating an edit log** of each change made in the **books of account** along with the date when such changes were made and ensuring that the audit trail **cannot be disabled**.

## Contd...

Implement Accounting software which has the following features:

- Records an audit trail of each and every transaction, creating an edit log of each change made in the books of account along with the date when such changes were made; and
- Ensuring that audit trail is not disabled.
- Accounting software may be hosted and maintained in India or outside India or may be on premise or on cloud or subscribed to as Software as a Service (SaaS) software. Further, a company may be using a software which is maintained at a service organization.

# Auditor's Responsibility

Amendments to Rule 11(g) of Companies (Audit and Auditors) Rules, 2014

Insertion of clause g

Rule 11(g): “Whether the company, in respect of financial years commencing on or after the **1st April, 2022**, has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated **throughout the year** for all transactions recorded in the software and the audit trail feature has **not been tampered** with and the **audit trail has been preserved** by the company as per the statutory requirements for **record retention.**”



## Contd...

Report on Other Legal and Regulatory Requirements'. Auditor is required to make specific assertion

The auditor is expected to verify the following aspects:

- • whether the audit trail feature is configurable (i.e., if it can be disabled or tampered with)?
- • whether the audit trail feature was enabled/operated throughout the year?
- • whether all ***transactions*** recorded in the software are covered in the audit trail feature?
- • whether the audit trail has been preserved as per statutory requirements for record retention?
- only in context of books of accounts

# Applicability

- Audit reporting will be triggered for financial years commencing on or after April 1, 2022, however, the applicability of the Account Rules will commence on or after April 1, 2023.
- Section 8 Companies
- Manual books
- Consolidated Financial Statements

Suggested reporting clause.

*Since the Proviso to rule 3 (1) of the Companies (Accounts) Rules, 2014 is applicable for the Company w.e.f April 1, 2023. Therefore, reporting under rule 11 (g) is not applicable for the financial year ending on 31<sup>st</sup> March 2023 in respect of use of accounting software for maintaining books of accounts with requisite audit trail facility.*

# Audit Approach

- Auditor may employ mix of procedures-e.g., checking management controls and direct checking.
- Correctly identify the records and transactions that constitute **books of account** under section 2(13) of the Act.
- Correctly identify the software and controls i.e., IT environment including applications, web-portals, databases, Interfaces, any other IT component used for creation and maintenance of books of accounts
- Ensured such software have the audit trail feature; auditor can check software set-up information, surprise checks, print-outs of audit trail
- Ensured that the audit trail captures changes to each and every transaction of books of account-When, who and what Data was changed

# Audit Approach

- Ensure that the audit trail is enabled at the database level (if applicable) for logging any direct data changes
- Ensure that the audit trail is retained as per statutory requirements for record retention-
- Ensure completeness and accuracy of audit trail (date, time, field changed, which user changed, what was changed, etc)
- Ensuring tampering of date and time feature not permitted by system
- Use Service of IT specialists

It is expected that management ensures that the administrative access to the audit trail is restricted to authorized representatives

# Audit Approach

## ➤ Interplay of Sec 143(3)(i) and Rule 11(g)

Section 143(3)(i) of the Act, where applicable under the provisions of the Act, requires the auditor to state in his audit report regarding the IFCoFR

Guidance note – para 52 reference to Audit trail

Detailed guidance is available in Implementation guide

Mere non-availability of audit trail does not necessarily imply failure or material weakness in the operating effectiveness of internal financial controls over financial reporting.

# Reporting

- In respect of audit trail, following are likely to be expected scenarios:
  - i. Management may maintain adequate audit trail as required by the Account Rules.
  - ii. Management may not have identified all records/transactions for which audit trail should be maintained.
  - iii. The accounting software does not have the feature to maintain audit trail, or it was not enabled throughout the audit period.
- Scenarios ii and iii mentioned above would result in a modified /adverse reporting against this clause

# Reporting

## ➤ Illustration of unmodified reporting -

Based on our examination which included test checks, the company has used an accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has operated throughout the year for all relevant transactions recorded in the software. Further, during the course of our audit we did not come across any instance of audit trail feature being tampered with. [Additionally, the audit trail has been preserved by the company as per the statutory requirements for record retention.

# Qualification / Modification

Some Instances:

- Books of accounts are not accessible in India or not always accessible in India
- Back-up of books available, but no back-ups of underlying invoices, vouchers
- Back-ups maintained physically but not on server
- Back-ups maintained electronically but not on server
- Back-up server is not physically located in India
- Back-ups done weekly, but not daily
- Back-up done daily, except a few days when server was down
- Back-up is being done daily, but that process was started only in March 2023, prior to back-ups was done monthly



# Qualification / Modification

Some Instances:

- Audit trail feature was disabled for one of the books of account/ records or for an accounting software - (e.g., fixed asset software did not have audit trail)
- Audit Trail feature is not operating effectively during the reporting period
- Accounting software is maintained by third party and auditor is unable to assess whether audit trail feature can be disabled during the reporting period
- Migration of software and thus not able to obtain evidence
- The audit trail has not been preserved by the company as per the statutory requirements for record retention.- Applicable from 2<sup>nd</sup> year of reporting

## Written Representations- SA 580

- Acknowledging management's responsibility for establishing and maintaining adequate controls for identifying, maintaining, controlling, and monitoring of audit trails
- Stating that management has performed an evaluation and assessed the adequacy and effectiveness of the company's procedures for complying to the requirements prescribed for audit trails.
- Stating management's conclusion, as set forth in its assessment, about the adequacy and effectiveness of the company's procedures in relation to audit trails.
- Stating that management has disclosed to the auditor all deficiencies in the design or operation of controls maintained for audit trails identified as part of management's evaluation
- Describing instances where identification of fraud- while reviewing and testing the samples related to the disablement of audit trail facility

# Audit Documentation- SA 230

- A sufficient and appropriate record of the basis for the auditor's reporting under Rule 11(g)
- Evidence that the audit was planned and performed in accordance with the Implementation Guide , Standards on Auditing issued by ICAI.
- Comply with the requirements of SA 230, "Audit Documentation"



**Thank you**

J B Nagar CPE Study Circle of WIRC of ICAI