



SUPPLEMENTARY FOR JUNE 2020 & DECEMBER 2020 EXAMINATION

PAPER - 12

SYLLABUS - 2016



Study Note - 7 (Revised)

PROVISION RELATING TO AUDIT UNDER COMPANIES ACT



This Study Note includes

- 7.1 Auditor's qualifications, disqualifications, appointment, remuneration, removal, powers and duties.**
- 7.2 Cost Audit, Secretarial Audit**
- 7.3 Reporting requirements under Companies Act, Report vs. Certificate, contents of the reports and qualifications in the report.**
- 7.4 Miscellaneous Audit**
 - (i) Branch Audit, Joint Audit**
 - (ii) Audit of Shares and debentures**
 - (iii) Audit of divisible Profits and dividends**
 - (iv) Statutory Auditors Vs. Internal Auditors**
 - (v) Auditing and Assurance Standards relating to Audit of Inventories and Audit of fixed assets.**
 - (vi) Auditing of different types of undertaking – Education, Hospitals, Co-operative Societies, Banks, Trusts, Municipalities, Panchayats.**

7.1 AUDITOR'S QUALIFICATIONS, DISQUALIFICATIONS, APPOINTMENT, REMUNERATION, REMOVAL, POWERS AND DUTIES.

Introduction

The Companies Act 2013 has made the audit of accounts of companies in India compulsory.

Section 139 to 148 provide for the qualifications, disqualifications, appointment, removal, rights, duties & liabilities of company auditors.

APPOINTMENT OF AUDITORS [SECTION 139]

- (1) Subject to the provisions of this Chapter, every company shall, at the first annual general meeting, appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting and the manner and procedure of selection of auditors by the members of the company at such meeting shall be such as prescribed in rule 3 of chapter X under the act.

Rule 3 : Manner and Procedure of Selection and Appointment of Auditors

(1) In case of a company that is required to constitute an Audit Committee under section 177, the committee, and, in cases where such a committee is not required to be constituted, the Board, shall take into consideration the qualifications and experience of the individual or the firm proposed to be considered for appointment as auditor and whether such qualifications and experience are commensurate with the size and requirements of the company;

Provided that while considering the appointment, the Audit Committee or the Board, as the case may be, shall have regard to any order or pending proceeding relating to professional matters of conduct against the proposed auditor before the Institute of Chartered Accountants of India or any competent authority or any Court.



- (2) The Audit Committee or the Board, as the case may be, may call for such other information from the proposed auditor as it may deem fit.
- (3) Subject to the provisions of sub-rule (1), where a company is required to constitute the Audit Committee, the committee shall recommend the name of an individual or a firm as auditor to the Board for consideration and in other cases, the Board shall consider and recommend an individual or a firm as auditor to the members in the annual general meeting for appointment.
- (4) If the Board agrees with the recommendation of the Audit Committee, it shall further recommend the appointment of an individual or a firm as auditor to the members in the annual general meeting.
- (5) If the Board disagrees with the recommendation of the Audit Committee, it shall refer back the recommendation to the committee for reconsideration citing reasons for such disagreement.
- (6) If the Audit Committee, after considering the reasons given by the Board, decides not to reconsider its original recommendation, the Board shall record reasons for its disagreement with the committee and send its own recommendation for consideration of the members in the annual general meeting; and if the Board agrees with the recommendations of the Audit Committee, it shall place the matter for consideration by members in the annual general meeting.
- (7) The auditor appointed in the annual general meeting shall hold office from the conclusion of that meeting till the conclusion of the sixth annual general meeting, with the meeting wherein such appointment has been made being counted as the first meeting:

Provided further that before such appointment is made, the written consent of the auditor to such appointment, and a certificate from him or it that the appointment, if made, shall be in accordance with the conditions as prescribed in rule 4 of chapter X under the Act, shall be obtained from the auditor.

Rule 4 : Conditions for Appointment and Notice to Registrar

- (1) The auditor appointed under rule 3 shall submit a certificate that -
- (a) the individual or the firm, as the case may be, is eligible for appointment and is not disqualified for appointment under the Act, the Chartered Accountants Act, 1949 and the rules or regulations made thereunder;
 - (b) the proposed appointment is as per the term provided under the Act;
 - (c) the proposed appointment is within the limits laid down by or under the authority of the Act;
 - (d) the list of proceedings against the auditor or audit firm or any partner of the audit firm pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.
- (2) The notice to Registrar about appointment of auditor under fourth proviso to sub-section (1) of section 139 shall be in Form **ADT-1**.

Provided also that the certificate shall also indicate whether the auditor satisfies the criteria provided in section 141.

Provided also that the company shall inform the auditor concerned of his or its appointment, and also file a notice of such appointment with the Registrar within fifteen days of the meeting in which the auditor is appointed. In case of unlisted public company licensed to operate by SEBI/ RBI/IRDA from International Financial Centre located in SEZ, "fifteen days shall be thirty days".

Explanation. — For the purposes of this Chapter, "appointment" includes re-appointment.



- (2) No listed company or a company belonging to such class or classes of companies as prescribed in rule 5 of chapter X under the act, shall appoint or re-appoint—
- (a) an individual as auditor for more than one term of five consecutive years; and
 - (b) an audit firm as auditor for more than two terms of five consecutive years:

Rule 5 : Class of Companies

For the purposes of sub-section (2) of section 139, the class of companies shall mean the following classes of companies excluding one person companies and small companies:-

- (a) all unlisted public companies having paid up share capital of rupees ten crore or more;
- (b) all private limited companies having paid up share capital of rupees 1 [fifty] crore or more;
- (c) all companies having paid up share capital of below threshold limit mentioned in (a) and (b) above, but having public borrowings from financial institutions, banks or public deposits of rupees fifty crores or more.

Provided that—

- (i) an individual auditor who has completed his term under clause (a) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of his term;
- (ii) an audit firm which has completed its term under clause (b), shall not be eligible for re-appointment as auditor in the same company for five years from the completion of such term.

Provided further that as on the date of appointment no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years.

Provided also that every company, existing on or before the commencement of this Act which is required to comply with provisions of this sub-section, shall comply with the requirements of this sub-section within three years from the date of commencement of this Act.

Provided also that, nothing contained in this sub-section shall prejudice the right of the company to remove an auditor or the right of the auditor to resign from such office of the company.

- (3) Subject to the provisions of this Act, members of a company may resolve to provide that—
- (a) in the audit firm appointed by it, the auditing partner and his team shall be rotated at such intervals as may be resolved by members; or
 - (b) the audit shall be conducted by more than one auditor.
- (4) The Central Government may, by rules 6 of chapter X, prescribe the manner in which the companies shall rotate their auditors in pursuance of sub-section (2).

Rule 6 : Manner of Rotation of Auditors by the Companies on Expiry of Their Term

- (1) The Audit Committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent.



(2) Where a company is required to constitute an Audit Committee, the Board shall consider the recommendation of such committee, and in other cases, the Board shall itself consider the matter of rotation of auditors and make its recommendation for appointment of the next auditor by the members in annual general meeting.

(3) For the purpose of the rotation of auditors-

(i) in case of an auditor (whether an individual or audit firm), the period for which the individual or the firm has held office as auditor prior to the commencement of the Act shall be taken into account for calculating the period of five consecutive years or ten consecutive years, as the case may be;

(ii) the incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms.

Explanation. I - For the purposes of these rules the term "same network" includes the firms operating or functioning, hitherto or in future, under the same brand name, trade name or common control.

Explanation. II - For the purpose of rotation of auditors,-

(a) a break in the term for a continuous period of five years shall be considered as fulfilling the requirement of rotation;

(b) if a partner, who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another firm of chartered accountants, such other firm shall also be ineligible to be appointed for a period of five years.

Explanation.—For the purposes of this Chapter, the word "firm" shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008.

(5) Notwithstanding anything contained in sub-section (1), in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, the Comptroller and Auditor-General of India shall, in respect of a financial year, appoint an auditor duly qualified to be appointed as an auditor of companies under this Act, within a period of one hundred eighty days from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.

(6) Notwithstanding anything contained in sub-section (1), the first auditor of a company, other than a Government company, shall be appointed by the Board of Directors within thirty days from the date of registration of the company and in the case of failure of the Board to appoint such auditor, it shall inform the members of the company, who shall within ninety days at an extraordinary general meeting appoint such auditor and such auditor shall hold office till the conclusion of the first annual general meeting.

(7) Notwithstanding anything contained in sub-section (1) or sub-section (5), in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government, or Governments, or partly by the Central Government and partly by one or more State Governments, the first auditor shall be appointed by the Comptroller and Auditor-General of India within sixty days from the date of registration of the company and in case the Comptroller and Auditor-General of India does not appoint such auditor within the said period, the Board of Directors

of the company shall appoint such auditor within the next thirty days; and in the case of failure of the Board to appoint such auditor within the next thirty days, it shall inform the members of the company who shall appoint such auditor within the sixty days at an extraordinary general meeting, who shall hold office till the conclusion of the first annual general meeting.

(8) Any casual vacancy in the office of an auditor shall—

(i) in the case of a company other than a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Board of Directors within thirty days, but if such casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting;

(ii) in the case of a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Comptroller and Auditor-General of India within thirty days.

Provided that in case the Comptroller and Auditor-General of India does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next thirty days.

(9) Subject to the provisions of sub-section (1) and the rules made thereunder, a retiring auditor may be re-appointed at an annual general meeting, if—

(a) he is not disqualified for re-appointment;

(b) he has not given the company a notice in writing of his unwillingness to be re-appointed; and

(c) a special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed.

(10) Where at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

(11) Where a company is required to constitute an Audit Committee under section 177, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee.

Summary at Glance

First Auditor

First auditor of the company, other than a Government company, shall be appointed by the BOD within 30 days from the date of registration of the company;

If BOD fails to appoint, by the member of the company within 90 days at an extraordinary general meeting appoint the first auditor;



In case of Government company, first auditor shall be appointed by CAG within 60 days from the date of registration;

If CAG fails to appoint, by the BOD of the company within next 30 days;

If again BOD fails to appoint the first auditor of the company, by the member of the company within 60 days at an extraordinary general meeting;

Tenure of the first auditor of the company in both the above cases shall be till the conclusion of the first annual general meeting;

Subsequent Auditor

At the first annual general meeting, appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting;

Before such appointment, the written consent of the auditor to such appointment and a certificate from him shall be in accordance with the condition as may be prescribed;

Within 15 days of the meeting the company shall file a notice of such appointment with the Registrar.

No listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint—

- (a) an individual as auditor for more than one term of five consecutive years; and
- (b) an audit firm as auditor for more than two terms of five consecutive years;

Cooling Period

an individual auditor who has completed his term under clause (a) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of his term;

an audit firm which has completed its term under clause (b), shall not be eligible for re-appointment as auditor in the same company for five years from the completion of such term.

At the time of rotation of auditors, incoming audit firms/ auditor having common partner/s with the erstwhile audit firm shall not be eligible for appointment;

Firm shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008;

In the case of Government company, CAG in respect of a financial year, appoint an auditor duly qualified to be appointed as an auditor of the company within a period of 180 days from the commencement of the financial year who shall hold the office till the conclusion of the AGM;



Re-appointment

A retiring auditor may be re-appointed at an annual general meeting, if—

he is not disqualified for re-appointment;

he has not given the company a notice in writing of his unwillingness to be re-appointed; and

a special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed;

Where at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company;

Where provision of section 177 is applicable i.e., constitution of Audit Committee, all appointments, including the filling of a casual vacancy of an auditor shall be made after taking into account the recommendations of such committee.

General Circular No. 33/2014

Clarification with Regard to Applicability of Provisions of Section 139(5) and 139(7) of the Companies Act, 2013

It is clarified that the new Act does not alter the position with regard to audit of such deemed Government companies through C&AG and thus such companies are covered under sub-section (5) and (7) of section 139 of the Companies Act, 2013.

MANNER OF ROTATION OF AUDITORS BY THE COMPANIES ON EXPIRY OF THEIR TERM

The Audit Committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent.

Where a company is required to constitute an Audit Committee, the Board shall consider the recommendation of such committee, and in other cases, the Board shall itself consider the matter of rotation of auditors and make its recommendation for appointment of the next auditor by the members in annual general meeting.

For the purpose of the rotation of auditors-

in case of an auditor (whether an individual or audit firm), the period for which the individual or the firm has held office as auditor prior to the commencement of the Act shall be taken into account for calculating the period of five consecutive years or ten consecutive years, as the case may be;



the incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms.

Explanation. I - For the purposes of these rules the term "same network" includes the firms operating or functioning, hitherto or in future, under the same brand name, trade name or common control.

Explanation. II - For the purpose of rotation of auditors,-

a break in the term for a continuous period of five years shall be considered as fulfilling the requirement of rotation;

if a partner, who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another firm of chartered accountants, such other firm shall also be ineligible to be appointed for a period of five years.

REMOVAL, RESIGNATION OF AUDITOR AND GIVING OF SPECIAL NOTICE [SECTION 140]

(1) The auditor appointed under section 139 may be removed from his office before the expiry of his term only by a special resolution of the company, after obtaining the previous approval of the Central Government in that behalf in the manner prescribed in rule 7 of chapter X under the act.

Rule 7 : Removal of the Auditor Before Expiry of his Term

(1) The application to the Central Government for removal of auditor shall be made in eForm ADT-2 and shall be accompanied with fees as provided for this purpose under the Companies (Registration Offices and Fees) Rules, 2014.

(2) The application shall be made to the Central Government within thirty days of the resolution passed by the Board.

(3) The company shall hold the general meeting within sixty days of receipt of approval of the Central Government for passing the special resolution.

Provided that before taking any action under this sub-section, the auditor concerned shall be given a reasonable opportunity of being heard.

(2) The auditor who has resigned from the company shall file within a period of thirty days from the date of resignation, a statement in the prescribed form (ADT - 3) with the company and the Registrar, and in case of companies referred to in sub-section (5) of section 139, Govt. companies and companies where CAG, appoints auditor, the auditor shall also file such statement with the Comptroller and Auditor-General of India, indicating the reasons and other facts as may be relevant with regard to his resignation.



(3) If the auditor does not comply with the provision of sub-section (2), he or it shall be liable to a penalty of fifty thousand rupees or an amount equal to the remuneration of the auditor, whichever is less, and in case of continuing failure, with further penalty of five hundred rupees for each day after the first during which such failure continues, subject to a maximum of five lakh rupees.

(4) (i) Special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor, or providing expressly that a retiring auditor shall not be re-appointed, except where the retiring auditor has completed a consecutive tenure of five years or, as the case may be, ten years, as provided under sub-section (2) of section 139.

(ii) On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor.

(iii) Where notice is given of such a resolution and the retiring auditor makes with respect thereto representation in writing to the company (not exceeding a reasonable length) and requests its notification to members of the company, the company shall, unless the representation is received by it too late for it to do so,—

(a) in any notice of the resolution given to members of the company, state the fact of the representation having been made; and

(b) send a copy of the representation to every member of the company to whom notice of the meeting is sent, whether before or after the receipt of the representation by the company, and if a copy of the representation is not sent as aforesaid because it was received too late or because of the company's default, the auditor may (without prejudice to his right to be heard orally) require that the representation shall be read out at the meeting.

Provided that if a copy of representation is not sent as aforesaid, a copy thereof shall be filed with the Registrar.

Provided further that if the Tribunal is satisfied on an application either of the company or of any other aggrieved person that the rights conferred by this sub-section are being abused by the auditor, then, the copy of the representation may not be sent and the representation need not be read out at the meeting.

(5) Without prejudice to any action under the provisions of this Act or any other law for the time being in force, the Tribunal either suo motu or on an application made to it by the Central Government or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors.

Provided that if the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall within fifteen days of receipt of such application, make an order that he shall not function as an auditor and the Central Government may appoint another auditor in his place.



Provided further that an auditor, whether individual or firm, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of any company for a period of five years from the date of passing of the order and the auditor shall also be liable for action under section 447.

Explanation I.— It is hereby clarified that the case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

Explanation II.— For the purposes of this Chapter the word “auditor” includes a firm of auditors.

Summary at Glance

Removal

By a special resolution of the company and after obtaining the previous approval of the central Government, the auditor appointed under section 139 may be remove from his office before the expiry of his term;

Resignation

The auditor shall file within 30 days from the date of resignation, a statement in prescribed form with the company and the registrar;

In case of Government company, the auditor shall send such statement with the CAG, indicating the reason and other facts with regards to his resignation;

If fails to comply with sub-section (2), punishable with fine not less than ₹ 50,000 but may extend to ₹5,00,000;

Special notice

Special notice for resolution at an annual general meeting for appointment of auditor other than a retiring auditor;

On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor;

Where notice is given of such a resolution and the retiring auditor makes with respect thereto representation in writing to the company and requests its notification to members of the company, the company shall, unless the representation is received by it too late for it to do so,—

in any notice of the resolution given to members of the company, state the fact of the representation having been made; and

send a copy of the representation to every member of the company to whom notice of the meeting is sent, whether before or after the receipt of the representation by the company,

If a copy of the representation is not sent as aforesaid because it was received too late or because of the company's default, the auditor may require that the representation shall be read out at the meeting.

ELIGIBILITY, QUALIFICATIONS AND DISQUALIFICATIONS OF AUDITORS [SECTION 141]

(1) A person shall be eligible for appointment as an auditor of a company only if he is a chartered accountant.



Provided that a firm whereof majority of partners practicing in India are qualified for appointment as aforesaid may be appointed by its firm name to be auditor of a company.

(2) Where a firm including a limited liability partnership is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm.

(3) The following persons shall not be eligible for appointment as an auditor of a company, namely:—

(a) a body corporate other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008;

(b) an officer or employee of the company;

(c) a person who is a partner, or who is in the employment, of an officer or employee of the company;

(d) a person who, or his relative or partner—

(i) is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company.

Provided that the relative may hold security or interest in the company of face value not exceeding one thousand rupees or such sum as prescribed in rule 10 of chapter X under the act;

Rule 10 : Disqualifications of Auditor

(1) For the purpose of proviso to sub-clause (i) of clause (d) of sub-section (3) of section 141, a relative of an auditor may hold securities in the company of face value not exceeding rupees one lakh:

Provided that the condition under this sub-rule shall, wherever relevant, be also applicable in the case of a company not having share capital or other securities:

Provided further that in the event of acquiring any security or interest by a relative, above the threshold prescribed, the corrective action to maintain the limits as specified above shall be taken by the auditor within sixty days of such acquisition or interest.

(2) For the purpose of sub-clause (ii) of clause (d) of sub-section (3) of section 141, a person who or whose relative or partner is indebted to the company or its subsidiary or its holding or associate company or a subsidiary of such holding company, in excess of rupees five lakh shall not be eligible for appointment.

(3) For the purpose of sub-clause (iii) of clause (d) of sub-section (3) of section 141, a person who or whose relative or partner has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of one lakh rupees shall not be eligible for appointment.

(4) For the purpose of clause (e) of sub-section (3) of section 141, the term "business relationship" shall be construed as any transaction entered into for a commercial purpose, except -

(i) commercial transactions which are in the nature of professional services permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;

(ii) commercial transactions which are in the ordinary course of business of the company at arm's length price - like sale of products or services to the auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.



- (ii) is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of such amount as prescribed in rule 10 of chapter X under the act; or
- (iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for such amount as prescribed in rule 10 of chapter X under the act;
- (e) a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as prescribed in rule 10 of chapter X under the act;
- (f) a person whose relative is a director or is in the employment of the company as a director or key managerial personnel;
- (g) a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;
- (h) a person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;
- (i) A person who, directly or indirectly, renders any service referred to in section 144 to the company or its holding company or its subsidiary company.

Explanation.— For the purposes of this clause, the term “directly or indirectly” shall have the meaning assigned to it in the Explanation to section 144.

Where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in sub-section (3) after his appointment, he shall vacate his office as such auditor and such vacation shall be deemed to be a casual vacancy in the office of the auditor.

REMUNERATION OF AUDITORS [SECTION 142]

- (1) The remuneration of the auditor of a company shall be fixed in its general meeting or in such manner as may be determined therein.

Provided that the Board may fix remuneration of the first auditor appointed by it.

- (2) The remuneration under sub-section (1) shall, in addition to the fee payable to an auditor, include the expenses, if any, incurred by the auditor in connection with the audit of the company and any facility extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company.

POWERS AND DUTIES OF AUDITORS [SECTION 143]

(1) Every auditor of a company shall have a right of access at all times to the books of account and vouchers of the company, whether kept at the registered office of the company or at any other place and shall be entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor and amongst other matters inquire into the following matters, namely:—

(a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;

(b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;

(c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company;

(d) whether loans and advances made by the company have been shown as deposits;

(e) whether personal expenses have been charged to revenue account;

(f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

Provided that the auditor of a company which is a holding company shall also have the right of access to the records of all its subsidiaries and associates companies in so far as it relates to the consolidation of its financial statements with that of its subsidiaries and associates companies.

(2) The auditor shall make a report to the members of the company on the accounts examined by him and on every financial statements which are required by or under this Act to be laid before the company in general meeting and the report shall after taking into account the provisions of this Act, the accounting and auditing standards and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under sub-section (11) and to the best of his information and knowledge, the said accounts, financial statements give a true and fair view of the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year and such other matters as prescribed in rule 11 of chapter X under Act.

Rule 11 : Other Matters to be Included in Auditors Report

The auditor's report shall also include their views and comments on the following matters, namely:-

(a) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

(b) whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;



(c) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

d) whether the company had provided requisite disclosures in its financial statements as to holdings as well as dealings in Specified Bank Notes during the period from 8th November, 2016 to 30th December, 2016 and if so, whether these are in accordance with the books of accounts maintained by the company.

(3) The auditor's report shall also state—

(a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;

(b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;

(c) whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

(d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;

(g) whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls;

(j) such other matters as may be prescribed.

(4) Where any of the matters required to be included in the audit report under this section is answered in the negative or with a qualification, the report shall state the reasons therefor.

(5) In the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Government, or partly by the Central Government and partly by one or more State Government, the Comptroller and Auditor-General of India shall appoint the auditor under sub-section (5) or sub-section (7) of section 139 and direct such auditor the manner in which the accounts of the company are required to be audited and thereupon the auditor so appointed shall submit a copy of the audit report to the Comptroller and Auditor-General of India which, among other things, include the directions, if any, issued by the Comptroller and Auditor-General of India, the action taken thereon and its impact on the accounts and financial statement of the company.

(6) The Comptroller and Auditor-General of India shall within sixty days from the date of receipt of the audit report under sub-section (5) have a right to,—

- (a) conduct a supplementary audit of the financial statement of the company by such person or persons as he may authorise in this behalf; and for the purposes of such audit, require information or additional information to be furnished to any person or persons, so authorised, on such matters, by such person or persons, and in such form, as the Comptroller and Auditor- General of India may direct; and
- (b) comment upon or supplement such audit report.

Provided that any comments given by the Comptroller and Auditor-General of India upon, or supplement to, the audit report shall be sent by the company to every person entitled to copies of audited financial statements under sub section (1) of section 136 and also be placed before the annual general meeting of the company at the same time and in the same manner as the audit report.

(7) Without prejudice to the provisions of this Chapter, the Comptroller and Auditor- General of India may, in case of any company covered under sub-section (5) or sub-section (7) of section 139 of Companies Act, 2013, if he considers necessary, by an order, cause test audit to be conducted of the accounts of such company and the provisions of section 19A of the Comptroller and Auditor- General's (Duties, Powers and Conditions of Service) Act, 1971, shall apply to the report of such test audit.

(8) Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company (herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section 139, or where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country and the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as prescribed in rule 12 of chapter X under the act.

Rule 12 : Duties and Powers of the Company's Auditor with Reference to the Audit of the Branch and the Branch Auditor

(1) For the purposes of sub-section (8) of section 143, the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in sub-sections (1) to (4) of section 143.

(2) The branch auditor shall submit his report to the company's auditor.

(3) The provisions of sub-section (12) of section 143 read with rule 12 hereunder regarding reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.

Provided that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

(9) Every auditor shall comply with the auditing standards.



(10) The Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949, in consultation with and after examination of the recommendations made by the National Financial Reporting Authority.

Provided that until any auditing standards are notified, any standard or standards of auditing specified by the Institute of Chartered Accountants of India shall be deemed to be the auditing standards.

(11) The Central Government may, in consultation with the National Financial Reporting Authority, by general or special order, direct, in respect of such class or description of companies, as may be specified in the order, that the auditor's report shall also include a statement on such matters as may be specified therein.

Provided that until the National Financial Reporting Authority is constituted under section 132, the Central Government may hold consultation required under this sub-section with the Committee chaired by an officer of the rank of Joint Secretary or equivalent in the Ministry of corporate Affairs and the committee shall have the representatives from the Institute of Chartered Accountants of India and Industry Chambers and also special invitees from the National Advisory Committee on Accounting Standards and the office of the Comptroller and Auditor-General.

(12) Notwithstanding anything contained in this section, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amounts as prescribed in rule 13 of chapter X under the act, is being or has been committed in the company by its officers or employees the auditor shall report the matter to the Central Government within such time and in such manner as prescribed in rule 13 of chapter X under the act:

Provided that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as prescribed in rule 13 of chapter X under the act:

Provided further that the companies, whose auditors have reported frauds under this sub-section to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as prescribed in rule 13 of chapter X under the act.

Rule 13 Reporting of Frauds by Auditor and Other Matters:

(1) If an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government.

(2) The auditor shall report the matter to the Central Government as under:-



(a) the auditor shall report the matter to the Board or the Audit Committee, as the case may be, immediately but not later than two days of his knowledge of the fraud, seeking their reply or observations within forty-five days;

(b) on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within fifteen days from the date of receipt of such reply or observations;

(c) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of forty-five days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;

(d) the report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same;

(e) the report shall be on the letter-head of the auditor containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number; and

(f) The report shall be in the form of a statement as specified in Form ADT-4.

(3) In case of a fraud involving lesser than the amount specified in sub-rule (1), the auditor shall report the matter to Audit Committee constituted under section 177 or to the Board immediately but not later than two days of his knowledge of the fraud and he shall report the matter specifying the following:-

(a) Nature of Fraud with description;

(b) Approximate amount involved; and

(c) Parties involved.

(4) The following details of each of the fraud reported to the Audit Committee or the Board under sub-rule (3) during the year shall be disclosed in the Board's Report:-

(a) Nature of Fraud with description;

(b) Approximate Amount involved;

(c) Parties involved, if remedial action not taken; and

(d) Remedial actions taken.

(5) The provision of this rule shall also apply, mutatis mutandis, to a Cost Auditor and a Secretarial Auditor during the performance of his duties under section 148 and section 204 respectively."]

(13) No duty to which an auditor of a company may be subject to shall be regarded as having been contravened by reason of his reporting the matter referred to in sub-section (12) if it is done in good faith.

(14) The provisions of this section shall mutatis mutandis apply to—

(a) the cost accountant in practice conducting cost audit under section 148; or

(b) the company secretary in practice conducting secretarial audit under section 204.



(15) If any auditor, cost accountant or company secretary in practice do not comply with the provisions of sub-section (12), he shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.

OTHER MATTERS TO BE INCLUDED IN AUDITOR'S REPORT

The auditor's report shall also include their views and comments on the following matters, namely:-

whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;

whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

Report of the Auditor shall state about existence of adequate internal financial control systems and operating effectiveness.

DUTIES AND POWERS OF THE COMPANY'S AUDITOR WITH REFERENCE TO THE AUDIT OF THE BRANCH AND THE BRANCH AUDITOR

For the purposes of sub-section (8) of section 143, the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in sub-sections (1) to (4) of section 143.

The branch auditor shall submit his report to the company's auditor.

The provisions of sub-section (12) of section 143 read with rule 12 hereunder regarding reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.

REPORTING OF FRAUDS BY AUDITOR

(1) For the purpose of sub-section (12) of section 143, in case the auditor has sufficient reason to believe that an offence involving fraud, is being or has been committed against the company by officers or employees of the company, he shall report the matter to the Central Government immediately but not later than sixty days of his knowledge and after following the procedure indicated herein below.

auditor shall forward his report to the Board or the Audit Committee, as the case may be, immediately after he comes to knowledge of the fraud, seeking their reply or observations within forty-five days;

on receipt of such reply or observations the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government within fifteen days of receipt of such reply or observations;



in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of forty-five days, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he failed to receive any reply or observations within the stipulated time.

The report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed post followed by an e-mail in confirmation of the same.

The report shall be on the letter-head of the auditor containing postal address, e-mail address and contact number and be signed by the auditor with his seal and shall indicate his Membership Number.

The report shall be in the form of a statement as specified in Form ADT-4.

The provision of this rule shall also, mutatis mutandis, to a cost auditor and a secretarial auditor during the performance of his duties under section 148 and section 204 respectively.

AUDITOR NOT TO RENDER CERTAIN SERVICES [SECTION 144]

An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case maybe, but which shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely:—

- (a) accounting and book keeping services;
- (b) internal audit;
- (c) design and implementation of any financial information system;
- (d) actuarial services;
- (e) investment advisory services;
- (f) investment banking services;
- (g) rendering of outsourced financial services;
- (h) management services; and
- (i) any other kind of services as may be prescribed.

Provided that an auditor or audit firm who or which has been performing any non-audit services on or before the commencement of this Act shall comply with the provisions of this section before the closure of the first financial year after the date of such commencement.

Explanation.—For the purposes of this sub-section, the term “directly or indirectly” shall include rendering of services by the auditor,—



- (i) In case of auditor being an individual, either himself or through his relative or any other person connected or associated with such individual or through any other entity, whatsoever, in which such individual has significant influence or control, or whose name or trade mark or brand is used by such individual;
- (ii) In case of auditor being a firm, either itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trade mark or brand is used by the firm or any of its partners.

AUDITOR TO SIGN AUDIT REPORTS, ETC. [SECTION 145]

The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of sub-section (2) of section 141, and the qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

AUDITORS TO ATTEND GENERAL MEETING [SECTION 146]

All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company, and the auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorised representative, who shall also be qualified to be an auditor, any general meeting and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.

PUNISHMENT FOR CONTRAVENTION [SECTION 147]

(1) If any of the provisions of sections 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees, or with both.

(2) If an auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees or four times the remuneration of the auditor, whichever is less.

Provided that if an auditor has contravened such provisions knowingly or wilfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less.



(3) Where an auditor has been convicted under sub-section (2), he shall be liable to—

- (i) refund the remuneration received by him to the company; and
- (ii) pay for damages to the company, statutory bodies or authorities or to members and creditors of the company for loss arising out of incorrect or misleading statements of particulars made in his audit report.

(4) The Central Government shall, by notification, specify any statutory body or authority or an officer for ensuring prompt payment of damages to the company or the persons under clause (ii) of sub-section (3) and such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.

(5) Where, in case of audit of a company being conducted by an audit firm, it is proved that the partner or partners of the audit firm has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability, whether civil or criminal as provided in this Act or in any other law for the time being in force, for such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally.

Provided that in case of criminal liability of an audit firm, in respect of liability other than fine, the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud shall only be liable.

Audit Committee- Section 177

Constitution of an Audit committee is mandatory for the;

- Every listed Company; and
- Such directors or classes of the companies, as may be prescribed.

As per the Rule 6 of the Companies (Meetings of the Board and its Power) Rules, 2014 following class of the companies have been prescribed for this purpose;

- All public companies with a paid up share capital ₹ 10 Crore or more;
- All Public Companies having turnover of ₹ 100 Crore or more;
- All Public Companies having in aggregate, outstanding Loans, or borrowings and debentures or deposits exceeding ₹ 50 Crore or more.

An Audit committee shall have minimum 3 Directors majority of them should be Independent Directors. Majority of the member of the Audit Committee should be able to read & understand the financial statement.

Function of Audit Committee: The various Functions of the Audit Committee is enumerated below;

- Recommend the appointment and fixation of the remuneration of Auditor.



- Review and monitor the Auditors independence and performance and effectiveness of audit process.
- Examination of the Financial Statement and Auditor's report thereon.
- Scrutiny of Inter Corporate Loans and Investment,
- Valuation of the Assets of the Company,
- Evaluation of the internal financial control and risk management system of the entity.
- Evaluation of the use of the funds rose through public offers.
- Evaluation of any related party transaction.

Powers of the Audit Committee: The powers of the Audit Committee are enumerated below;

- Audit Committee has the power to call for comments of the Auditor about Internal Control Systems and the scope of the Audit including its observation.
- Before submission of the report to the Board the Audit Committee have the power to review the Financial Statement.
- Power to discuss any issues with the Statutory & Internal Auditor and the Management of the Company in relation to matter contained in the Financial Statement.
- Power to investigate into any matter under the perview of Audit Committee.
- Auditors of the company and key managerial personnel shall have a right to be heard into the meeting.
- Composition of Audit Committee is to be disclosed in Board's Report.
- In case recommendation of the Audit Committee is not accepted by the Board, the Board shall disclose in Board's report along with reasons.

Self Examination Questions

1. Is an auditor entitled to attend the general meetings? Discuss the rights of an auditor while he is present in general meeting?
2. Discuss the procedure of appointment of the first auditor of a company.
3. State the procedure of for removal of statutory auditor before the expiry of his term.
4. Discuss the provision of section 140 of the companies Act 2013.
5. Who are qualified to act as auditor of the company? Discuss the person who is disqualified to become as an auditor of a company.
6. State the provision relating to audit of branch office of a company in India and Abroad.
7. Discuss the reporting requirement of Frauds by Auditor.
8. List down the certain services which are not to be rendered by the Auditor of the Company.
9. Write short notes on Audit Committee.
10. Why Central Government permission is required, when the auditor is to be removed before the expiry of their term?

State whether the following statements are true or false.

1. In case of Government Company auditor is appointed by the CAG within 182 Days from the commencement of Financial Year.
2. Cooling period of Individual Auditor is 2 consecutive terms of 5 years.
3. The first auditor appointed shall hold office till the conclusion of first AGM.
4. Government Company means a company where 21% of shares are hold by the Central government or State Government or partly by Central Government or State Government.
5. A Body Corporate can become Auditor of the company.
6. The auditor shall have access at all times to the books of account and voucher of the company.
7. An auditor of a company can render Investment Banking Service.
8. The auditor report shall be signed only by the person appointed as an auditor of the company.
9. All notices of the general meeting shall be forwarded to the auditor of the company.
10. An audit committee shall have minimum 5 directors.

[Answer: False, False, True, False, False, True, False, True, True, False]

Fill in the blanks:

1. An Audit committee shall have _____ directors.
2. Audit committee formation is mandatory for a public company having _____ paid up share capital.
3. Cost Audit is mandatory only when specific order is issued by the _____.
4. Cost Audit report is submitted to the Central Government within _____ days.
5. First auditor is appointed by the BOD of the company within ____ days.
6. Cost Audit is conducted by the _____ in practice.
7. Any fraud to involve an amount of _____ is to be reported to the Central Government.
8. The auditor shall have a right to be _____ at Annual General Meetings.
9. Punishment for contravention of section 139 is _____.
10. Auditor of Government Company is appointed by _____.

[Answer: 3, 10 Crore or more, Central Government, 30 days, 30 days, Cost Accountants, 1 crore, Heard, 25000, Comptroller and Auditor General of India.]

**Match the following**

	Column A		Column B
1	Maximum term of Firm as Auditor	A	2 Consecutive terms of 5 years
2	Minimum fees for contravention of section 139	B	BOD
3	Maximum fees for contravention of section 139	C	A company which is a subsidiary of Government Company.
4	Independent Directors	D	Section 145 of the Companies Act 2013
5	First auditor appointment is done by	E	1 term of 5 years
6	Auditor Remuneration is to be fixed at	F	Special Resolution
7	Government Company	G	₹ 25,000
8	Maximum term of Individual Auditor	H	₹ 5,00,000
9	Resolution for removal of auditor before expiry of term	I	General Meeting
10	Signing of audit report	J	Audit Committee

[Answer: E, G, H, J, B, I, C, A, F, D]

Multiple choice questions

- First auditor of the company is appointed by the BOD within
 - 15 days
 - 30 days
 - 45 days
 - 60 days
- Cost Audit is covered under
 - Section 204
 - Section 148
 - Section 139
 - None of the above
- Secretarial Audit is covered under section
 - Section 204
 - Section 148
 - Section 139
 - None of the above



4. Appointment of auditor for government company is done by
 - (a) BOD
 - (b) Audit committee
 - (c) Managing Director
 - (d) CAG

5. While conducting audit of financial statement auditor need to comply with
 - (a) Cost Audit Standards
 - (b) Secretarial standards
 - (c) Auditing Standards
 - (d) None of the above

[Answer: B, B, A, D, C]

7.2 COST AUDIT, SECRETARIAL AUDIT

Cost Audit Provision of Section 148 of the Companies Act.

148. (1) Notwithstanding anything contained in this Chapter, the Central Government may, by order, in respect of such class of companies engaged in the production of such goods or providing such services as may be prescribed, direct that particulars relating to the utilisation of material or labour or to other items of cost as may be prescribed shall also be included in the books of account kept by that class of companies:

Provided that the Central Government shall, before issuing such order in respect of any class of companies regulated under a special Act, consult the regulatory body constituted or established under such special Act.

- (2) If the Central Government is of the opinion, that it is necessary to do so, it may, by order, direct that the audit of cost records of class of companies, which are covered under subsection (1) and which have a net worth of such amount as may be prescribed or a turnover of such amount as may be prescribed, shall be conducted in the manner specified in the order.
- (3) The audit under sub-section (2) shall be conducted by a Cost Accountant who shall be appointed by the Board on such remuneration as may be determined by the members in such manner as may be prescribed:

Provided that no person appointed under section 139 as an auditor of the company shall be appointed for conducting the audit of cost records:



Provided further that the auditor conducting the cost audit shall comply with the cost auditing standards.

Explanation.—For the purposes of this sub-section, the expression “cost auditing standards” mean such standards as are issued by the Institute of Cost Accountants of India, with the approval of the Central Government.

(4) An audit conducted under this section shall be in addition to the audit conducted under section 143.

(5) The qualifications, disqualifications, rights, duties and obligations applicable to auditors under this Chapter shall, so far as may be applicable, apply to a cost auditor appointed under this section and it shall be the duty of the company to give all assistance and facilities to the cost auditor appointed under this section for auditing the cost records of the company:

Provided that the report on the audit of cost records shall be submitted by the cost accountant to the Board of Directors of the company.

(6) A company shall within thirty days from the date of receipt of a copy of the cost audit report prepared in pursuance of a direction under sub-section (2) furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein.

(7) If, after considering the cost audit report referred to under this section and the information and explanation furnished by the company under sub-section (6), the Central Government is of the opinion that any further information or explanation is necessary, it may call for such further information and explanation and the company shall furnish the same within such time as may be specified by that Government.

8) If any default is made in complying with the provisions of this section,—

(a) The company and every officer of the company who is in default shall be punishable in the manner as provided in sub-section (1) of section 147;

(b) The cost auditor of the company who is in default shall be punishable in the manner as provided in sub-sections (2) to (4) of section 147.

PROCEDURE FOR COST AUDIT AND APPOINTMENT OF COST AUDITOR (FOR FINANCIAL YEAR COMMENCING ON OR AFTER 1st APRIL, 2014 ONWARDS)

Pursuant to Companies Act 2013 and in supersession of Cost Accounting Records Rules 2011 and Companies (Cost Audit Report) Rules 2011, the Ministry of Corporate Affairs notified Companies (Cost Records and Audit) Rules 2014 on 30th June 2014 which were amended vide Companies (Cost Records and Audit) Amendment Rules 2014 on 31st December 2014. The mechanism with respect to maintenance of cost records, cost audit and appointment of cost auditors has been changed and shall be in accordance with Companies (Cost Records and Audit) Rules 2014 as amended.

The applicability of maintenance of Cost Records and Cost Audit shall be for those sectors which are mentioned in the Tables 'A' and 'B' to the Companies (Cost Records and Audit) Amendment Rules 2014 dated 31st December 2014 notified by the Government vide GSR 1/2015(E) dated 1st January 2015.

Maintenance of Cost Accounting Records and Cost Audit

The Rules state that cost records are to be maintained in Form CRA-1, which provides principles to be followed for different cost elements. The principles are in sync with the cost accounting standards issued by the Institute of Cost Accountants of India. Since the Rules are principle based, no format has been prescribed for maintenance of cost accounting records like pre-2011 industry specific rules. It is opened for industry to maintain cost accounting records according to its size and nature of business so long as it determines a true and fair view of the cost of production, cost of sales and margin of the products/services.

The cost audit report is required to be in conformity with the "cost auditing standards" as referred to in Section 148 of the Companies Act, 2013.

It may be noted that the Council of the Institute of Cost Accountants of India has made it mandatory for cost accountants in practice to follow and conform to the Cost Accounting Standards issued by it and it is incumbent on the cost auditors to report any deviations from cost accounting standards.

Applicability of Cost Audit

The Rules have classified sectors/industries under Regulated and Non-Regulated sectors. The sectors/industries covered under Table A of the Rules are under the Regulated Sector and sectors/industries covered under Table B are under the Non-Regulated Sector.

Every company, under regulated category (table A) shall get cost records audited if the turnover from all its products or services is ₹ 50 crores or more and the aggregate turnover from individual product or services is ₹ 25 cores or more.

In case of non regulated category (table B) the threshold is 150 crores or more and 35 crores or more.

The rule shall not apply if revenue from exports exceeds 75% of total revenue or which is operating from SEZ turnover from all its products and services of fifty crore or more during the immediately preceding financial year, shall be required to maintain cost accounting records.

However, foreign companies having only liaison office in India and engaged in production, import and supply or trading of medical devices listed in Sl. 33 of Table B are exempted. Further, companies which are classified as a micro enterprise or a small enterprise including as per the turnover criteria under sub-section (9) of section 7 of the Micro, Small and Medium Enterprises Development Act, 2006 (27 of 2006) are also excluded from the purview of the Rules.

The Rules are effective from April 1, 2014 in respect of certain class of companies and for the others it is effective from April 1, 2015 as detailed below:



Rules Applicable from April 1, 2014 - Regulated Sectors		
Sl. No.	Industry /Sector/ Product/Service	CETA Heading
1.	Telecommunication services made available to users by means of any transmission or reception of signs, signals, writing, images and sounds or intelligence of any nature (other than broadcasting services) and regulated by the Telecom Regulatory Authority of India under the Telecom Regulatory Authority of India Act, 1997 (24 of 1997);	Not applicable
	Generation, transmission, distribution and supply of electricity regulated by the relevant regulatory body or authority under the Electricity Act, 2003 (36 of 2003), other than for captive generation (referred to in the Electricity Rules, 2005);
	Petroleum products regulated by the Petroleum and Natural Gas Regulatory Board under the Petroleum and Natural Gas Regulatory Board Act, 2006 (19 of 2006);	2709 to 2715;
	Drugs and pharmaceuticals	2901 to 2942; 3001 to 3006.
	Fertilizers;	3102 to 3105.
	Sugar and industrial alcohol;	1701; 1703; 2207

Rules Applicable from April 1, 2014 - Regulated Sectors		
Sl. No.	Industry /Sector/ Product/Service	CETA Heading
	Machinery and mechanical appliances used in defence, space and atomic energy sectors excluding any ancillary item or items; Explanation. - For the purposes of this sub-clause, any company which is engaged in any item or items supplied exclusively for use under this clause, shall be deemed to be covered under these rules.	8401 to 8402; 8801 to 8805; 8901 to 8908
	Turbo jets and turbo propellers;	8411
	Arms and ammunitions;	3601 to 3603; 9301 to 9306
	Propellant powders; prepared explosives (other than propellant powders); safety fuses; detonating fuses; percussion or detonating caps; igniters; electric detonators;	3601 to 3603
	Radar apparatus, radio navigational aid apparatus and radio remote control apparatus;	8526
	Tanks and other armoured fighting vehicles, motorised, whether or not fitted with weapons and parts of such vehicles, that are funded (investment made in the company) to the extent of ninety percent or more by the Government or Government agencies;	8710



Port services of stevedoring, pilotage, hauling, mooring, re-mooring, hooking, measuring, loading and unloading services rendered by a Port in relation to a vessel or goods regulated by the Tariff Authority for Major Ports under section 111 of the Major Port Trusts Act, 1963 (38 of 1963);	Not applicable
Aeronautical services of air traffic management, aircraft operations, groundsafety services, ground handling, cargo facilities and supplying fuel rendered by airports and regulated by the Airports Economic Regulatory Authority under the Airports Economic Regulatory Authority of India Act, 2008 (27 of 2008);	Not applicable
Steel;	7201 to 7229; 7301 to 7326
Roads and other infrastructure projects corresponding to para No.(1) (a) as specified in Schedule VI of the Companies Act, 2013;	Not applicable
Rubber and allied products being regulated by the Rubber Board constituted under the Rubber Act, 1947 (XXIV of 1947)	4001 to 4017
Railway or tramway locomotives, rolling stock, railway or tramway fixtures and fittings, mechanical (including electro mechanical) traffic signalling equipment's of all kind;	8601 to 8608
Cement;	2523; 6811 to 6812
Ores and Mineral Products;	2502 to 2522; 2524 to 2526; 2528 to 2530; 2601 to 2617
Mineral fuels (other than Petroleum), mineral oils etc.;	2701 to 2708
Base metals;	7401 to 7403; 7405 to 7413; 7419; 7501 to 7508; 7601 to 7614; 7801 to 7802; 7804; 7806; 7901 to 7905; 7907; 8001; 8003; 8007; 8101 to 8113.
Inorganic chemicals, organic or inorganic compounds of precious metals, rare-earth metals of radioactive elements or isotopes, and Organic Chemicals;	2801 to 2853; 2901 to 2942; 3801 to 3807; 3402 to 3403; 3809 to 3824
Jute and Jute Products;	5303, 5310
Edible Oil;	1507 to 1518
Construction Industry as per para No.(5) (a) as specified in Schedule VI of the Companies Act, 2013 (18 of 2013)	Not applicable
Health services, namely functioning as or running hospitals, diagnostic centres, clinical centres or test laboratories;	Not applicable
Education services, other than such similar services falling under philanthropy or Production, import and supply or trading of following medical devices, namely:	Not applicable



	Cardiac Stents, Drug Eluting Stents, Catheters, Intra Ocular Lenses, Bone Cements, Heart Valves, Orthopedic Implants, Internal Prosthetic Replacements, Scalp Vein Set, Deep Brain Stimulator, Ventricular peripheral Shod, Spinal Implants, Automatic Impalpable Cardiac Deflobillator, Pacemaker (temporary and permanent), patent ducts arteriosus, atrial septal defect and ventricular sepal defect closure device, Cardiac Re-synchronize Therapy, Urethra Spinicture Devices, Sling male or female, Prostate occlusion device, Urethral Stents	9018 to 9022
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Rules Applicable from April 1, 2015 - Non-Regulated Sectors		
Sl.	Industry /Sector/ Product/Service	CETA Heading
	Coffee and tea;	0901 to 0902
	Milk powder;	0402
	Insecticides;	3808
	Plastics and Polymers;	3901 to 3914; 3916 and 3921; 3925
	Tyres and Tubes;	4011 to 4013
	Paper;	4801 to 4802
	Textiles;	5004 to 5007; 5106 to 5113; 5205 to 5212; 5303; 5310; 5401 to 5408; 5501 to 5516
	Glass;	7003 to 7008, 7011, 7016
	Other machinery;	8403 to 8487
	Electricals or electronic machinery;	8501 to 8507; 8511 to 8512; 8514 to 8515; 8517; 8525 to 8536; 8538 to 8547

APPOINTMENT OF COST AUDITOR

Procedure

The cost auditor is to be appointed by the Board of Directors (BOD) on the recommendation of the Audit Committee, where the company is required to have an Audit Committee. The cost auditor proposed to be appointed is required to give a letter of consent to the Board of Directors. The company shall inform the cost auditor concerned of his or its appointment as such and file a notice of such appointment with the Central Government within a period of thirty days of the Board meeting in which such appointment is made or within a period of one hundred and eighty days of the commencement of the financial year, whichever is earlier, through electronic mode, in form CRA-2 along with the fee as specified in Companies (Registration Offices and Fees) Rules, 2014

Any casual vacancy in the office of a cost auditor, whether due to resignation, death or removal, shall be filled by the Board of Directors (BOD) within thirty days of occurrence of such vacancy and the company shall inform the Central Government in Form CRA-2 within thirty days of such appointment of cost auditor.



Who can be appointed cost auditor?

Only a Cost Accountant, as defined under section 2(28) of the Companies Act, 2013, can be appointed as a cost auditor.

Clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 defines "Cost Accountant". It means a Cost Accountant who holds a valid certificate of practice under sub-section (1) of section 6 of the Cost and Works Accountants Act, 1959 and is in whole-time practice. Cost Accountant includes a Firm of Cost Accountants and a LLP of cost accountants.

Eligibility criteria for appointment as a cost auditor

Eligibility Criteria under Section 141 of the Companies Act, 2013 read with Rule 10 of the Companies (Audit and Auditors) Rules, 2014 and Section 148 of the Companies Act, 2013. The following persons are not eligible for appointment as a cost auditor:

A body corporate. However, a Limited Liability partnership registered under the Limited Liability Partnership Act, 2008 can be appointed. [Section 141(3)(a)].

An officer or employee of the company. [Section 141(3)(b)].

A person who is a partner, or who is in the employment, of an officer or employee of the company. [Section 141(3)(c)].

A person who, or his relative or partner is holding any security of or interest in the company or any of its subsidiary or of its holding or associate company or a subsidiary of such holding company. [Section 141(3)(d)(i)].

Relatives of any partner of the firm holding any security of or interest in the company of face value exceeding ₹ 1 lakh. [Section 141(3)(d)(i) and Rule 10(1) of Companies (Audit and Auditors) Rules, 2014].

A person who is indebted to the company or its subsidiary, or its holding or associate company or a subsidiary or such holding company, for an amount exceeding ₹ 5 lakhs. [Section 141(3)(d)(ii) and Rule 10(2) of Companies (Audit and Auditors) Rules, 2014].

A person who has given any guarantee or provided any security in connection with the indebtedness of any third person to the company or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for an amount exceeding ₹ 1 lakh. [Section 141(3)(d)(iii) and Rule 10(3) of Companies (Audit and Auditors) Rules, 2014].

A person or a firm who, whether directly or indirectly, has business relationship with the company or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company. [Section 141(3)(e) and Rule 10(4) of Companies (Audit and Auditors) Rules, 2014].

"Business Relationship" is defined in Rule 10(4) of Companies (Audit and Auditors) Rules, 2014 and the same shall be construed as any transaction entered into for a commercial purpose, except commercial transactions which are in the nature of professional services permitted to be rendered by a cost auditor or a cost audit firm under the Act and commercial transactions which are in the ordinary course of business of the company at arm's length price - like sale of products or services to the cost auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.



A person whose relative is a director or is in the employment of the company as a director or key managerial personnel of the company. [Section 141(3)(f)].

A person who is in the full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor if such person or persons is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies. [Section 141(3)(g)].

A person who has been convicted by a court for an offence involving fraud and a period of ten years has not elapsed from the date of such conviction. [Section 141(3)(h)].

Any person whose subsidiary or associate company or any other form of entity, is engaged as on date of appointment in consulting and providing specialised services to the company and its subsidiary companies: [Section 141(3)(i) and Section 144].

- accounting and book keeping services
- internal audit
- design and implementation of any financial information system
- actuarial services
- investment advisory services
- investment banking services
- rendering of outsourced financial services
- management services

Is Rotation applicable to cost auditor?

The provisions for maintenance of cost accounting records and cost audit are governed by Section 148 of the Companies Act, 2013. The provisions of Section 148 clearly states that no person appointed under Section 139 as an auditor of the company shall be appointed for conducting audit of cost records of the company. Section 148 also provides that qualifications, disqualifications, rights, duties and obligations applicable to auditors (financial) shall apply to a cost auditor appointed under this section. The eligibility, qualifications and disqualifications are provided in Section 141 of the Act and powers and duties are provided in Section 143. Section 143(14) specifically states that the provisions of Section 143 shall mutatis mutandis apply to a cost auditor appointed under Section 148. There are no other provisions governing the appointment of a cost auditor.

Section 139(3) of the Act, applicable to appointment of auditors (financial), and Rule 6 of Companies (Audit and Auditors) Rules, 2014 deals with the provision of rotation of auditors and these provisions are applicable only to appointment of auditors (financial). The Act does not provide for rotation in case of appointment of cost auditors and the same is not applicable to a cost auditor. It may, however, be noted that though there is no statutory provision for rotation of cost auditors, individual companies may do so as a part of their policy, as is the practice with Public Sector Undertakings.

Authority for fixing Remuneration of a Cost Auditor

Rule 14 of the Companies (Audit and Auditors) Rules, 2014 has laid down the procedure of appointment and fixing the remuneration of a cost auditor. It states as follows:

Remuneration of the Cost Auditor: For the purpose of sub-section (3) of section 148-
in the case of companies which are required to constitute an audit committee-

the Board shall appoint an individual, who is a cost accountant in practice, or a firm of cost accountants in practice, as cost auditor on the recommendations of the Audit committee, which shall also recommend remuneration for such cost auditor;

the remuneration recommended by the Audit Committee under (i) shall be considered and approved by the Board of Directors and ratified subsequently by the shareholders;

in the case of other companies which are not required to constitute an audit committee, the Board shall appoint an individual who is a cost accountant in practice or a firm of cost accountants in practice as cost auditor and the remuneration of such cost auditor shall be ratified by shareholders subsequently.

Obligation to report offence of fraud

Sub-rule (7) of Rule 6 of the Companies (Cost Records and Audit) Rules 2014 states that "the provisions of sub-section (12) of section 143 of the Act and the relevant rules made thereunder shall apply mutatis mutandis to a cost auditor during performance of his functions under section 148 of the Act and these rules".

As per sub-section (12) of section 143 of the Companies Act 2013, extract of which is given above, it is obligatory on the part of cost auditor to report offence of fraud which is being or has been committed in the company by its officers or employees, to the Central Government as per the prescribed procedure under the Rules.

As per the proviso to above sub-section, it has been stated that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as may be prescribed.

Cost Audit Report

As per sub-rule (4) of Rule 6 of the Companies (Cost Records and Audit) Rules 2014 as amended, a Cost Auditor is required to submit the Cost Audit Report along with his or its reservations or qualifications or observations or suggestions, if any, in form CRA-3 to Board of Directors of the company within a period of one hundred and eighty days from the closure of the financial year to which the report relates.



Form for filing Cost Audit Report with the Central Government

As per sub-rule (6) of Rule 6 of the Companies (Cost Records and Audit) Rules 2014 as amended, every company to whom cost auditor submits his or its report shall, within a period of thirty days from the date of receipt of a copy of the cost audit report, furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein, in form CRA-4 along with fees specified in the Companies (Registration Offices and Fees) Rules, 2014. The report shall be filed using XBRL taxonomy.

It is to be noted that the cost audit report is required to be filed in XBRL format.

SECRETARIAL AUDIT

Extract of Provision of Section 204 of the Companies Act 2013 Section 204.

(1) Every listed company and a company belonging to other class of companies as may be prescribed in rule 9 of chapter XIII under the Act, shall annex with its Board's report made in terms of sub-section (3) of section 134, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed in rule 9 of chapter XIII under the Act.

Rule 9 Secretarial Audit Report.

(1) For the purposes of sub-section (1) of section 204, the other class of companies shall be as under-

- (a) Every public company having a paid-up share capital of fifty crore rupees or more; or
- (b) Every public company having a turnover of two hundred fifty crore rupees or more.

(2) The format of the Secretarial Audit Report shall be in Form No. MR.3.

(2) It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

(3) The Board of Directors, in their report made in terms of sub-section (3) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his report under sub-section (1).

(3) If a company or any officer of the company or the company secretary in practice, contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

As per section 204(1) of Companies Act, 2013 read with rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014, the following companies are required to obtain Secretarial Audit Report:

Every listed company;

Every public company having a paid-up share capital of fifty crore rupees or more; or-

Every public company having a turnover of two hundred fifty crore rupees or more.

Every company having outstanding loans or borrowings from banks or public financial institutions of ₹100 crores or more.



However the "Turnover" means the aggregate value of the realisation of amount made from the Sale, Supply or Distribution of goods or on account of services rendered, or both, by the company during a financial year [Section 2(91)].

The Secretarial Audit Report is required to be provided in the format prescribed in Form MR-3 (Rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014).

Procedures of appointment of Secretarial Auditor

As per Rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014, Secretarial Auditor is required to be appointed by means of resolution passed at a duly convened Board meeting. It is advisable for the Secretarial Auditor to get a letter of engagement from the company. Secretarial Auditor should accept the letter of engagement. However, it is advisable that any changes in the Secretarial Auditor during the financial year are to be reported to the members in the Board's Report. The qualifications, observations or comments / remarks of the secretarial Audit Report shall be read at the annual general meeting of the company along with the explanation and comments of the Board of Directors (Clause 13 of Secretarial Standard - 2).

Self Examination questions

1. Which Rules govern maintenance of cost accounting records and cost audit as per Section 148 of the Companies Act, 2013?
2. What is the applicability of the Companies (Cost Records and Audit) Rules, 2014 and what is the date on which it becomes effective and applicable?
3. The Rules state that cost records are to be maintained in Form CRA-1. However, CRA-1 does not prescribe any format but only provides principles to be followed for different cost elements. What are the role and status of Cost Accounting Standards/GACAP and its applicability vis-à-vis CRA-1?
4. What is the procedure for appointment of cost auditor under the Companies Act, 2013?
5. Who can be appointed as a cost auditor?
6. What are the eligibility criteria for appointment as a cost auditor?
7. The Companies Act, 2013 has introduced provision regarding rotation of auditors. Is the provision of rotation of auditors applicable to cost auditors also?
8. What is the procedure to be followed for fixing the remuneration of a cost auditor?
9. Who can conduct the Secretarial Audit and which company have to undergo such?
10. Discuss the procedures of appointment of Secretarial Auditor.



State whether the following statements are true or false.

- Cost Records are to be maintained as per Form CRA-1.
- The Cost Auditor has to follow the Cost Auditing Standards while conducting Cost Audit.
- Cost Accounting Standards is mandatory as per section 143 of the companies Act 2013.
- CRA-2 is used to intimate the appointment of Cost Auditor to the Central Government.
- Chartered Accountants are eligible to conduct Secretarial Audit having valid certificate of practice.
- Company Secretaries are eligible to conduct Cost Audit having valid certificate of practice.
- Secretarial Audit is applicable to all unlisted companies.
- Secretarial Audit report is given as per the Form MR-3.
- Appointment of Secretarial Auditor is done by means of resolution at Board Meetings.
- Secretarial Audit Report is attached with the Board report.

[Answer: T, T, F, T, F, F, F, T, T, T]

Fill in the blanks

- Secretarial Audit is applicable to all _____ companies.
- Cost Audit is done by _____ in practice having valid certificate of practice.
- Secretarial Audit is done by _____ in practice having valid certificate of practice.
- Cost Records are to be maintained in form _____.
- Format for Secretarial Audit report is form _____.
- Secretarial Audit is applicable to public companies having paid up share capital of _____ crore or more.
- Secretarial Audit is applicable to public companies having turnover of _____ crore or more.
- Secretarial Audit is covered under Section _____ of the companies Act 2013.
- Cost Audit is covered under Section _____ of the companies Act 2013.
- Cost Auditor is required to be appointed by the _____ of the company on recommendation of Audit Committee.

[Answer: Listed, Cost Accountant, Company Secretary, CRA-1, MR-3, 50 crore, 200 crore, 204, 148, Board of Directors]

Match the following

	Column A		Column B
1	Secretarial Audit Report	A	CRA-1
2	Sec 204 of the companies Act	B	Cost Audit
3	Secretarial Audit	C	Board of Directors
4	Intimation for appointment of cost auditor to Central Government	D	CRA-4
5	Casual vacancy in the office of a Cost Auditor is filled by-	E	Cost Audit report by the Auditor to Company
6	Form for filing Cost Audit Report with the Central Government	F	MR-3
7	Sec 148 of the companies Act	G	1 Lakh rupees which can extend to 5 Lakh rupees
8	CRA 3	H	Secretarial Audit
9	Cost Accounting Records	I	Listed Companies
10	Penalty for non compliance of Sec 204	J	CRA-2

[Answer: F, H, I, J, C, D, B, E, A, G]

Multiple Choice Questions

- Cost Audit can be done by the-
 - Employee of the organization
 - Cost Auditor
 - Secretarial Auditor
 - None of the above
- Secretarial Audit can be done by-
 - Employee of the organization
 - Cost Auditor
 - Secretarial Auditor
 - None of the above
- Form for maintainence of Cost Records by the Company.
 - CRA-1
 - CRA-2
 - CRA-3
 - CRA-4



4. Secretarial Audit is applicable to the public sector company having the paid up share capital of-
- (a) 50 crore
 - (b) 75 crore
 - (c) 100 crore
 - (d) 200 crore
5. Secretarial Audit is applicable to the public sector company having the turnover of-
- (a) 100 crore
 - (b) 200 crore
 - (c) 250 crore
 - (d) 300 crore
6. Form for Secretarial Audit Report is-
- (a) MR-2
 - (b) MR-3
 - (c) MR-4
 - (d) MR-5
7. Cost Auditor is appointed by the-
- (a) Audit Committee
 - (b) BOD
 - (c) BOD on recommendation Audit Committee
 - (d) None of the above

[Answer: B, C, A, A, C, B, C]

7.3 REPORTING REQUIREMENTS UNDER COMPANIES ACT, REPORT Vs. CERTIFICATE, CONTENTS OF THE REPORTS & QUALIFICATIONS IN THE REPORT

SCOPE, BASIC ELEMENTS AND SIGNIFICANCE OF AUDIT REPORT

Concept & Definitions

While conducting every audit auditor has to go through three phases

- Preliminary work for audit.
- Conduct of actual audit, and
- Conclusion of audit, which means submission of Audit Report.

Therefore, Audit Report is called as the ultimate and final product of every audit.

The meaning of Audit Report can be well understood from the following selected definitions.

Lancaster – “A Report is a statement of collected & considered facts, so drawn up as to give clear and concise information to persons who are not already in possession of the full facts of the subject matter of the report.”

J. B. Ray – “The Report shall either contain an expression of opinion regarding the financial statements, taken as a whole or an assertion to the effect that an opinion cannot be expressed when an overall opinion cannot be expressed, the reason therefore should be stated. In all cases, where auditor's name is associated with financial statements the report should contain a clear cut indication of the character of the auditor's examination, if any, and the degree of responsibility he is taking.”

In short, the Audit Report is nothing but a statement of observation gathered & considered while proving conclusive evidence of company's financial position. It is a medium through which an auditor expresses his opinion on the financial statement under audit. It is an important part of the audit as it provides the results of the audit conducted by the auditor.

Importance of Audit Report

An Audit report is the end product of the auditing & concluding part of the audit process.

Audit report gives the auditor's opinion on the accounts & record of the company, as examined by him.

Audit Report reflects the work done by the auditor.

Audit report is the instrument which, measures the auditor's responsibility in regard to the true & fairness of the financial statement of the company.

Audit Report indicates the real position of the financial status of the company & which is used by different stakeholders as a reliable document to assess the financial condition of the company.

The Basic Elements of the Auditors' Report are –

Title: The Auditor's Report should have an appropriate title i.e. “Auditor's Report”. It should be distinguished from other Reports, e.g. reports of officers of the entity, Board of Directors.

Addressee: The Auditor's Report should be appropriately addressed as required by the circumstances of the engagement and applicable laws and regulations. Ordinarily, the Auditor's Report is addressed to the authority appointing the Auditor. In case of statutory auditor, it is addressed to shareholders and in case of internal Audit to the Board.

Opening or Introductory Paragraph:

The Auditor's Report should identify the Financial Statements of the entity that have been audited, including the date of and period covered by the Financial Statements.



The Report should include a Statement that the Financial Statements are the responsibility of the entity's management and a Statement that the responsibility of the Auditor is to express an opinion on the Financial Statements based on the audit.

Scope Paragraph:

The Auditor's Report should describe the scope of the audit by stating that the audit was conducted in accordance with standards on auditing generally accepted in India.

The Report should include a statement that the audit was planned and performed to obtain reasonable assurance whether the Financial Statements are free of material misstatement.

The Auditor's Report should describe the Audit as including examining, on a test basis, evidence to support the amounts and disclosures in Financial Statements, assessing the accounting principles used in the preparation of the Financial Statements, assessing significant estimates made by management, in the preparation of Financial Statements, & evaluating the overall position of Financial Statements.

The Report should include a statement by the Auditor that the audit provides a reasonable basis for his opinion.

Opinion Paragraph: The Opinion paragraph of the Report should indicate the Financial Reporting framework used to prepare the Financial Statements. It should state the Auditor's opinion as to whether the Financial Statements give a true and fair view in accordance with the financial reporting framework and, where appropriate, whether the Financial Statements comply with the statutory requirements.

Date of the Report: The date of an Auditor's Report is the date on which the Auditor signs the Report expressing an opinion on the Financial Statements. The Auditor should not date the Report earlier than the date on which the Financial Statements are signed or approved by Management. However, they can commence audit earlier.

Place of Signature: The Report should name the specific location, which is ordinarily the city where the Audit Report is signed.

Auditor's Signature: The Report should be signed by the Auditor in his personal name. Where a Firm is appointed as the Auditor, the Report should be signed in the personal name of the Auditor and in the name of the Audit Firm. The Partner / Proprietor signing the Report should mention his ICAI Membership Number, preferably with seal/rubber stamp.

Note: Where the governing statute requires the Auditor to include certain matters in his Report or prescribe the form in which the Auditor should issue his Report, such additional matters should be included in addition to the requirements of SA 700 on "Forming an opinion and reporting on financial statements."

Significance of Opening Paragraph:

The Opening or Introductory Paragraph identifies the Financial Statements of the entity that have been audited, including the date of and period covered by the Financial Statements.

The 'Opening Paragraph' seeks to bring to the notice of the Users of Financial Statements, that preparation of the accounts is the responsibility of the Management of the enterprise, whereas the responsibility of the Auditor is to express an opinion on the said accounts based on the audit carried out by him.

Through the Opening Paragraph, the Auditor communicates the basic message that the preparation of Financial Statements requires Management to make significant accounting estimates and judgements, as well as to determine the appropriate accounting principles and methods used in preparation of the said Financial Statements.

Significance of Scope Paragraph:

The 'Scope Paragraph' seeks to inform the Users about the practices and procedures followed in the conduct of audit by the Auditor.

In the Scope Paragraph, the Auditor states that the audit was planned and performed in accordance with Standards on Auditing generally accepted in India, and also that the audit provides a reasonable basis for his opinion.

The significance of the Scope Paragraph lies in the fact that the Auditor intends to convey to the readers of his report, about the scope of audit by highlighting the nature and progress of audit. The test check approach of audit adopted by the Auditor in performing his audit work as also the significant aspect of evaluation of accounting principles and accounting estimates is also clarified.

The basic objective of auditing that the Auditor provides only "reasonable assurance" is emphasized in the Scope Paragraph. Thus, this paragraph signifies the inherent limitations of audit.

UNQUALIFIED OPINION

An opinion is said to be unqualified, when the Auditor concludes that the Financial Statements give a true and fair view in accordance with the financial reporting framework used for the preparation and presentation of the Financial Statements. Or,

The Auditor gives a Clean or Unqualified Report, when he does not have any significant negative reservation in respect of matters contained in the Financial Statements. Unqualified opinion is the best audit report which company can expect.



An Unqualified Opinion indicates the following -

The Financial Statements have been prepared using the Generally Accepted Accounting Principles, which have been consistently applied,

The Financial Statements comply with relevant statutory requirements and regulations, and

There is adequate disclosure of all material matters relevant to the proper presentation of the financial information, subject to statutory requirements, where applicable.

Any changes in the accounting principles or in the method of their application, and the effects thereof, have been properly determined and disclosed in the Financial Statements. For issuing an Unqualified Audit Report, the Auditor has to satisfy himself that -

Evidence: Reasonable evidence is obtained in support of transactions recorded in the books of account.

Standards: Accounting entries passed in the books of account are in conformity with the generally applicable accounting principles and Indian Accounting Standards followed consistently.

True and Fair: The Financial Statements prepared represent a true and fair summary of the transactions that took place during the year.

Classification: The process of classification and aggregation followed in the preparation of the Financial Statements is fair and it does not hide a material fact nor does it highlight something, which may distort the real state of affairs.

Format: The form of Financial Statements is in accordance with the form prescribed by law, if any.

Free of Misstatements: There are no material misstatements in the Financial Statements. No material transaction recorded in the books of account is illegal or beyond the legal competence of the Company.

Disclosure: All the disclosures statutorily required or otherwise relevant have been made appropriately.

Modified Audit Report

When the Auditor issues any Report other than unqualified, his Report is said to be modified. As per SA 750, an Auditor's Report is considered to be modified when it includes –

- Matters That Do Not Affect the Auditor's Opinion - with Emphasis of Matter Paragraph.
- Matters That Do Affect the Auditor's Opinion viz:
 - Qualified Opinion,
 - Disclaimer of Opinion, and,
 - Adverse Opinion.

**Emphasises Matters that do not affect the Auditor's Unqualified Opinion.**

Going Concern Not Resolved: The Auditor should modify the Auditor's Report by adding a paragraph to highlight a material matter regarding a going concern problem where the going concern question is not resolved and adequate disclosures have been made in the Financial Statements.

Significant Uncertainty: The Auditor should consider modifying his Report by adding a paragraph if there is a significant uncertainty (other than going concern problem), the resolution of which is dependent upon future events and which may affect the Financial Statements.

Multiple Uncertainties: In extreme cases, e.g. multiple uncertainties that are significant to the Financial Statements, the Auditor may consider it appropriate to express a Disclaimer of Opinion instead of adding an emphasis of matter paragraph.

Impact of Paragraph: The addition of an emphasis of matter paragraph does not affect the Auditor's opinion. The paragraph would preferably be included preceding the Opinion Paragraph and would ordinarily refer to the fact that the Auditor's opinion is not qualified in this respect.

Example:

"Without qualifying our opinion, we draw attention to Note X of Schedule to the Financial Statements. The entity is the defendant in a lawsuit alleging infringement of certain patent rights and claiming royalties and punitive damages. The entity has filed a counter action, and preliminary hearings and discovery proceedings on both actions are in progress. The ultimate outcome of the matter cannot presently be determined, and no provision for any liability that may result has been made in the Financial Statements.

In our opinion and to the best of our information and according to the explanations given to us, the Financial State-ments give a true and fair view in conformity with the accounting principles generally accepted in India - in the case of the Balance Sheet, of the state of affairs of as at 31st March 2XXX, and in the case of the Profit and Loss Account, of the Profit / Loss for the year ended on that date."

Circumstances that may Result in other than an Unqualified Opinion?

An Auditor may not be able to express an Unqualified Opinion when any of the following circumstances exist and in the Auditor's judgement, the effect of the matter is or may be material to the Financial Statements. [SA 700]

Limitation on Scope: Limitation on scope of Auditor's work may be imposed by the clients or imposed by circumstances. It may lead to situations where the Auditor may have to issue a Qualified Opinion or a Disclaimer of Opinion.



Disagreement with management: The Auditor may disagree with the Management as to - (a) the acceptability of the accounting policies selected, or the method of their application, (b) the adequacy of disclosure in the Financial Statements, or (c) the compliance of the Financial Statements with relevant regulations and statutory requirements. In such cases, he may have to give an Adverse Opinion or a Qualified Opinion.

Significant Uncertainty: If there is a significant uncertainty affecting the Financial Statements (other than Going Concern problem), for example, litigation involving legal claims, etc. the result of which is dependent upon the resolution of the future events, the Auditor may have to qualify his opinion or disclaim an opinion. However, where such significant uncertainty is not material, the Auditor may issue an Unqualified Opinion, by adding an "Emphasis of Matter" paragraph, without qualifying his opinion.

Manner of Qualification / Disclaimer:

Whenever the Auditor expresses an opinion other than unqualified, a clear description of all the substantive reasons should be included in the report and, unless impracticable, a quantification of the possible effect(s), individually and in aggregate, on the Financial Statements should be mentioned in the Auditor's Report.

Where it is not practicable to quantify the effect of modifications made in the Audit Report accurately, the Auditor may do so on the basis of estimates made by the Management, after carrying out possible audit tests. He should clearly indicate the fact that the figures are based on Management estimates.

This information would be set out in a separate paragraph preceding the opinion or disclaimer of opinion and may include a reference to a more extensive discussion, if any, in a note to the Financial Statements.

QUALIFIED OPINION/ REPORT

A Qualified Audit Report is one where an Auditor gives an opinion on the truth and fairness of Financial Statements, subject to certain reservations.

The Auditor's Reservation is generally stated as: "Subject to the above, we report that the Balance Sheet shows a true and fair view."

The overall impact of all reservations or qualification taken together is not material enough to vitiate the overall true and fair view of Financial Statements, but it is important that such a matter(s) should be brought to the attention of the shareholders.

The Report should also give detailed reasons along with quantitative impact on the qualifications on Financial Statements.

A Qualified Opinion should be expressed when the Auditor concludes that –



An Unqualified Opinion cannot be expressed, or

The effect of any disagreement with Management is not so material and pervasive as to require an Adverse Opinion, or

The Limitation on scope is not so material and pervasive as to require a Disclaimer of Opinion.

Features of a Qualified Report

The features of a Qualified Report are -

Clarity: The Auditor must express the nature of qualification, in a clear and unambiguous manner.

Explanation: Where the Auditor answers any of the statutory affirmations in the negative or with a qualification, his Report shall state the reasons for such answer.

Placement: All qualifications should be contained in the Auditor's Report. When there are Notes, which are subject matter of a qualification, the same should preferably be annexed to the Auditors' Report. However a reference to the Notes to Accounts in the Auditors' Report does not automatically become a qualification.

Subject to: The words "subject to" are essential to state any qualification. The qualification should be preceded by words such as "Subject to" or "Except that" to make it clear that he is making an exception.

Nature of Qualification: Vague statements, the effect of which on accounts cannot be ascertained, like, 'The debtors balances are subject to confirmation', 'No provision for taxation has been made in view of the loss during the year', etc. should be avoided.

Violation of Law: Where the Company has committed an irregularity resulting in a breach of law, the Auditor should bring the same to the notice of the shareholders by properly qualifying his report.

Quantification: The Auditors should quantify, wherever possible, the effect of these qualifications on the Financial Statements if the same is material. Where the effect of qualification cannot be accurately quantified, the Auditor may reflect the effect on the basis of Management estimates, after carrying out necessary audit tests on such estimates.

Notes -

Report Relationship: Where notes of a qualificatory nature appear in the accounts, the Auditors should state all qualifications independently in their report so that the user can assess the significance of these qualifications.



Draft Report: The Auditor may discuss matters of qualification with the Management of the Company to acquire their views. It is not necessary that the Auditor should accept the Management's view and modify his opinion. But it would enable the Auditor to accurately draft the qualifications in his Final Report.

Aspects to be Considered in Qualifying a Report

Examine whether the Auditors are in active disagreement with something which has been done by the Company, or they are merely unable to form an opinion, say, for lack of adequate information about an item.

Establish whether the matters in question are so material as to affect the presentation of a true and fair view of the whole of the affairs of the Company, or they are of such a nature as to affect on particular item disclosed in the ac-counts.

See whether the matters constituting the qualification involve a material contravention of any requirements of the Companies Act, which have a bearing on the accounts.

Illustrations:

Some situations calling for qualifications in Audit Reports are

Where the Auditors are unable to obtain all the information and explanations which they consider necessary for the purposes of their audit, e.g. -

Absence of satisfactory documentary evidence of the existence of ownership of the material assets, such as, title deeds in respect of land,

Absence of vouchers in respect of material payments made by the Company,

Destruction of books and records by fire or accident,

Non-availability of books and records owing to unavoidable circumstances, such as books and records of a foreign branch with which no communication is possible.

Where proper books of accounts have not been kept in accordance with the law.

Where the Balance Sheet and P&L Account are not in agreement with the books of account and returns.

When the information required by law is not furnished.



Board of Directors are required to reply to the qualifications which forms part of the Board's report which is circulated to shareholders.

When the accounts do not disclose a true and fair view like -

Where the accounting practices followed by the Company are not considered appropriate to the circumstances and nature of the business e.g. treatment of HP Sales as outright sales,

Where there has been a change in accounting principles or procedures in relation to material items, such, valuation of stock, depreciation, treatment of by-product cost, etc. without adequate explanation and disclosure of effect of the change,

Where difference of opinion with management has arisen regarding valuation or realisability of assets, such as Stock-in-Trade, Debtors, Loans & Advances or the extent of liabilities, contingent or otherwise,

Where income or expenditure is not properly reflected so as to show a fair figure of profit for the year,

Where information is not required by law to be disclosed but the disclosure of which is considered essential by the Auditors in order to show a true and fair view,

Where there is a contravention of the provisions of the Companies Act having a bearing upon the accounts and transactions of the Company e.g. donations to political parties or for political purposes in contravention of Section 182, or contributions to charitable or other funds in excess of the limitation specified in Section 181;

Where the Company has contravened the provisions of its Memorandum and Articles of Association.

DISCLAIMER OF OPINION

A Disclaimer of Opinion Report is given when the Auditor is unable to form an overall opinion about the matters contained in the Financial Statements.

A Disclaimer of Opinion should be expressed when the possible effect of a limitation on scope is so material and pervasive that the Auditor has not been able to obtain sufficient appropriate audit evidence and is, accordingly, unable to express an opinion on the Financial Statements.

It may happen in situations such as -- (a) when books of account of the Company seized by Income-Tax Authorities, (b) when it is not possible for the Auditor to obtain certain information or (c) when scope of audit work is restricted.

The Auditor will state in his Report that he is unable to term an opinion on the Financial Statements. Such Report is called as "Disclaimer of Opinion Report".



PIECEMEAL OPINION

The Auditor, may in some cases, find that the Financial Statements he has examined present only a partial true and fair view. In such cases, he may report that he is unable to express an opinion, limited to certain items in the statement, with which he is satisfied. Such a situation would warrant a Piecemeal Opinion.

As the name suggests, the Auditor gives a divided opinion on matters with which he is satisfied and with which he is not. The Auditor should state the reasons for having given a Piecemeal Opinion.

ADVERSE OR NEGATIVE REPORT

An Adverse or Negative Report is given when the Auditor concludes that based on his examination, he does not agree with the affirmations made in the Financial Statements / Financial Report.

The Auditor states that the Financial Statements do not present a true and fair view of the state of affairs and the working results of the organisation.

The Auditor should state the reasons for issuing such a report.

An Adverse Opinion should be expressed when the effect of a disagreement is so material and pervasive to the Financial Statements, that the Auditor concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the Financial Statements.

Some Remarks which are not Qualifications.

Meaning: Statements or Observations which are not qualificatory in nature may exist in the Auditor's Report. Some requirements under CARO or inquiry U/S 143 are of this non-qualificatory character.

Conditions under which "Remarks" can be inserted are -

The matter is of such importance in relation to the Balance Sheet as a whole that it should be brought to the notice of the members, and

The point is not clearly brought out on the face of the accounts, as they stand by the note or otherwise, and

The point does not affect the true and fair character of the accounts.

Manner of Reporting: Where it is necessary, either statutorily or otherwise, to include a "remark" in an Audit Report which is not a qualification, the remark should be inserted as a single sentence prior to the Auditor's Opinion which should not include any reference to the remark. This remark can be put in the body of the Auditor's Report only when the Notes on Accounts do not include this information.

Example:

"The properties abroad shown in the Balance Sheet at are in the course of being but have not yet been, registered in the Company's name." (The Opinion Paragraph should not have any reference to the above remark).

Distinguish Between Explanatory Notes and Qualificatory Notes

Explanatory Notes	Qualificatory Notes
An Explanatory Note is meant to explain or supplement a matter contained in or related to Financial Statements.	A Qualificatory Note is intended to communicate the Auditor's reservation on the accounts.
The matter on which an Explanatory Note is given is one on which the Auditor has not taken an adverse view.	Qualificatory Notes on which the Auditor has taken an adverse view e.g. tax provision not made in the accounts.
Explanatory Notes are given by the Directors of the Company.	Qualifications are made by the Auditor in his Report to the Company's shareholders.
These are usually shown under "Notes to Accounts". All Notes, wherever shown, including those required by the Schedule III constitute an integral part of the accounting statement.	These notes are included in the Auditors' Report before the Opinion Paragraph. The reader's attention is drawn to the Qualification paragraph by use of the word "Subject to".

Distinguish Between qualified report and Adverse Report

Situation	Auditor's Duties
When the limitation of scope infringes the duties of the Auditor under the statute.	The Statutory Auditor should not accept the engagement.
1. When the Auditor believes that limitations in the terms of a proposed engagement is of such a nature that he would need to issue a Disclaimer of Opinion.	The Auditor should not accept such a limited engagement as an Audit Engagement.
2. Other limitations imposed by entity or by circumstances - i. When the terms of engagement specify that the Auditor will not carry out an audit procedure which he believes necessary e.g. verification of investments, or, ii. When the timing of the Auditor's work is such that he is unable to observe the counting of physical inventories, or, iii. When in his opinion the accounting records are inadequate, or, iv. When he is unable to carry out an audit procedure that he believes desirable.	(i) The Auditor should carry out reasonable alternative audit procedures to obtain sufficient audit evidence to support an Unqualified Opinion. (ii) If the Auditor is unable to carry out alternative audit procedures or is not satisfied with the evidence obtained by such alternative procedures, he should issue a Qualified Opinion or Disclaimer of Opinion. (iii) The Auditor's Report should describe the limitation and indicate the possible adjustments to the Financial Statements that might have been determined to be necessary had the limitation not existed. (iv) The Auditor cannot escape his responsibility by obtaining Management Certificates or stating that certain audit procedures were not carried out.



Qualified Report	Adverse Report
i. A Qualified Audit Report is one where an Auditor gives an opinion subject to certain reservations.	An Adverse Report is given when the Auditor concludes that based on his examination, he does not agree with the affirmations made in the Financial Statements / Financial Report.
ii. The Auditor's reservation is generally Stated as: "Subject to the above, we report that the Balance Sheet shows a true and fair view."	The Auditor states that the Financial Statements do not present a true and fair view of the state of affairs and working results of the organisation.
iii. The accounts present a true and fair view subject to certain reservations.	The accounts do not present a true and fair view on the whole.
iv. A Qualification is made in the Audit Report when the Auditor has reservation on specific item(s) of material nature.	An Adverse Report is given when the Auditor has his reservations on the true and fair view presented by the Financial Statements.

Distinguish between Clean Audit Report and Qualified Audit Report.

Clean Audit Report	Qualified Audit Report
The Auditor issues a Clean Report (also called as unconditional opinion) when he does not have any reservation with regard to the matters contained in the Financial Statements.	A Qualified Audit Report is one where an Auditor gives an opinion subject to certain reservations.
In a Clean Report, the Auditor states that the Financial Statements give a true and fair view of the state of affairs and results for the period.	The Auditor's reservation is generally stated as - "Subject to the above, we report that the Balance Sheet shows a true and fair view."
The Auditor is justified in issuing a clean report if - (i) The accounts are prepared using generally accepted accounting principles. (ii) The Auditor has examined sufficient reliable evidence in respect of transactions recorded in the books. (iii) The transactions recorded represent a true recording of the events. (iv) The transactions are within the legal competence of the entity. (v) There are no material misstatements in the Financial Statements. (vi) The Financial Statements comply with the format and disclosure requirements as per the Statute.	A Qualified Opinion should be expressed when the Auditor concludes that - i. An Unqualified Opinion cannot be expressed, ii. The effect of any disagreement with Management is not so material and pervasive as to require an Adverse Opinion, or iii. The Limitation on scope is not so material and pervasive as to require a Disclaimer of Opinion.
There is no specific duty of Management for Clean Reports.	Management is bound to give explanation & full details in respect of each qualification in the Auditors Report. [Section 134]

Both adverse opinion and disclaimer talk bad about the company.

**Date of the Audit Report.**

Since significant events may take place from the date of Financial Statements, date of completing audit field work and date of Audit Report, the date of the Audit Report should be the actual date of completion of audit.

Any event coming to be known after the date of the Audit Report is not the responsibility of the Auditor even though it may have a highly significant effect on the Financial Statements reported upon.

Even though the Audit Report may be actually prepared at a date later than the date of actual completion of the audit work, it is desirable that it should be made as on the former date to limit the Auditors' responsibility.

In relation to reporting on Company Accounts, it is possible for the Auditor to report on the same day on which the Financial Statements are approved by the Board of Directors.

Significance of the phrase "to the best of our Information and according to the explanations given to us" which is generally found in the Auditors' Reports.

Narrow Interpretation:

The Statement "to the best of our information and according to the explanations given to us" is an expression of opinion by the Auditors.

Such opinion is a matter of professional judgement to be exercised by the Auditors under the given situations.

Auditors will not be held responsible if they acted on information and explanations, which they **behave** to be bonafide, but which are as a matter of fact untrue or incorrect. They have to exercise reasonable care and skill in the evaluation of information made available to them.

As a narrow interpretation of the phrase, the Auditors may state that they have acted on the basis of explanations given to them. To that extent this phrase definitely restricts the scope of enquiry to be made by an Auditor.

Broad Interpretation:

The Auditors should apply professional judgment to obtain all that information and explanations, which are necessary for the performance of conducting the audit.

Under the Chartered Accountants (CA) Act 1959, a (CA) Chartered Accountant is guilty of professional misconduct if he fails to obtain sufficient information which is necessary for the expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion.

There may be situations where –

the Balance Sheet shows the correct position as per books but other information indicate that the books themselves were incorrect, the Financial Statements do not reflect proper position which could have been revealed had the Auditor obtained necessary information during the course of audit.



At a wider interpretation level, the Auditor should obtain all information and explanations, which he deems necessary, for the expression of an opinion. If he does not obtain all such information, he is entitled to issue a Disclaimer of Opinion Report.

Conclusion: Hence, the given phrase is a double-edged sword, which may be interpreted either to restrict the scope of enquiry or to stretch responsibilities beyond a limit.

Significance of Obtaining Information and Explanations from the Management.

Legal Recognition: Legal recognition is given to the process of obtaining information as part of the whole auditing process. The provisions of the Companies Act in this regard are -

(a) Where any particulars or information is required to be given in the Balance Sheet or P&L Account of a Company or in any document required to be annexed or attached thereto, it shall be the duty of the concerned Officer of the Company to furnish without delay, to the Company, and also to the Company's Auditor, whenever he so requires, those particulars or that information in as full a manner as possible.

The Company Auditor should state whether he has obtained all the information and explanations which to the best of his knowledge and belief, were necessary for the purpose of his audit. [Section 143]

Management's Responsibility and Auditor's Limitations:

Auditors cannot be expected to know all the technicalities and the complexities of the business deals.

Further, the relevant papers and documents to explain the transactions may not be really available to the Auditor and, even if they are available they may still need to be explained so that one can clearly understand the impact of the transactions on the accounts.

The Management, which actually enters into transactions on behalf of the Company, is expected to have thoroughly understood the implications of all material transactions, and hence Auditors are empowered to obtain explanations from the management.

Auditors' Responsibility:

If any vital information is deliberately withheld from the Auditor in the ordinary course of audit, and he had no means to know the existence of such information, in case the accounts turn to be wrong for that reason, the Auditor should not be held guilty or negligent.

If however, the Auditor has means to know of the existence of such vital information but he ignored it, he would be held guilty on that account.

Where the Auditor has not been able to obtain all information and explanations as required he should issue a Modified Audit Report (i.e. other than an Unqualified Report)



Branch Audit Reports be Considered by the Statutory Auditor

Forwarding of Branch Audit Reports: Where the branch audit carried out by a person other than the Statutory Auditor, the Branch Auditor shall prepare a report on the accounts of the branch office examined by him and forward the same to the Company's Auditor who shall deal with the same in such manner as he considers necessary. [Section 143]

Qualifications in Branch Audit Reports: If the Branch Auditor's Report contains any qualification, the Statutory Auditors should normally include it in their own report unless they are satisfied that either -

Objections raised by the Branch Auditor have been met while preparing the Company's accounts or during the conduct of the Company's audit, or

The matter on which the qualification is made is not material in the context of the Company's Accounts as a whole, or

In the light of information and explanations given to them, which were not available to the Branch Auditor, they are satisfied that the qualification is not called for.

Scope of Enquiry u/s 143(1) of the Act

Inquiry: Every auditor of the company should inquire into the following matters, namely:—

- (a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;
- (b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;
- (c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company;
- (d) whether loans and advances made by the company have been shown as deposits;
- (e) whether personal expenses have been charged to revenue account;
- (f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

Provided that the auditor of a company which is a holding company shall also have the right of access to the records of all its subsidiaries in so far as it relates to the consolidation of its financial statements with that of its subsidiaries.



Report:

- (a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;
 - (b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;
 - (c) whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;
 - (d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;
 - (e) whether, in his opinion, the financial statements comply with the accounting standards;
 - (f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;
 - (g) whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;
 - (h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;
 - (i) whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls;
- such other matters as may be prescribed.

CARO – COMPANIES (AUDITOR'S REPORT) ORDER, 2016

CARO – COMPANIES (AUDITOR'S REPORT) ORDER, 2016 issued by the Central Government as per the power granted under section 143(11) of the Companies Act, 2013.

According to Sec 143, the auditor is required to report on certain matters only if he is not satisfied after his examination of the accounts but after this new order, the auditor has to make a statement on each of the specified matters likewise in case of Govt. companies, this order is in addition to the directions of the Comptroller and Auditor General in India.

This new order is applicable to every company except.

a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);

an insurance company as defined under the Insurance Act, 1938 (4 of 1938);

a company licensed to operate under section 8 of the Companies Act;

a One Person Company as defined under clause (62) of section 2 of the Companies Act and a small company as defined under clause (85) of section 2 of the Companies Act; and a private limited company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than rupees one crore as on the balance sheet date and which does not have total borrowings exceeding rupees one crore from any bank or financial institution at



any point of time during the financial year and which does not have a total revenue as disclosed in Scheduled III to the Companies Act, 2013 (including revenue from discontinuing operations) exceeding rupees ten crore during the financial year as per the financial statements.

Auditor's report to contain matters specified in paragraphs 3 and 4. - Every report made by the auditor under section 143 of the Companies Act, 2013 on the accounts of every company audited by him, to which this Order applies, for the financial years commencing on or after 1st April, 2015, shall in addition, contain the matters specified in paragraphs 3 and 4, as may be applicable:

Provided the Order shall not apply to the auditor's report on consolidated financial statements.

Matters to be included in the auditor's report. - The auditor's report on the accounts of a company to which this Order applies shall include a statement on the following matters, namely:-

- (a) whether the company is maintaining proper records showing full particulars, including quantitative details and situation of fixed assets;
- (b) 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;
- (c) whether the title deeds of immovable properties are held in the name of the company. If not, provide the details thereof;
- (d) whether physical verification of inventory has been conducted at reasonable intervals by the management and whether any material discrepancies were noticed and if so, whether they have been properly dealt with in the books of account;
- (e) whether the company has granted any loans, secured or unsecured to companies, firms, Limited Liability Partnerships or other parties covered in the register maintained under section 189 of the Companies Act, 2013. If so,
- (f) whether the terms and conditions of the grant of such loans are not prejudicial to the company's interest;
- (g) whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;
- (h) if the amount is overdue, state the total amount overdue for more than ninety days, and whether reasonable steps have been taken by the company for recovery of the principal and interest;
- (i) in respect of loans, investments, guarantees, and security whether provisions of section 185 and 186 of the Companies Act, 2013 have been complied with. If not, provide the details thereof.



- (j) in case, the company has accepted deposits, whether the directives issued by the Reserve Bank of India and the provisions of sections 73 to 76 or any other relevant provisions of the Companies Act, 2013 and the rules framed there under, where applicable, have been complied with? If not, the nature of such contraventions be stated; If an order has been passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any court or any other tribunal, whether the same has been complied with or not?
- (k) whether maintenance of cost records has been specified by the Central Government under sub-section (1) of section 148 of the Companies Act, 2013 and whether such accounts and records have been so made and maintained.
- (l) whether the company is regular in depositing undisputed statutory dues including provident fund, employees' state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as on 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;
- (m) where dues of income tax or sales tax or service tax or duty of customs or duty of excise or value added tax have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned. (A mere representation to the concerned Department shall not be treated as a dispute).
- (n) Whether the company has defaulted in repayment of loans or borrowing to a financial institution, bank, Government or dues to debenture holders? If yes, the period and the amount of default to be reported (in case of defaults to banks, financial institutions, and Government, lender wise details to be provided).
- (o) Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported;
- (p) whether any fraud by the company or any fraud on the Company by its officers or employees has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated;
- (q) Whether managerial remuneration has been paid or provided in accordance with the requisite approvals mandated by the provisions of section 197 read with Schedule V to the Companies Act? If not, state the amount involved and steps taken by the company for securing refund of the same;
- (r) Whether the Nidhi Company has complied with the Net Owned Funds to Deposits in the ratio of 1: 20 to meet out the liability and whether the Nidhi Company is maintaining ten per cent unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability;
- (s) Whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards;



- (t) Whether the company has made any preferential allotment or private placement of shares or fully or partly convertible debentures during the year under review and if so, as to whether the requirement of section 42 of the Companies Act, 2013 have been complied with and the amount raised have been used for the purposes for which the funds were raised. If not, provide the details in respect of the amount involved and nature of non-compliance;
- (u) Whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether the provisions of section 192 of Companies Act, 2013 have been complied with;
- (v) Whether the company is required to be registered under section 45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained.

Reasons to be stated for unfavorable or qualified answers.-

Where, in the auditor's report, the answer to any of the questions referred to in paragraph 3 is unfavorable or qualified, the auditor's report shall also state the basis for such unfavorable or qualified answer, as the case may be.

Where the auditor is unable to express any opinion on any specified matter, his report shall indicate such fact together with the reasons as to why it is not possible for him to give his opinion on the same.

AUDITOR'S REPORT ON REVISED ACCOUNTS OF COMPANIES BEFORE CIRCULATION TO SHAREHOLDERS

There may be instances, where the Management of a Company amends its audited accounts, and re-approves it and then requests the Statutory Auditors to make a Report once again on the amended accounts. The Auditors' duties in this regard are enumerated below;

Return: Ensure that all copies of the Original Accounts and Report are returned to the Auditor.

Disclosure: Ensure that the fact of Revision of accounts already approved by the Board and reported upon by the Statutory Auditors, appears as a specific Note on the amended accounts.

Reporting: Reporting requirements are as under

Adequate Disclosure: If the Statutory Auditor is satisfied that the disclosure made by the Company in the Notes on Accounts is adequate, there is no further need for the Auditor to refer to the revision of the Balance Sheet and/ or the Profit and Loss Account in his report.

Inadequate Disclosure: If the Notes on Accounts do not contain any note on the revision or if such Note is not considered as adequately comprehensive by the Auditor, the Auditor should refer to the fact of revision of the accounts in his report.

The above principles are also applicable to the audit of Government Companies.



REVISION/ RECTIFICATION OF FINANCIAL STATEMENTS

Qualified Report: Where past accounts have been re-opened and revised on technical grounds, and the Company has asked the Auditor to give his report u/s 143 on the revised accounts, he should issue a Qualified Report only.

Format: The Report should indicate that the Company has re-opened the accounts contrary to the opinion of ICAI (CA) The relevant paragraph of the Report may appear as under -

"As per the opinion of the ICAI (CA) a Company cannot re-open and revise the accounts once adopted by the Shareholders at an Annual General Meeting (AGM). However, the Department of Company Affairs vide Circular dated 28.07.1987, has opined that for meeting technical requirements of taxation laws, the accounts can be re-opened. The Board of Directors of the Company, contrary to the aforesaid opinion of the ICAI, has re-opened and revised the aforesaid accounts for adjusting (the matter for meeting the technical requirements of taxation laws regarding which accounts are re-opened may be specified here)."

REVISION OF THE AUDIT REPORT

Revision of Financial Statements: The Auditor should issue a fresh report on the revised Financial Statements in accordance with - (a) Guidance Note on Auditor's Report on Revised Accounts of Companies before circulation to Shareholders, and (b) Guidance Note on Revision/Rectification of Financial Statements.

Revision of Audit Report:

Situations: Revision of Audit Report is required -

When the Auditor considers that amendment in Financial statements is not warranted, or When the Auditor advises amendment to Financial Statements, but the Management does not intend to revise the same, or

When the Management agrees for revision in the Financial Statements but is unable to do so despite its bonafide intention, but Management extends its co-operation to the Auditor and agrees to ensure that anyone in receipt of there previously issued Financial Statements together with the Audit Report thereon is informed of the situation and would be issued the revised Audit Report.

Auditor's Duties: In the above situations, the Auditor should - (i) issue a Revised Report in which he should refer to the earlier report, and (ii) state the reasons for revising the report.

Timing: For corporate entities, the Audit Report may be revised till the accounts are adopted at the AGM. For entities where such adoption is not required, the Auditor may consider revising the Audit Report within a reasonable time, but in any case not later than the issuance of the Audit Report for the immediately succeeding accounting period.



Subsequent Financial Statements: A Continuing Auditor may consider that the revision of Financial Statements and issuance of a Revised Report is not necessary if appropriate disclosures are made in the Financial Statements of the immediately succeeding accounting period.

Preventing Reliance on Earlier Report:

If the management neither agrees to revise the Financial Statements nor agrees to circulate the proposed Revised Audit Report to the recipients of the earlier report, the Auditor should notify the persons ultimately responsible for the overall direction of the entity that action will be taken by him to prevent reliance on the Audit Report.

The Auditor may take the following steps in this regard -

Notify the client that the Audit Report must no longer be associated with the Financial Statements.

Notify the regulatory agencies (ROC / Income Tax Department / SERI / RBI / IRDA etc.) having jurisdiction over the client that the Audit Report should be no longer be relied upon. Make an appropriate statement at the AGM, if requested by the Chairman.

Withdrawal from Engagement: When the Management neither agrees to revise the Financial Statements nor agrees to ensure that anyone in receipt of the previously issued Financial Statements and Audit Report thereon will be informed of the situation and would be issued Devised Audit Report, the Auditor may conclude that withdrawal from the further engagement with the entity is necessary.

Signature: Where a Firm is the Auditor, the Partner who signed the Original Audit Report, should also sign the Revised Report or the letter indicating preventing reliance on the Audit Report, as the case may be. In case of signing by any other Partner, the reasons thereof should be stated.

AUDIT OF ABRIDGED FINANCIAL STATEMENT

Legal Requirements: The Auditor should examine whether the requirements relating to Abridged Balance Sheet and Abridged Profit & Loss Account as laid down in Section 136 have been duly complied with.

Subsequent Events: If the Audit Report on Abridged Financial Statements is issued on a date subsequent to the issuance of the Audit Report on Annual Accounts as per Schedule III, the Auditor's responsibility in relation to events occurring after the Balance Sheet date is limited to the events occurring up to the date of his report on the annual accounts.

Unqualified Report: If the Auditor is satisfied that the Abridged Financial Statements are proper in all respects, he should issue an Unqualified Audit Report.

Qualified Report: The Auditor should express a Qualified Opinion or an Adverse Opinion, as appropriate, if he has certain reservations about the Abridged Financial Statements, e.g. if a material piece of information has not been disclosed in the Abridged Financial Statements or has been disclosed in an inappropriate manner.



PROVISION FOR PROPOSED DIVIDEND

When a Company does not provide for an amount for Proposed Dividend, the attention of Shareholders should be drawn to the fact that no appropriation has been made.

The fact that provision for Proposed Dividend has not been made should be disclosed by means of a Note in the Accounts.

The Auditor should refer to the Note in his Report and make his Report subject thereto.

ACCOUNTS OF LIQUIDATORS / REPORT U/S 348 OF COMPANIES ACT, 2013

Skills: The professional skill and audit procedures to be applied for an audit u/s 348 are similar to that used during a normal audit of a Company.

Report: There should be a fair measure of uniformity in the Reports submitted by Auditors conducting an audit u/s 348 of the Companies Act, 2013. The Auditor's Report may be on the following lines -

Whether he has obtained all the information and explanations, which to the best of his knowledge and belief, were necessary for the purposes of his audit,

Whether in his opinion, proper books of account as required by the Companies Act, 2013 and Companies (Court) Rules, 1959 have been kept by the Liquidator, so far as appears from his examination of these books,

Whether the Liquidator's Account relating to realisations and disbursements is in agreement with the books and records produced before him,

Whether in his opinion, and to the best of his information and according to the explanations given to him, the Liquidator's Account including Annexures give the information required by the Companies Act, 2013, and the Companies (Court) Rules, 1959 in the manner so required and give a true and correct view of the realisations and disbursements of the Liquidator.

SECTION 182 OF THE COMPANIES ACT AND THE AUDITOR

Conditions for contribution to Political Party / Political Purpose:

The Board should pass a resolution authorizing such contribution.



The aggregate of the amount contributed in any financial year should not exceed 5% of the average net profits during three immediately preceding financial years.

Payments covered under Political Contribution:

Contribution made directly to a Political Party whether in cash or in other form.

Expenditure incurred on printing and distribution of posters and leaflets, either directly concerned or connected with elections or otherwise for a political purpose.

Contribution made directly to a political party whether in cash or in other form for running an educational institution or for undertaking philanthropic activities.

Donation, Contribution, or other form of support to a Trust, Society or Association in any of the under noted circumstances -

If the Trust, Society, or Association has any political objectives either wholly or even partially. If the Trust, Society, or Association is formed for any political purpose either wholly or even partially.

If the Trustees or Governing Council or Committee of the Trust, Society, Association have the discretion of using the funds wholly or partially for a political purpose or in furtherance of a political objective. On the other hand, the mere fact that some of the objects of a particular Trust, Society, or Association are similar to the objects of a particular political party but are not of a political nature should not act as disqualification.

Expenditure incurred on remuneration (including other benefits) to employees or on other establishment where the services of the employees are made available in connection with the activities of some political party, such as elections to Legislative Assembly, Parliament etc.

Making available vehicles owned by the Company to any political party or to any candidate seeking election to any local authority, assembly, Parliament, etc. either free of cost, or at less than market rate.

Expenditure incurred directly or indirectly by a Company on advertisement in any publication like Souvenir, Brochure, Tract, etc by or on behalf of a Political Party or for its advantage.

Donation, Subscription or payment by a Company to any person which can be regarded as likely to affect public support for a Political Party shall be deemed as contribution for a political purpose.

Disclosure: Every Company should disclose in its P&L Account, the amount contributed by it during the financial year to any political party or for any political purpose, giving the particulars of the name of the recipient party or person.



Auditor's Duties:

The Auditor should qualify his Audit Report under the following circumstances, if he is satisfied - that the political contribution has been made in excess of the limit prescribed. (He should also indicate the amount involved.) that facts regarding such contributions are not properly disclosed.

If the Auditor is in doubt about applicability of Section 182, he should disclose this fact in his report.

The Auditor should obtain a certificate from the Board stating the following

That all amounts of contributions to Political Parties have been properly recorded;

No amounts of such nature other than those so included in the books have been paid / given directly or indirectly.

The Auditor need not make any special inquiry to unearth cases of unauthorized political contributions if they are not readily apparent from the examination of the accounts made in the normal course of audit.

Where the Auditor fails to discover cases of contraventions of Section 182, he would be responsible only to the extent it can be established that in the conduct of the audit he acted without reasonable care and skill.

AUDIT OF CONSOLIDATED FINANCIAL STATEMENTS (CFS)

Parent Company: The Parent Company (i.e. Holding Company) has the following responsibilities -

- (a) Identifying components, and including the financial information of the components to be included in the Consolidated Financial Statements,
- (b) Identifying reportable segments for segmental reporting,
- (c) Identifying related parties and related party transactions for reporting,
- (d) Obtaining accurate and complete financial information from components, and
- (e) Making appropriate consolidation adjustments.

Objective of Audit of CFS:

To satisfy that the CFS have been prepared as per the requirements of Ind AS - 27, 18 & 31.

To enable the Auditor to express an opinion on the true and fair view presented by the CFS (Consolidated Financial Statement).

Features of CFS:

CFS are prepared using the Separate Financial Statements of the Parent, Subsidiaries, Associates and Joint Ventures and also other financial information, which might not be covered by the Separate Financial Statements of these entities.

The 'other financial information' would include disclosures to be made in the CFS about the Subsidiaries, Associates and joint Ventures, proportion of items included in the CFS to which different accounting policies have been applied, adjustments made for the effects of significant transactions or other events that occur between the Financial Statements of Subsidiaries, Associates or Joint Ventures and the Parent, as the case may be, etc.

The Auditor of the CFS has to use the work of other Auditors i.e. the Auditor of Financial Statements of the components, as required under SA 600.

Verification Procedures:

Aspect	Auditors' Duties
Completeness	<p>To ensure that all relevant Subsidiaries, Associates and Joint Ventures (JVs) have been included, the Auditor should review the following -</p> <ul style="list-style-type: none"> • His working papers for the prior years for known Subsidiaries, Associates and JVs, • Parent's procedures for identification of Subsidiaries, Associates and JVs, • Investments made, to determine the shareholding in other entities, • Joint Ventures and other relevant agreements entered into by the Parent, • Statutory records maintained by the Parent, e.g. Registers u/s 190 / 186.
Control	<p>Since control of the composition of the Board of Directors/ Governing Body of an enterprise also results in a Parent-Subsidiary Relationship, the Auditor should examine the minutes of Board Meetings, Shareholder Agreements with entities to which technology or know-how might have been provided, etc.</p>
Exclusion	<ul style="list-style-type: none"> • Where a Subsidiary'/ Associate /Jointly Controlled Entity is excluded from the CFS, the Auditor should examine the reasons for the exclusion. • If it is argued that the reason for exclusion from consolidation is that the relationship of the entity with the Parent is temporary, the Auditor should examine whether the Parent had the intention to dispose of its interest at the time of making the investment.
Others	<p>The Auditor should -</p> <ul style="list-style-type: none"> • Examine the relevant law and agreements to identify long-term restrictions prohibiting transfer of funds. • Review whether the procedures and disclosure requirements laid down by the relevant AS have been followed, in preparing the CFS. • Verify that the gross amounts of Goodwill and Capital Reserve have also been disclosed, if such Goodwill arising in respect of one Subsidiary is set-off against Capital Reserve arising in respect of another. • See whether any impairment loss exists in respect of Goodwill arising on consolidation.



Permanent Consolidation Adjustments: The Auditor should see whether the following adjustments have been made appropriately –

Capital Reserve / Goodwill: Determination of excess / deficit of the cost to the Parent of its investment in a Subsidiary over the Parent's portion of Equity of the Subsidiary, at the date on which investment in the Subsidiary is made (determination of Goodwill or Capital Reserve).

Minority Interest: Determination of the amount of equity attributable to minorities at the date on which investment in Subsidiary is made.

Associates: Determination of Goodwill or Capital Reserve arising on application of Equity Method to account for investments in Associates in CFS.

Other Verification: The Auditor should review the Memorandum Records to verify the adjustments entries made in the preparation of CFS including the following -

- Intra-group interest paid and received, or management fees, etc.
- Unrealised intra-group profits on assets acquired from other Subsidiaries.
- Intra-group indebtedness.
- Adjustments related to harmonising the different accounting policies being followed by the Parent enterprise and its Subsidiaries.
- Adjustments made for the effects of significant transactions or other events that occur between the date of the Financial Statements of the Parent and one or more of the components, if the Financial Statements to be used for consolidation are not drawn up to the same reporting date; and
- Determination of movement in equity attributable to the minorities since the date of acquisition of the Subsidiary.

AUDIT CERTIFICATE

Sometimes apart from an audit report for general use, an auditor is often called upon to give a certificate for special purpose. The certificate should include the following: —

- Auditor should see that there is a suitable declaration by the management about the subject matter.
- Auditor should give the certificate on his letter head or on stationary carrying his name and address to avoid misunderstanding.



- Auditor should clearly state his limitations and indicate the extent to which he has relied upon a technical expert if any.
- Auditor should indicate the specific record covered by the certificate.
- Auditor should mention the manner in which the audit was conducted.
- Auditor should indicate in the certificate if he has made certain fundamental assumptions. Auditor should make a reference to the information and explanations obtained. Auditor should give clear title to it, indicating whether it is a report or a certificate.
- Auditor should mention whether he has used any general purpose statement like Profit & Loss Account for his investigation and also, state whether that general purpose statement has been audited by other auditors.
- Auditor should be careful while interpreting any law related matter, he should clearly mention that he is expressing merely his own opinion.
- Auditor should see that the certificate should be self contained documents. Auditor should clearly mention the responsibility assumed by him.
- Auditor should, if he has referred the audited statements, clearly mention that the figures are used from the audited statements and relied upon.
- Auditor should address the certificate to the client or the Public Authority or the person requiring it as the case may be. In appropriate circumstances it may be issued by using the words as "to whom so ever it may concern".

Examples and Specimens of Auditor Certificates —

There are many more circumstance, where for, auditor is called for issuing a certificate, e.g.,

"Deposits Return" Certificate.

"Ability to Refund Depositors" Certificate.

Deposits Return Certificate: As provided under rule 10(1) of the Companies (Acceptance of Deposits), Rules, a non banking, non financial company has to file periodical return in prescribed form containing the information about deposits accepted and the copy of the return is required to be filed with the R.B.I. (Reserve Bank of India). This return is to be certified by the Company Auditor.



The specimen of the Certificate may be as under:

CERTIFICATE

We certify that to the best of our knowledge and according to the information and explanation given to us and as shown by the records examined by us, the figures of deposits and interest rates under parts A, B and C of the return of the Co. Ltd. are correct.

We further certify the correctness of the particulars of the paid up capital and free reserves etc. given in the manager's certificate.

Date: _____ Signature & Seal of
Chartered Accountant /Cost Accountant

Place: _____ Full Address

Ability to Refund Deposits Certificate: As per the provisions of the Non Banking Financial Companies(Reserve Bank)Directions, issued from time to time every non banking financial company is required to furnish to the RBI a certificate from its auditor to the effect that, the full liabilities to the depositor of the company including interest are properly reflected in the Balance Sheet and that the company is in a position to meet the amount of such liability to the depositors. As prescribed by the RBI, the certificate shall be in following format—

CERTIFICATE

We certify that, on the basis of the checks carried out by us and the information and explanations given to us I am of the opinion that full liabilities to the depositors of the company including interest payable thereon have been reflected in the financial statements as on 31st March of the company, as per the said financial statements and on a going concern basis and based on information and explanation given to me, is in a position to meet the liabilities to the depositors, as on that date.

Also, an auditor is required to give certificate under various provisions of the Companies Act 2013, for example, u/s 26 for matters in the prospectus, U/s 73 for public deposits, etc.

In short, Audit Certificate is a written confirmation of the accuracy of the information stated therein but does not involve any opinion.

Date: _____ Signature & Seal of
Chartered Accountant /Cost Accountant

Place: _____ Full Address

Difference between Audit Report and Audit Certificate

Sl. No.	Basis	Audit Report	Audit Certificate
	Meaning	Audit Report is a statement of collected and considered information so as to give a clear picture of the state of affairs of the business to the persons who are not in possession of the full facts.	While Audit Certificate is a written confirmation of the accuracy of the information stated there in.
	Opinion	Audit Report contains the opinion of the auditor on the accounts	while Audit Certificate does not contain any opinion but only confirms the accuracy of the figures with the books of accounts.
	Basis	Audit Report is made out on the basis of information obtained & books of account verified by the auditor,	while Audit Certificate is made out on the basis of the particular data capable of verification as regards accuracy.
	Guarantee	Audit Report may not guarantee correctness of financial statement in absolute terms	While Audit Certificate guarantees absolute correctness of the figures & information mentioned in the certificate.
	Coverage	Audit Report always covers entire accounts of the concern,	While Audit Certificate covers only certain part of the accounts of the concern.
	Responsibility	Audit Report does not hold auditor responsible for anything wrong in the accounts,	While Audit Certificate makes an auditor responsible if anything mentioned in the certificate found as wrong later on.
	Suggestion	Audit Report may provide certain suggestions for improvement	While Audit certificate does not provide any such suggestion.
	Nature	Audit Report is based on the vouching & verification of books of accounts, voucher, assets & liabilities,	while Audit Certificate is based on checking arithmetical accuracy of the facts.
	Scope	Audit Report covers all transactions done during the year,	while the Audit Certificate is very specific.
	Characteristics	Audit Report is subjective as it is opinion oriented,	while Audit certificate is objective as it is fact oriented.
	Form	Audit Report is required to be presented in the prescribed format,	while Audit Certificate, except in few cases, is not required to be presented in any standard format.
	Address	Audit report is addressed to the members of the company at large or appointing authority,	while Audit Certificate is addressed to particular person or sometimes may include the words like "To Whomsoever it may concern".



Self Examination Questions:

1. Describe the procedure of submission of Cost Audit report by the Auditor of the Company.
2. Distinguish between the followings
3. Qualified Report and Adverse Report
4. Explanatory Notes and Qualificatory Notes
5. Write short notes on signing the Audit Report.
6. Write short notes on Qualification of Company Auditor under section 141 of the Companies Act 2013.
7. Explain the matters that do and do not affect the auditor's opinion.
8. What do you mean by Qualified Audit Report and Piecemeal Opinion?
9. What consideration should an auditor bear in mind when he is drafting a certificate for a special purpose? Discuss the scope and contents of such reports.
10. What are the various types of opinion that an auditor can express as a result of his audit? Under what circumstances should an auditor express an adverse opinion or disclaimer of opinion?
11. Explain the nature of verification the auditor should conduct before issuing report or certificate on financial information in offer documents.

State whether the following statements are true or false:

1. SA 700 stands for "Forming an opinion and reporting on Financial Statement".
2. Audit report reflects the work done by the employees.
3. An audit report is addressed to the authority appointing the Auditor.
4. The auditor gives a clean report when he doesn't have any significant reservation in respect of matters contained in the Financial Statements.
5. A disclaimer of opinion is issued by the auditor when he cannot form an overall opinion about the matters contained in the Financial Statements.
6. A piecemeal opinion is issued when whole of the matters contained in the financial statement is true and fair.



7. An adverse report is given when the auditor concludes that based on his examination he does not agree with the affirmations made in the financial report.
8. CARO order 2016 is applicable to the Banking Company.

[Answer: T, F, T, T, T, F, T, F,]

Fill in the blanks:

1. Violation of section 143 (12) imply a fine of R _____
2. A report is statement of _____ & _____ facts.
3. The audit report shall either contain as _____ of regarding financial statements.
4. Audit report is meant for the _____ of the company.
5. Audit report reflects the work done by the _____.
6. The audit report should be signed in the personal name of the _____.

[Answer: 1 Lakh Rupees, Collected and Considered, Expression of opinion, Shareholders, Auditor, Auditor]

Match the following:

	Column A		Column B
1	True and Fair Audit Report	A	Forming an opinion and Reporting on Financial Statements.
2	Audit report with certain reservations	B	Audit Report
3	SA 700	C	Unable to form overall opinion on Financial Statement
4	Negative report	E	One Lakh Rupees.
5	Fine for violation of sec 143 (12)	F	Four times.
6	SA 600	G	Unqualified Opinion.
7	Expression of opinion on Financial Statement	H	Using the work of another Auditor
8	Disclaimer of opinion	I	Does not agree with affirmation made by the management in the books.
9	Scope paragraph	J	Qualified Report.

[Answer: G, J, A, I, E, H, B, C, D]



Multiple choice questions:

1. The meetings of Audit committee should be ____ in a year.
(A)4
(B)5
(C)3
(D)2
2. An audit committee should have ____ directors.
(A)3
(B)2
(C)1
(D)4
3. The _____ shall act as the secretary of the Audit Committee.
(A)Employee
(B)Auditor
(C)Company Secretary
(D)Chairman
4. A nomination and remuneration committee should have ____ directors.
(A)3
(B)2
(C)1
(D)4
5. An audit report is the _____ product of audit.
(A)Main
(B)Final
(C)Semi final
(D)None of the above

[Answer: A, A, C, A, B]

7.4 MISCELLANEOUS AUDIT

BRANCH AUDIT, JOINT AUDIT

"Branch office", in relation to a company, means any establishment described as such by the company - section 2(14) of the 2013 Act.

Audit of Branch Office by company's auditor or branch auditor - Where a company has a branch office, the accounts of that office shall be audited either by the company's auditor (i.e. auditor appointed for the company in AGM) or by any other person qualified for appointment as an auditor of the company under the 2013 Act. Such 'branch auditor' shall be appointed as such under section 139 of the 2013 Act - first part of section 143(8) of the 2013 Act.

Audit of branch offices outside India - Where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country. The duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as may be prescribed second part of section 143(8) of the 2013 Act.

Report by Branch Auditor to company's auditor - The branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the company's auditor. The company's auditor shall deal with the report of branch auditor in his report in such manner as he considers necessary proviso to section 143(8) of the 2013 Act.

Duties and powers of company's auditors in connection with branch audit - Duties and powers of company's auditor (main auditor) with reference audit of branch and branch auditor shall be as contained in section 143(1) to 143(4) of the 2013 Act and Rule 12(1) of Companies (Audit and Auditors) Amendment Rules, 2015. Thus, the company's auditor is responsible even if branch auditor is appointed.

Branch auditor's responsibility to report fraud - Responsibility to report fraud, as applicable to company's auditor applies to branch auditor.

Joint Audit

In big corporate more than one persons or firm of Chartered Accountants are appointed as a Joint Auditor for conducting the audit of the company. This practice of appointing joint auditor accrues great advantages to the company. In a big organisation the task of carrying audit cannot be accomplished with single individual so for overcoming such situation joint auditor wheres appointed.

Advantages of Joint Audit: The various advantages that accrue out of Joint Audit are enumerated below;



- Lower workload
- Timely completion of work
- Sharing of expertise
- Improved quality of services
- Healthy competition
- Quality of performance
- Knowledge pool

Disadvantages of Joint Audit: The disadvantages of Joint Audit are enumerated below;

- Superiority complex of some auditor
- Costly for small entity
- Lack of coordination in work
- Uncertainty about liability of work
- Adjustment / Psychological problem amongst the auditor
- Difficulty in fixation of work among other

SA 299 issued by The Institute of Cost Accountants of India on "Responsibility of Joint Auditor" lay down the responsibilities on joint auditors. The responsibilities of joint auditor's

Normally, the joint auditors are able to arrive at an agreed report. However, where the joint auditors are in disagreement with regard to any matters to be covered by the report, each one of them should express his own opinion through a separate report. A joint auditor is not bound by the views of the majority of the joint auditors regarding matters to be covered in the report and should express his opinion in a separate report in case of a disagreement.

In respect of audit work divided among the joint auditors, each joint auditor is responsible only for the work allocated to him, whether or not he has prepared a separate report on the work performed by him. On the other hand, all the joint auditors are jointly and severally responsible -

- in respect of the audit work which is not divided among the joint auditors and is carried out by all of them;
- in respect of decisions taken by all the joint auditors concerning the nature, timing or extent of the audit procedures to be performed by any of the joint auditors. It may, however, be clarified that all the joint auditors are responsible only in respect of the appropriateness of the decisions concerning the nature,
- timing or extent of the audit procedures agreed upon among them; proper execution of these audit procedures is the separate and specific responsibility of the joint auditor concerned;
- in respect of matters which are brought to the notice of the joint auditors by any one of them and on which there is an agreement among the joint auditors;
- for examining that the financial statements of the entity comply with the disclosure requirements of the relevant statute; and
- for ensuring that the audit report complies with the requirements of the relevant statute.



AUDIT OF SHARE AND DEBENTURES

Allotment of Securities by Company [Section 39]

"Securities" means the securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956.

How to check the allotment of Securities of a Company:

- Study of the contract pursuant to which the issue is made to determine how many shares are agreed to be issued and for what value and the nature and other details of the consideration.
- Examination of the prospectus to see the substance of the contract and the relevant terms of the issue including the mode of payment of the purchase consideration in case of an issue to a vendor of the business or payability of commission to the underwriters or payability of the preliminary expenses.
- To check whether minimum amount has been subscribed or not as stated in the prospectus.
- To check whether the sums payable on application for the amount so stated have been paid to and received by the company by cheque or other instrument.
- To check whether the amount payable on application on every security shall not be less than five per cent. of the nominal amount of the security or such other percentage or amount, as may be specified by the Securities and Exchange Board by making regulations in this behalf.
- Examine the Board meeting minutes for the purpose for which securities is issued and utilized for the same.
- Check whether the amount is refunded to the applicant within prescribed time period in case of minimum amount has not been subscribed and the sum payable on application is not received within a period of thirty days from the date of issue of the prospectus.
- To check whether the company has file with the Registrar a return of allotment or not, where the Company having a share capital makes any allotment of securities.
- To check whether the Company has defaulted under sub-section (3) or sub-section (4). In case the company is found default under above provision then the same should be reported by the auditor in his report.



Alteration of Share Capital [Section 61]

- Confirm that alteration was authorised by articles.
- Verify the minutes of the Board meeting and ordinary resolution passed in the general meeting in which the approval of members is obtained.
- Verify that alteration had been effected in copies of Memorandum, Articles, etc.
- Obtain the reasons for which the memorandum of the company is altered.
- Check whether there is any change in the voting percentage of shareholders due to consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares.
- To confirm that the alter share capital's denomination should be more than R1.
- Verify that proper accounting entries have been passed. Register of members may also be checked to see that the necessary alteration have been effected therein.

Issue of Bonus Shares [Section 63]

- Confirm that issue of Bonus Share was authorized by articles.
- Verify the minutes of the Board meeting and ordinary resolution passed in the general meeting in which the approval of members is obtained.
- Check that the company has issue fully paid-up bonus shares to its members only.
- Confirm that the issue of bonus shares shall not be made by capitalising reserves created by the revaluation of assets.
- Check whether the company has made any default in payment of interest or principal in respect of fixed deposits or debt securities issued by it.
- Check whether the company has made any default in payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus.
- Whether the partly paid-up shares are made fully paid-up.
- Check whether the bonus shares shall not be issued in lieu of dividend.



Power of company to Purchase its Own Securities [Section 68]

- Confirm that Buy-Back was authorized by articles.
- Verify the minutes of the Board meeting and special resolution passed in the general meeting in which the approval of members is obtained.
- Where the buy-back has been authorised by the Board by means of a resolution passed at its meeting then check that the buy-back is not more than ten per cent. or less of the total paid-up equity capital and free reserves of the company.
- Check that the no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.
- To check that the buy-back shall not be more than twenty-five per cent. of the aggregate of paid-up capital and free reserves of the company. In case of buy-back of equity shares in any financial year, the reference to twenty-five per cent. in this clause shall be construed with respect to its total paid-up equity capital in that financial year.
- To check that the ratio of the aggregate of secured and unsecured debts owed by the company after buy-back is not more than twice the paid-up capital and its free reserves.
- To check that all the shares or other specified securities for buy-back should be fully paid-up.
- To check whether the buy-back is made as per SEBI regulations in case of buy-back of the shares or other specified securities listed on any recognized stock exchange.
- To check that no offer of buy-back under this sub-section shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back.
- To ensure that buy-back shall be completed within a period of one year from the date of passing of the special resolution, or as the case may be, the resolution passed by the Board under clause (b) of sub-section (2).
- Ensure that the buy-back has been done only out of the company's free reserves or its securities premium account or out of the proceeds of any shares or other specified securities other than out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.
- Ascertain that declaration of solvency was filed with the SEBI and/or the Registrar of Companies before making buy-back but subsequent the passing of the special resolution.



- To ensure that company shall extinguish and physically destroy the shares or securities so bought back within seven days of the last date of completion of buy-back.
- To ensure that the company shall not make a further issue of the same kind of shares or other securities including allotment of new shares or other specified securities within a period of six months except by way of a bonus issue.
- Whether the company has maintained any register of the shares or securities so bought.
- Check whether that the after the completion of the buy-back under this section the company file with the Registrar and the Securities and Exchange Board a return containing such particulars relating to the buy-back within thirty days of such completion.

Splitting of shares of face value from ₹ 10 to ₹ 1 per share

- Confirm that alteration was authorised by articles.
- Verify the minutes of the Board meeting and ordinary resolution passed in the general meeting in which the approval of members is obtained.
- Verify that alteration had been effected in copies of Memorandum, Articles, etc.
- Verify that proper accounting entries have been passed. Register of members may also be checked to see that the necessary alteration have been effected therein.

Share Transfer Audit:

The following aspects are required to be examined by the auditor in conducting the share transfer audit:

- i. Inspection of the Articles of Association regarding the prescribed form of transfer and other provisions, particularly the time limits laid down by the Articles or law.
- ii. Notification by transferor of the lodgement made by the transferee and inspect the objections received, if any. Also see, where calls due or not paid, whether transfer can be refused under the articles and whether any transfer was so refused.
- iii. Examining in the case of particularly partly-paid shares, where the application for registration was made by the transferor, a notice was sent to the transferee and registration was effected only on receipt of 'non-objection' received from him.



iv. Scrutiny of transfer forms, noting specially:

- That in every case, the application for transfer was made in the prescribed form and the prescribed authority had stamped the date on which it was presented to it; also that it was delivered to the company within 60 days exaction.
 - That each transfer form is properly executed and bears the proper stamp duty.
 - That the name of the company is correctly stated on the form.
 - That where the consideration for transfer appears to be inadequate, an inquiry was made by the company for ascertaining the reasons therefor. (This is not necessary if the transfer form bears the seal of the Collector of Stamps.)
 - That the alterations, if any, have been suitably initiated; and
 - That the name and address of the transferee have been recorded completely and fully for purposes of correspondence.
- (v) Comparison of the signatures of each transferor on the transfer form with his signature on the original application for shares or on the transfer form (if the shares were acquired on a transfer).
- (vi) Ascertaining that none of the transferees is disqualified from holding shares in the company.
- (vi) Vouching the entries in the Shares Transfer Journal by reference to the transfer forms, noting in each case:
- the name of transferor;
 - the name and address of the transferee;
 - the number and class of shares transferred; and
 - the distinctive numbers, if any, of the shares transferred.
- (vii) Verification of postings from the Share Journal to the Register of Members.
- (viii) Inspection of each transfer as to names, addresses, occupations, form of document, description, number (in words), distinctive number of shares, stamp, date, signature, witnesses, etc.



- (ix) Check whether the transfer to firms, etc. have been rejected or not and whether notes of trust has been entered in the share register.
- (x) Noting transferor's name, etc. and class, number and distinctive number of shares, as stated in the transfers, with old certificates and Register of Members. See that old certificates were cancelled.
- (ix) Inspection of the power of attorney and specimen signatures if transfer executed by an agent.
- (x) Inspection of letters of indemnity for lost certificates and ensuring that duplicate certificates have been issued on proper authority.
- (xi) Where part of the shares have been transferred, the issue of balance certificates to the transferors should be seen and confirm that the distinctive number of shares have been correctly stated.
- (xii) Refer to the minutes book to ensure that all transfers recorded in the share transfer journal have been approved by the Board.
- (xiii) Checking of counterfoils of new certificates.
- (xiv) Reconciliation of the amount of transfer fees collected with the total number of transfers lodged and verifying that the amount of transfer fees have been accounted for.
- (xv) Reconciliation of the total number of shares of different classes issued by the company with the total amount of capital issue and its sub-divisions by extracting balances of shares held by different members from the Register of members.
- (xvi) Ensuring that, in case of any share transactions by directors, corresponding entries have been made in the Register of Directors' shareholding.

Re-issue of forfeited shares

- i. The auditor should ascertain that the board of directors has the authority under the Articles of Association of the company to reissue forfeited shares. Check the relevant resolution of the Board of Directors.
- ii. Vouch the amounts collected from persons to whom the shares have been allotted and verify the entries recorded from re-allotment. Auditor should check the total amount received on the shares including received prior to forfeiture, is not less than the par value of shares.
- iii. Verify that computation of surplus amount arising on the reissue of shares credited to Capital Reserve Account and
- iv. Where partly paid shares are forfeited for non-payment of call, and re-issued as fully paid, the reissue is considered as an allotment at a discount and compliance of the provisions of Section 53 is essential.

AUDIT OF DEBENTURES [SECTION 71]

"Debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not;

Issue of Debenture

A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption. Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting. No company shall issue any debentures carrying any voting rights. Secured debentures may be issued by a company subject to such terms and conditions as may be prescribed.

Where debentures are issued by a company under this section, the company shall create a debenture redemption reserve account out of the profits of the company available for payment of dividend and the amount credited to such account shall not be utilised by the company except for the redemption of debentures. Appointment debenture trustee is mandatory for the following –

- The offer of issue of debenture is made to public
- The company makes the offer to members exceeding five hundred in number.

The purpose of appointment of debenture trustee is for the protection of interest & redress grievances of debenture holders.

Now a days, the share accounting is done by Registering and Transfer Agents (RTA)/ The auditor may have to check the records of RTA with dematerialisation and electronic record keeping, the concept of audit has changed.

Auditor's Duty:

- The auditor should verify that the prospectus had been duly filed with the registrar before the date of allotment of debentures.
- He should check the amount collected in the cash book with the counterfoils of receipts issued to the applicants and also cross check the amount into the application and allotment book.
- He should examine the debenture trust deed and note the conditions contained therein as to issue and repayment.
- If the debentures are covered by a mortgage or a charge, it should be verified that the charge has been correctly recorded in the register of mortgage and charges and it has also been registered with the registrar of the companies.
- Compliance with SEBI guidelines should also be ensured.
- Where debentures have been issued as fully paid up to vendors as a part of the purchase consideration, the contract in this regard should be checked.



Interest on Debentures:

A predetermined fixed rate of interest is payable on debentures irrespective of the fact that company has earned the profit or not. Debenture holders are creditors of the company, they are not the owners. They have no voting powers and cannot influence the management but their claim of interest rank ahead of the claims of the shareholders.

Auditor's Duty:

- i. The payment of interest should be vouched by the auditor with the acknowledgement of the debenture-holders, endorsed warrants and in case of bearer debentures with the coupons surrendered.
- ii. The auditor should reconcile the total amount paid with the total amount due and payable with the amount of interest outstanding for payment.
- iii. He should ensure that the interest paid on debenture like that on other fixed loans, must be disclosed as a separate item in the profit & loss account.

Redemption of Debentures:

A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption. If debentures are redeemable it can be redeemed in any of the following way:

- By way of periodical drawing i.e. by creating Debenture Redemption Reserve Account.
- By way of payment on fixed date.
- By payment whenever the company desires to do so.

Auditor's Duty:

- i. The auditor should inspect the debentures or trust deed for the terms and conditions regarding redemption of debentures.
- ii. He should see the Director's minute book authorizing the redemption of debentures.
- iii. He should also vouch the redemption with the help of debenture bonds cancelled and the cash book.
- iv. He should also examine the accounting treatment thoroughly.



Debenture issued as Collateral Security

If the debentures are issued as collateral security to the banks or creditors then auditor needs to ensure that such issue is approved by Board of Directors and very by the term as per loan agreement.

AUDIT OF DIVISIBLE PROFITS & DIVIDENDS

Declaration of dividend [Section 123]

Final dividend is declared in the general meeting. Board of Directors have to recommend a dividend. Declaration of dividend is 'Ordinary Business' in general meeting.

No dividend shall be declared or paid by a company for any financial year except—

- out of the profits of the company for that year arrived at after providing for depreciation in accordance with the provisions of sub-section (2), or out of the profits of the company for any previous financial year or years arrived at after providing for depreciation in accordance with the provisions of that sub-section and remaining undistributed, or out of both; or
- out of money provided by the Central Government or a State Government for the payment of dividend by the company in pursuance of a guarantee given by that Government.

Provided that a company may, before the declaration of any dividend in any financial year, transfer such percent-age of its profits for that financial year as it may consider appropriate to the reserves of the company.

Provided further that where, owing to inadequacy or absence of profits in any financial year, any company proposes to declare dividend out of the accumulated profits earned by it in previous years and transferred by the company to the reserves, such declaration of dividend shall not be made except in accordance with such rules as may be prescribed in this behalf.

Provided also that no dividend shall be declared or paid by a company from its reserves other than free reserves.

Provided also that no company shall declare dividend unless carried over previous losses and depreciation not pro-vided in previous year or years are set off against profit of the company for the current year.

For the purposes of clause (a) of sub-section (1), depreciation shall be provided in accordance with the provisions of Schedule II.



Interim Dividend:

The Board of Directors of a company may declare interim dividend during any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be declared.

Declaration of interim dividend if company has incurred losses in current financial year:

In case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

Legal Provisions applicable to interim dividend:

The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate ac-count within five days from the date of declaration of such dividend.

Entitlement of Dividend:

No dividend shall be paid by a company in respect of any share therein except to the registered shareholder of such share or to his order or to his banker and shall not be payable except in cash.

Provided that nothing in this sub-section shall be deemed to prohibit the capitalisation of profits or reserves of a company for the purpose of issuing fully paid-up bonus shares or paying up any amount for the time being unpaid on any shares held by the members of the company.

Provided further that any dividend payable in cash may be paid by cheque or warrant or in any electronic mode to the shareholder entitled to the payment of the dividend.

Consequences on non-compliance:

A company which fails to comply with the provisions of sections 73 and 74 shall not, so long as such failure continues, declare any dividend on its equity shares.

Unpaid Dividend Account [Section 124] Transfer of unpaid dividend to separate account:

Where a dividend has been declared by a company but has not been paid or claimed within thirty days from the date of the declaration to any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the Unpaid Dividend Account.

Information about unpaid dividend on Company's website:

The company shall, within a period of ninety days of making any transfer of an amount under sub-section (1) to the Unpaid Dividend Account, prepare a statement containing the names, their last known addresses and the unpaid dividend to be paid to each person and place it on the website of the company, if any, and also on any other website approved by the Central Government for this purpose, in such form, manner and other particulars as may be prescribed.

Effect of non-transfer:

If any default is made in transferring the total amount referred to in sub-section (1) or any part thereof to the Unpaid Dividend Account of the company, it shall pay, from the date of such default, interest on so much of the amount as has not been transferred to the said account, at the rate of twelve per cent. per annum and the interest accruing on such amount shall enure to the benefit of the members of the company in proportion to the amount remaining unpaid to them.

Transfer of unclaimed dividend and also shares to Investor Protection Fund:

- Any money transferred to the Unpaid Dividend Account of a company in pursuance of this section which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Fund established under sub-section (1) of section 125 and the company shall send a statement in the prescribed form of the details of such transfer to the authority which administers the said Fund and that authority shall issue a receipt to the company as evidence of such transfer.
- All shares in respect of which dividend has not been paid or claimed for seven consecutive years or more under sub-section (5) shall also be transferred by the company in the name of Investor Education and Protection Fund along with a statement containing such details as may be prescribed.
- Provided that any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with such procedure and on submission of such documents as may be prescribed.
- If a company fails to comply with any of the requirements of this section, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

Investor Education and Protection Fund [Section 125]

The Central Government shall establish a Fund to be called the Investor Education and Protection Fund (herein referred to as the Fund).



There shall be credited to the Fund—

- the amount given by the Central Government by way of grants after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the Fund;
- donations given to the Fund by the Central Government, State Governments, companies or any other institution for the purposes of the Fund;
- the amount in the Unpaid Dividend Account of companies transferred to the Fund under sub-section (5) of section 124;
- the amount in the general revenue account of the Central Government which had been transferred to that account under sub-section (5) of section 205A of the Companies Act, 1956, as it stood immediately before the commencement of the Companies (Amendment) Act, 1999, and remaining unpaid or unclaimed on the commencement of this Act;
- the amount lying in the Investor Education and Protection Fund under section 205C of the Companies Act, 1956;
- the interest or other income received out of investments made from the Fund;
- the amount received under sub-section (4) of section 38;
- the application money received by companies for allotment of any securities and due for refund;
- matured deposits with companies other than banking companies;
- matured debentures with companies;
- interest accrued on the amounts referred to in clauses (h) to (j);
- sale proceeds of fractional shares arising out of issuance of bonus shares, merger and amalgamation for seven or more years;
- redemption amount of preference shares remaining unpaid or unclaimed for seven or more years; and
- such other amount as may be prescribed:

Provided that no such amount referred to in clauses (h) to (j) shall form part of the Fund unless such amount has remained unclaimed and unpaid for a period of seven years from the date it became due for payment.

The Fund shall be utilised for—

- education, awareness and protection;
- the refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money due for refund and interest thereon; promotion of investors'
- distribution of any disgorged amount among eligible and identifiable applicants for shares or debentures, shareholders, debenture-holders or depositors who have suffered losses due to wrong actions by any person, in accordance with the orders made by the Court which had ordered disgorgement;
- reimbursement of legal expenses incurred in pursuing class action suits under sections 37 and 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal; and
- any other purpose incidental thereto, in accordance with such rules as may be prescribed:

Provided that the person whose amounts referred to in clauses (a) to (d) of sub-section (2) of section 205C trans-ferred to Investor Education and Protection Fund, after the expiry of the period of seven years as per provisions of the Companies Act, 1956, shall be entitled to get refund out of the Fund in respect of such claims in accordance with rules made under this section.

Authority to administer the fund:

- The Central Government shall constitute, by notification, an authority for administration of the Fund consisting of a chairperson and such other members, not exceeding seven and a chief executive officer, as the Central Government may appoint.
- Any person claiming to be entitled to the amount referred in sub-section (2) may apply to the authority constituted under sub-section (5) for the payment of the money claimed.

Administration and procedures of the fund:

- i. The manner of administration of the Fund, appointment of chairperson, members and chief executive officer, holding of meetings of the authority shall be in accordance with such rules as may be prescribed.
- ii. The Central Government may provide to the authority such offices, officers, employees and other resources in accordance with such rules as may be prescribed.



- iii. The authority shall administer the Fund and maintain separate accounts and other relevant records in relation to the Fund in such form as may be prescribed after consultation with the Comptroller and Auditor-General of India.
- iv. It shall be competent for the authority constituted under sub-section (5) to spend money out of the Fund for carrying out the objects specified in sub-section (3).

Books of Accounts:

- The accounts of the Fund shall be audited by the Comptroller and Auditor- General of India at such intervals as may be specified by him and such audited accounts together with the audit report thereon shall be forwarded annually by the authority to the Central Government.
- The authority shall prepare in such form and at such time for each financial year as may be prescribed its annual report giving a full account of its activities during the financial year and forward a copy thereof to the Central Government and the Central Government shall cause the annual report and the audit report given by the Comptroller and Auditor-General of India to be laid before each House of Parliament.

STATUTORY AUDITOR VS. INTERNAL AUDITOR

Statutory Audit is the act of checking books of accounts as per the provision of Companies Act, whereas Internal Audit is conducted by the either be a chartered accountant or a cost accountant, or such other professional as may be decided by the Board of the Company to detect weakness in internal control system and for their improvement. However both of these types of audit check books of accounts, detect frauds & errors however they differ from each other which is reproduced below;

SL No.	Basis	Statutory Audit	Internal Audit
i.	Appointing Authority	Statutory Auditor is appointed by the shareholder in the general meeting.	Internal Auditor is appointed by the Board.
ii.	Scope of the work	The scope of work is defined in the Companies Act.	The scope of work includes the adherence of management policies and procedures and indentifies the weakness in the internal control.
iii.	Removal of Auditor	Statutory Auditor can be removed by the shareholders.	Internal Auditor can be removed by the Board.
iv.	Remuneration	It is fixed by the shareholders.	It is fixed by the board.
v	Audit Report	It is submitted to the appointing Authority.	It is submitted to the Board as a suggestion to improve weakness in the internal control.

E. (i) AUDITING AND ASSURANCE STANDARDS RELATING TO AUDIT OF INVENTORIES

Inventories are tangible property held for sale in the ordinary course of business, or in the process of production for such sale, or for consumption in the production of goods or services for sale, including maintenance supplies and consumable stores and spare parts meant for replacement in the normal course. Inventories normally comprise raw materials including components, work-in-process, finished goods including by-products, maintenance supplies, stores and spare parts, and loose tools.

Inventories normally constitute a significant portion of the total assets, particularly in the case of manufacturing and trading entities as well as some service rendering entities. Audit of inventories, therefore, assumes special importance.

The following features of inventories have an impact on the related audit procedures:

- By their very nature, inventories normally turn over rapidly.
- Inventories are susceptible to obsolescence and spoilage. Further, some of the items of inventory may be slow-moving while others may follow a seasonal pattern of movement.
- Inventories are normally movable in nature, although there may be some instances of immovable inventories also, e.g., in the case of an entity dealing in real-estate.
- All the items of inventory may not be located at one place but may be held at different locations such as factories and warehouses, or with third parties such as selling agents.
- The individual items of inventory may not be significant in value, but taken together, they normally constitute a significant proportion of total assets and current assets of manufacturing, trading and certain service entities.
- Physical condition (e.g., stage of completion of work-in-process in certain industries) and existence of certain items of inventories may be difficult to determine.
- Valuation of inventories may involve varying degrees of estimation, including expert opinions, e.g., in the case of jewelry.

(ii) AUDITING AND ASSURANCE STANDARDS RELATING TO AUDIT OF FIXED ASSETS**Introduction**

- i. The term Property, plant and equipment in respect of those entities which are required to comply with the relevant Revised AS refers to such tangible items that:
 - are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and
 - are expected to be used during more than one period.



- ii. An asset can be classified as a PPE or otherwise, depending upon the use to which it is put or intended to be put. For example, assets which are classified as PPE in one type of business may be considered as current assets in another. Similarly, the same asset may be classified differently in an entity at different points of time. The recognition of Property, Plant and Equipment should be done as per the principles laid down in the "relevant applicable AS".

EDUCATION INSTITUTION

The special steps involved in the audit of an educational institution are the following:

- Examine the Trust Deed, or Regulations in the case of school or college and note all the provisions affecting accounts. In the case of a university, refer to the Act of Legislature and the Regulations framed thereunder.
- Read through the minutes of the meetings of the Managing Committee or Governing Body, noting resolutions affecting accounts to see that these have been duly complied with, specially the decisions as regards the operation of bank accounts and sanctioning of expenditure.
- Check names entered in the Students' Fee Register for each month or term, with the respective class registers, showing names of students on rolls and test amount of fees charged; and verify that there operates a system of internal check which ensures that demands against the students are properly raised.
- Check fees received by comparing counterfoils of receipts granted with entries in the cash book and tracing the collections in the Fee Register to confirm that the revenue from this source has been duly accounted for.
- Total up the various columns of the Fees Register for each month or term to ascertain that fees paid in advance have been carried forward and the arrears that are irrecoverable have been written off under the sanction of an appropriate authority.
- Check admission fees with admission slips signed by the head of the institution and confirm that the amount had been credited to a Capital Fund, unless the Managing Committee has taken a decision to the contrary.
- See that free studentship and concessions have been granted by a person authorised to do so, having regard to the prescribed Rules.
- Confirm that fines for late payment or absence, etc., have either been collected or remitted under proper authority.
- Confirm that hostel dues were recovered before students' accounts were closed and their deposits of caution money refunded.
- Verify rental income from landed property with the rent rolls, etc.



- Vouch income from endowments and legacies, as well as interest and dividends from investment; also inspect the securities in respect of investments held.
- Verify any Government or local authority grant with the relevant papers of grant. If any expense has been disallowed for purposes of grant, ascertain the reasons and compliance thereof.
- Report any old heavy arrears on account of fees, dormitory rents, etc., to the Managing Committee.
- Confirm that caution money and other deposits paid by students on admission have been shown as liability in the balance sheet and not transferred to revenue.
- See that the investments representing endowment funds for prizes are kept separate and any income in excess of the prizes has been accumulated and invested along with the corpus.
- Verify that the Provident Fund money of the staff has been invested in appropriate securities.
- Vouch donations, if any, with the list published with the annual report. If some donations were meant for any specific purpose, see that the money was utilised for the purpose.
- Vouch all capital expenditure in the usual way and verify the same with the sanction for the Committee as contained in the minute book.
- Vouch in the usual manner all establishment expenses and enquire into any unduly heavy expenditure under any head.
- See that increase in the salaries of the staff have been sanctioned and minuted by the Committee.
- Ascertain that the system ordering inspection on receipt and issue of provisions, foodstuffs, clothing and other equipment is efficient and all bills are duly authorised and passed before payment.
- Verify the inventories of furniture, stationery, clothing, provision and all equipment, etc. These should be checked by reference to Stock Register and values applied to various items should be test checked.
- Confirm that the refund of taxes deducted from the income from investment (interest on securities, etc.) has been claimed and recovered since the institutions are generally exempted from the payment of income-tax.
- Verify the annual statements of accounts and while doing so see that separate statements of account have been prepared as regards Poor Boys Fund, Games Fund, Hostel and Provident Fund of Staff, etc.



AUDIT OF HOSPITAL

The following points are to be considered necessary for conducting an audit of Hospital.

- Check the letter of appointment to ascertain the scope of responsibilities.
- Study the Charter or Trust Deed under which the hospital has been set up and take a special note of the provisions affecting the accounts.
- Examine, evaluate and verify the system of internal check, internal control and determine the nature, timing and the extent of the audit procedures.
- Vouch the entries in the Patient's Bill Register with a copies of bill issued. Test check the selected bills to see that these have been correctly prepared taking into consideration the period of stay of each patient as recorded in the Attendance Schedule.
- Vouch the collection from patients with copies of bills and entries in Bills Register. Arrears of dues should be properly carried forward and where these are deemed to be irrecoverable, they should be written off under due authorizations.
- Interest and/ or dividend income should be vouched with reference to the Investment Register and Interest and Dividend warrants.
- In case of legacies and donations which are received for specific purposes, it should be ensured that any income therefrom is not utilized for any other purposes.
- Where receipts of subscription show a significant deviations from budgeted figures, it should be thoroughly inquired into and the matter be brought to the notice of the trustees or the Managing Committee.
- Government grants or grants from local bodies should be verifies with the reference to the correspondence with the concerned authorities.
- Clear distinction should be made between the items of capital and revenue nature.
- The capital expenditure should be incurred under proper authorization by a valid resolution of the trustees or the Managing Committee.
- Verify the system of internal check as regards purchases and issue of stores, medicines etc.
- Examine that the appointment of the staff, payment of salaries etc. are duly authorized.
- Physically verify the investments, fixed assets and inventories.
- Check that adequate depreciation has been provided on all the depreciable assets.



CO- OPERATIVE SOCIETIES

Definition: A Co-operative society may broadly be defined as an association of persons who have voluntarily joined together to achieve a common economic objective through the formation of a democratically-controlled business organization, making equitable contributions to the capital as required, and accepting a fair share of risks and benefits of the undertaking. Elimination of middlemen and sharing of gains of economic activities seems to be the hallmark of a co-operative society.

A co-operative society may be formed for different purposes. Accordingly, there may be consumers' co-operative societies, housing co-operative societies, industrial co-operative societies, urban and rural co-operative banks, etc.

Audit as per Section 17 of the Co-Operative Societies Act, 1912

- The Registrar shall audit or cause to be audited by some person authorised by him by general or special order in writing in this behalf the accounts of every registered society once at least in every year.
- The audit under sub-section (1) shall include an examination of overdue debts, if any, and a valuation of the assets and liabilities of the society.
- The Registrar, the Collector or any person authorised by general or special order in writing in this behalf by the Registrar shall at all times have access to all the books, accounts, papers and securities of a society, and every officer of the society shall furnish such information in regard to the transactions and working of the society as the person making such inspection may require.
- "Registrar" means a person appointed to perform the duties of a Registrar of Co operative Societies under this Act.

The following points should be kept in mind where awains of an Co-operative society;

- Qualifications of auditor: generally, only a chartered accountant within the meaning of the Chartered Accountants Act 1949, can be appointed as the auditor of a co-operative society. However, in certain State Co-operative societies Act, a person holding a government diploma in co-operative accounts, or in co-operation and accounts, or a reason who has served as an auditor in the Co-operative Department of Government, may also be appointed as the auditor.

The auditor should ensure that he is duly qualified to act as auditor of the society.

Appointment of the Auditor: An auditor of a co-operative society is appointed by the Registrar of Co-operative Societies-and the auditor so appointed conducts the audit on behalf of the Registrar and submits his report to him as also to the society. The audit fees are paid by the society on the basis of statutory scale of fees prescribed by the Registrar, according to the category of the society audited. For example, the audit fees of co-operative credit society and Urban Co-operative Banks are to be calculated with reference to working capital at the prescribed rates. 'Working Capital' here means funds at the disposal of the society inclusive of paid up share capital, funds built up out of profits and monies raised by borrowing and by other means.



Books of accounting records: Under section 43(h) of the Co-operative Societies Act, a state government can frame rules prescribing the books and accounts to be kept by a co-operative society.

For example In Maharashtra the co-operative societies are required to maintain cash book, general ledger, personal ledger, stock register, property register, etc.

Cash book. It may be maintained to record particulars regarding cash receipts and expenses under suitable heads, with clear distinction between capital and revenue items of receipts and expenses.

Stock register. It may contain detailed information as regards receipts, issues and balances of stock-in-trade, date-wise. In a producers' co-operative society, perpetual inventory records may be maintained based on an appropriate costing method.

Register of assets and investments. It will contain detailed particulars regarding the various immovable and movable assets belonging to the society, such as, types of assets, location, date of acquisition, cost, depreciation provided, and so on.

Register of fixed deposits. In the case of a co-operative credit society, or a co-operative bank, or any other society which is authorised by its bye-laws to accept deposits from members/non-members, a register of fixed deposits may be maintained giving details as regards the dates of acceptance, maturity, interest accrual, repayment, etc.

Register of sureties. In the case of a co-operative credit society, loans are given against personal security of members as also surety (guarantee) provided by two other members. The Register of Sureties will give particulars about the number of borrowers in respect of which a member has stood surety, and show whether it is within the overall limit of surety-ship that may.

Restriction on shareholding: Shareholding in a co-operative society is subject to the limit prescribed in Sec. 5 of the Co-operative Societies Act 1912. Accordingly, no member of the society, other than a registered society, can hold more than twenty per cent of the total number of shares of the society, or such number of shares which in value exceeds Rs. 1,000. A co-operative society cannot prescribe any other limit in its bye-laws which is violative of this provision. In addition to this, the Acts passed by the states may also passed by the States may also prescribe other restrictions as regards shareholding.

The auditor should see that the provision regarding shareholding is duly followed.

Restriction on Loan: As per section 29 A registered co-operative society can only grant loans to its members though, with prior approval of the Registrar, it may grant loans to other registered co-operative societies. The auditor should see that the loans granted by the society are in conformity with this provision.

Restriction on Borrowing: Subject to the restrictions imposed by its bye-laws, a co-operative society may accept loans and deposits from its members as well as non-members. It is the, auditor's duty to ascertain that the restrictions, if any, laid down by the bye-laws are carefully observed



Investment of Funds: There are restrictions on investment of funds belonging to a co-operative society. Accordingly, a society may invest its funds in any of the following (Sec.32 of the Central Co-operative Societies Act):

- Central or State Co-operative Bank,
- Any securities specified in Section 20 of the Indian Trusts Act, 1882.
- Any shares, securities, bonds or debentures of any other Co-operative society with limited liability.
- Any bank, or person carrying on banking business or a Co- operative bank, other than a Central or State co-operative bank, as duly approved by the Registrar;
- In any other manners as duly permitted by the requisite authority.

Auditor's duty: The auditor should ascertain whether the requirement as to investment of the society funds are being observed.

Appropriation of profits: According to the Central Co-operatives Societies Act, 25% of the profits of a co-operatives society should be transferred to a Reserve Fund before distribution of dividend or payment of bonus to its members. However, the Registrar may, having regard to the financial position of the society, reduce the percentage of profits to be transferred to the Reserve Fund. But in any case, he cannot reduce it to less than 10% of the profits of the society.

Apart from the above mandatory provision, a co-operative society may, subject to the provisions of its bye-laws, appropriate its profits by way of transfer to other reserves, distribution of dividends to members, etc. However, appropriation of profits must be duly approved by the members of the society in the general meeting called for the purpose.

Contributions to charitable Purposes: According to Section 34, a registered society may, with the sanction of the Registrar, contribute an amount not exceeding 10% of the net profits remaining after the compulsory transfer to the reserve fund for any charitable purpose as defined in section 2 of the Charitable Endowments Act, 1890.

SPECIAL POINTS IN A CO-OPERATIVE SOCIETY

General Points: - In general while conducting audit of Co-operative society 'The auditor need to look into the followings: -

- The auditor should carefully go through the bye-laws of the society and see that they are being observed both in letter and spirit.
- He should examine the Register of Members of the society and individual shareholdings.
- He should test-check the internal check and control system operated by the society and model his audit examination based on its strengths and weaknesses.



Audit of income: He should carefully vouch the receipt of cash. Cash receipts on account of share capital should be vouched with the Register of Members. Cash received against sales should be vouched with the cash memos and invoices issued to customers as also Sales Account. Receipt of cash in respect of payment of interest and repayment of loans advanced by the society should be vouched with the loan agreements. Cash received from members towards construction of houses or their maintenance, should be vouched with the Register of Members, demands made by the society from time to time, and money receipts.

Audit of Expenditure:

- He should vouch all expenditure with reference to authorisation from the Managing Committee, particularly in the case of large capital expenditure, as also the bills received from individual parties, the money receipts obtained from them, and entries in the Bank Pass Book along with counter-foils of cheques.
- He should vouch the payment of loans from the loan agreements entered into with borrower-members.
- He should vouch establishment expenses with reference to the resolutions of the Managing Committee, agreements with the persons concerned, and money receipts obtained from them.

Other aspects points:

- He should appropriately classify overdue debts for a period from six months to five years and more, and report them to the members, with a note regarding the effects these might have on the financial position of the society. He should also put a note regarding the probability of recovery of such debts.
- Similarly, he should make a special reference to the overdue amount of interest from members. Generally, interest on overdue debts should not be credited to Interest Account but to the Overdue Interest Reserve Account.
- Writing off of bad debts should be after prior authorisation from the Managing Committee of the society. According to the Maharashtra Co-operative Societies Rules, a bad debt can be written off only when it is certified to be irrecoverable by the auditor. This casts a special obligation on the auditor to ascertain whether the debt in question was created within the Rules of the society, and whether it has now really become bad and irrecoverable.

BANK AUDIT

Introduction:

The banking industry is the pivot of any economy and its financial system. Banks are one of the foremost agents of financial intermediation in an economy like India and, therefore, development of a strong banking system is of utmost importance. The banking institutions in the country are working in a competitive environment and their regulatory framework is aligned with the international best practices. Thus, financial deepening has taken place in India and continues to be in progress with a focus on orderly conditions in financial markets while sustaining the growth momentum.

The Reserve Bank of India (hereinafter referred to as RBI) acts as the monetary authority and the central bank of the country.

Type of Banking institutions prevailing in India:

- Commercial banks;
- Regional Rural banks;
- Co-operative banks;
- Development banks (more commonly known as 'term-lending institutions');
- Payment Banks; and
- Small Finance Banks

Financial Statements of a bank

As per the Third Schedule to the Banking Regulation Act, 1949, the Balance Sheet of a Bank should be presented in the following manner, with comparative figures for previous financial year –

Balance Sheet (Form A)	Schedule	P & L Account (Form B)	Schedule
Capital and Liabilities:		I. Income:	
Capital	1	Interest Earned	13
Reserves and Surplus	2	Other Income	14
Deposits	3		
borrowings	4		
Other Liabilities & Provisions	5		
Total		Total	
		II. Expenditure:	
		Interest Expended	15
		Operating Expenses	16
		Provisions & Contingencies	
		Total	
Assets:		III. Profit / Loss:	
Cash & Balances with RBI	6	Net Profit / (Loss) for the year Profit /	
Balances with Banks & Money at Call	7	(Loss) brought	
& Short Notice		forward	
Investments	8		
		Total	
Advances	9	IV. Appropriations:	
Fixed Assets	10	Transfer to Statutory Reserves	
Other Assets	11	Transfer to Other Reserves	
		Transfer to Government / Proposed	
		Dividend	
		Balance carried over to Balance	
		Sheet	
Total		Total	

Auditing aspects of banking of financial Statement.



Advances: In relation advances made by bank an auditor need to review the followings:

- Ensure the internal control is in place in relation to advances made.
- To scrutinise the subsidiary, ledger, & control accounts
- To ensure the proper documentation of account.
- To scrutinising the overdue account and scheme for recovery of such amount.
- Cash balance with RBI and other bank and money at call and short Notice.

Cash in hand:

- Ensure that the Internal control is in place.
- Visit the bank branch and inspects physical cash and ensure that it will tallies with the banks cash book balance.
- To verify the amount of foreign currency held by bank and its translation at make rate on the date at which financial statement is prepared.

Balance with RBI:

- Inspect the ledger balance in each account with (a) bank confirmation certificates from Reserve Bank of India and (b) Reconciliation Statement.

Balance with other bank:

Inspection of reconciliation statement to ensure that no debit or credit for interest have been taken to Revenue account to the year. To examines the large transition and balances with banks outside India. Ensure that they are converted at market rate as on financial statement preparation

Money at call & short notice:

- Examines the system of authorisation for unding money at short and call notice
- The call loan made by bank are not nettled off against call loan received by it.
- Ensure that money market lending's for more than 6th days are not classified under this head but as a deposit or advance based on their nature of learning.

Fixed and other Assets: -



The auditor has to ensure the following while audit of F .A (Fixed Assets) held by banks

- Accounting method of bank
- Ownership document
- To examine with reference to schedule of fixed assets to find neew assets acquired.
- To examise sale deed in relation to sale of assets by bank.
- To ensure appropriateness of basis of revaluation of fixed assets.
- Ensure compliance of sec 9 of banking Regulation Act.

Banking and Deposits:

Barrowings:

- To ensure that amount have been property disclosed for
- Barrowing in India farm RBI.
- Barrowing outside India.
- Ensure the rate of interest paid payable with duration of borrowing.
- Verity whether the barrowings of maney at call and short notice are property authorized.

Deposits: -

- To ensure the interest accered but not due on deposits is not under other liabilities and provision
- See Whether there is any instances of window dressing reporting in LFAR.

Capital Reserve and Surplus:

Capital:

- Examine the opening balance of capital
- Examine with special resolution of shareholder or MOA about increase in authorized capital durig the year.



- Examine with prospectus about increase in subscribed/ paid up capital
- Examine with Government notification for any fresh contribution from them.

Reserve and Surplus:

To examine the opening balance of different type of Reserve.

- Addition/ deduction from reserves.
- Reason for appropriation of any fund from such account.
- Dividend paid by bank
- In respect of foreign branch ensure compliance with foreign laws.

Other Liabilities and provision:

The auditor may verify the various items under the head "other liabilities and provisions" in the following manner.

Bills Payable

The auditor should evaluate the existence, effectiveness and continuity of internal controls over bills payable. Such controls should usually include the following:

- Drafts, mail transfers, traveller's cheques, etc., should be made out in standard printed forms.
- Unused forms relating to drafts, traveller's cheques, etc., should be kept under the custody of a responsible officer.
- The bank should have a reliable private code known only to the responsible officers of its branches coding and decoding of the telegrams should be done only by such officers.
- The signatures on a demand draft should be checked by an officer with the specimen signature book.
- All the telegraphic transfers and demand drafts issued by a branch should be immediately confirmed by advices to the branches concerned. On payment of these instruments, the paying branch should send a debit advice to the originating branch.
- If the paying branch does not receive proper confirmation of any telegraphic transfers or demand draft from the issuing branch, it should take immediate steps to ascertain the reasons.
- In case an instrument prepared on a security paper, e.g., draft, has to be cancelled (say, due to error in preparation), it should be examined whether the manner of cancellation is such that



the instrument cannot be misused. (For example, in the case of drafts, banks generally cut the distinctive serial number printed on the form and paste it in the book in which drafts issued are entered.) Cases of frequent cancellation and reissuance of drafts, pay orders, etc., should be carefully looked into by a responsible official.

Others (Including Provisions)

It may be noted that the figure of advances and investments in the balance sheet of a bank excludes provisions in respect thereof made to the satisfaction of auditors. The issue of determining the adequacy of provision for doubtful advances is discussed in detail under advances chapter of this Guidance Note. The auditor should examine other provisions and other items of liabilities in the same manner as in the case of other entities. Specifically, in case of tax deducted by the bank and payable to the government authorities before the due date, this function may be centralized or decentralized. While verifying this, the auditor must check whether tax has been correctly deducted from payments as per the provisions of the Income Tax /Act, 1961 and paid on or before the due date as specified under the /Act or Rules therefore. Many a times in case of branch audit, reporting has to be done before the due date of paying tax deducted at source for the month of March. In such cases the auditor should report delays observed till the date of his verification and clearly bring out the fact that he has not verified the payment of tax, due date of which would be after the date of the audit report.

Contingent Liabilities and Bills for Collection:

In respect of contingent liabilities, the auditor is primarily concerned with seeking reasonable assurance that all contingent liabilities are identified and properly valued. To this end, the auditor should, generally follow the audit procedures given below:

- The auditor should verify whether there exists a system whereby the non fund based facilities to parties are extended only to their regular constituents, etc.
- Ascertain whether there are adequate internal controls to ensure that transactions giving rise to contingent liabilities are executed only by persons authorised to do so and in accordance with the laid down procedures.
- The auditor should also examine whether in case of LCs for import of goods, as required by the abovementioned Master Circular on guarantees and co-acceptances, the payment to the overseas suppliers is made on the basis of shipping documents and after ensuring that the said documents are in strict conformity with the terms of LCs.
- Ascertain whether the accounting system of the bank provides for maintenance of adequate records in respect of such obligations and whether the internal controls ensure that contingent liabilities are properly identified and recorded.
- Performs substantive audit tests to establish the completeness of the recorded obligations. Such tests include confirmation procedures as well as examination of relevant records in appropriate cases.
- Review the reasonableness of the year-end amount of contingent liabilities in the light of previous experience and knowledge of the current year's activities.



- Review whether comfort letters issued by the bank has been considered for disclosure of contingent liabilities.

Bills for Collection

- The auditor should examine whether the bills drawn on other branches of the bank are not included in bills for collection.
- Inward bills are generally available with the bank on the closing day and the auditor may inspect them at that time. The bank dispatches outward bills for collection soon after they are received. They are, therefore, not likely to be in hand at the date of the balance sheet. The auditor may verify them with reference to the register maintained for outward bills for collection.
- The auditor should also examine collections made subsequent to the date of the balance sheet to obtain further evidence about the existence and completeness of bills for collection.
- In regard to bills for collection, the auditor should also examine the procedure for crediting the party on whose behalf the bill has been collected. The procedure is usually such that the customer's account is credited only after the bill has actually been collected from the drawee either by the bank itself or through its agents, etc. This procedure is in consonance with the nature of obligations of the bank in respect of bills for collection.

Treasury Operation-Foreign Exchange and Derivatives:

- While innovative products and ways of trading create new possibilities for earnings for the bank, they also introduce novel and sometimes unfamiliar risks that must be identified and managed. Failure to do so can result losses entailing financial and reputational consequences that linger long after the loss has been recognized in financial statements. Hence, auditor should assess controls as part of audit work.
- It is imperative that an auditor obtains a complete overview of the treasury operations of a bank before the commencement of the statutory audit. After conducting appropriate risk assessment of the treasury processes, the audit program needs to be designed in a manner that it dovetails into not just the control assessments of the treasury process but there is an assurance that the figures appearing in the financial statements as well as the disclosures are true and reflect fairly the affairs of the bank treasury.

Reports to be given to be given by bank Auditors:

- The Auditors' Report should state whether the Balance Sheet, Profit and Loss Account and Cash Flow Statement of the Bank, show a true and fair view of the financial position / result of operations / cash flows respectively, for the period under audit. This is applicable in respect of Nationalised Banks, as well as Banking Companies.
- **Unaudited Branches:** Information relating to number of unaudited Branches should be given. Also, information in respect of Advances, Deposits, Interest Income and Interest Expense for such unaudited Branches should be collected and disclosed in the Audit Report.



- **Additional Matters:** Sec.30 (3) of Banking Regulation Act requires the Auditor to state the following-
 - Whether or not the information and explanations required by him have been found to be satisfactory,
 - Whether or not transactions of the Company fall within the powers of a Banking Company,
 - Whether or not the returns received from the Branch Offices of the Company have been found adequate for the purposes of his audit,
 - Whether the Profit & Loss Account shows a true balance of Profit or Loss for the period covered by such account, &
 - Any other matter, which the Auditor considers should be brought to the notice of Shareholders of the Company.
- **LFAR:** Auditors of Public Sector Banks, Private Sector Banks & Foreign Banks (as well as their Branches), are required to submit Long Form Audit Report (LFAR) on various matters specified by RBI.
- **Certificates:** In addition to Reports, the Auditors of Bank Branches as well as Central Statutory Auditors of Banks, have to furnish / issue various "Certificates" as required by RBI and other Regulations.

AUDIT OF TRUSTS

When conducting the audit of a charitable institution, the auditor should consider the following matters:

- **Constitution:** The auditor should study the constitution of the charitable institution, for example, whether it is set up under the Societies Registration Act or as per section 8 of the Companies Act or as a trust.
- **Interest of members:** Obtain a list of members of the governing body. This will help the auditor in identifying whether any of the members of the governing body has any interest in the charitable institution.
- **Budget:** The auditor should obtain a copy of the budget sanctioned or the financial statement. This would enable him to acquaint himself with the different heads of income and expenditures of incomes and expenditures of the institution.
- **Internal Check:** Examination of the system of internal check, especially as regards the accounting of the amounts collected.
- **Collection & Deposit of income:** Check that the amounts received towards income have been duly collected, received and deposited into the bank regularly and promptly.



- **Subscription and donation:** These institutions receive subscriptions and donations which form the major part of their collections. Therefore the auditor should check the following:
 - ▶ The amount or the rate of the annual subscription.
 - ▶ Any instructions given by the donors as to the specific utilization of donation.
 - ▶ Adequacy of internal controls existing as regards unused receipt books, counter foils, etc.
 - ▶ Where subscriptions are received in advance these should be properly dealt with in the accounts.
- Legacies received: Verify the amounts of legacies received by reference to correspondence with any figures and other available information's.
- Income from Investment: Where the institution has made any investments or given loans, the amount of dividend and interest should be properly vouched with reference to the counterfoils or dividend warrants received. It should be ensured that such loans or grants are given under proper authorizations.
- **Rent:** If some property is given or taken on rent, then the auditor should check the tenancy agreement, the rent slips and the authorized person for the collection or payment, as the case may be, of the rent.
- **Income/Expenditure relating to concert:** Most of the organisations organize special functions such as concert etc. The auditor should be careful in such cases. All the gross receipts and outgoings are to be properly vouched by him. It should be ensured that proper internal check was maintained as regards the receipts and outgoings. For example, the person responsible for collection and disbursements should be separate persons.
- **Expenditure-a major area of concern:** The expenditure of charitable institution is also one of the major areas of concern. Thus the auditor should verify that the expenditure is made only for the charitable purpose. If the expenditure is not for the charitable purpose, then the auditor should examine the implications of applicable law and document for the same.
- **Physical verification:** The auditor should physically verify the cash in hand, inventories and fixed assets.

AUDIT OF MUNICIPALITIES AND PANCHAYATS (LOCAL BODIES)

The major objective of audit of Municipalities and Panchayats are enumerated below;

- To ensure on the fairness and correctness of contents in the Financial Statement
- To report on adequacy of Internal control
- To ensure value of money is fully received on amount spent.
- To detect the frauds and errors.



The following points are to be considered necessary for carrying on audit of Municipalities and panchayats (Local Bodies);

- To ensure that the expenditures incurred conform to the relevant provision of the law and is in accordance with the financial Rules and regulation formed by the compliant authority.
- To ensure that sanction is accorded by the competent authority either special or general.
- To ensure that there is provision of funds for expenditure and is authorized by competent Authority.
- To ensure that where huge financial expenditure is made is run economically and is expected to contribute growth.

Self Examination Questions:

1. Write short notes on Branch and Joint Audit.
2. What are the factors to be considered while carrying on audit of Share and Debentures?
3. Precautions to be taken care of while carrying on audit of divisible profits and dividends.
4. Distinguish between Statutory and Internal Audit.
5. Discuss the Auditing and Assurance Standards relating to audit of Inventories and Fixed Assets.
6. Mention the special steps involved in conducting the audit of college?
7. What are the points which you as an Auditor would look into while auditing the accounts of a Hospital?
8. Discuss the important points in an audit of Co operative Society.
9. While carrying an audit of a Bank what are the special factors considered by you.
10. Write short notes on audit of Local Bodies.

State whether the following statements are true or false.

1. "Branch office", in relation to a company, means any establishment described as such by the company.
2. Where a company has a branch office, the accounts of that office shall be audited by auditor appointed at EGM.



3. Where the branch office of a company is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor.
4. The branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the Audit committee.
5. In big corporate more than one persons or firm of Chartered Accountants are appointed as a Joint Auditor for conducting the audit of the company.
6. "Debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.
7. Final dividend is declared in the general meeting.
8. Statutory Auditor is appointed by the shareholder in the general meeting.
9. Internal Auditor can be removed by the Board.
10. If the debentures are issued as collateral security to the banks or creditors then auditor needs to ensure that such issue is approved by debenture trustee.

[Answer: True, False, True, False, True, True, True, True, True, False.]

Fill in the blanks:

1. Final dividend is declared in the _____.
2. If the debentures are issued as collateral security to the banks or creditors then auditor needs to ensure that such issue is approved by _____.
3. A predetermined _____ rate of interest is payable on debentures irrespective of the fact that company has earned the profit or not.
4. Debenture holders are _____ of the company.
5. Where debentures are issued by a company, then company shall create a _____ account out of the profits of the company.
6. For protecting the interest of debenture holders the company is bound to form _____.
7. Responsibility to report fraud, as applicable to company's auditor applies to _____ auditor.
8. Splitting of shares shall be authorised by _____.



9. A company may issue debentures with an option to convert such debentures into _____.
10. Statutory Auditor is appointed by the shareholder in the _____ meeting.

[Answer: General Meeting, BOD, Rate, Creditors, Debenture Redemption Reserve, Debenture Trustee, Branch, AOA, Shares, General]

Match the Following:

	Column A		Column B
1	More than one persons or firm of Chartered Accountants are appointed	A	Branch Audit
2	Section 68 of the Co. Act 2013	B	Alteration of Share Capital
3	Section 63 the Co. Act 2013	C	Power of company to Purchase its Own Securities
4	Section 61 of the Co. Act 2013	D	Joint Audit
5	Section 139 of the Companies Act 2013.	E	Issue of Bonus Shares

[Answer: D, C, E, B, A]

Multiple choice questions:

- Audit of debenture is covered under section-
 (A)Section 70
 (B)Section 71
 (C)Section 72
 (D)Section 73
- Declaration of dividend is covered under setion-
 (A)Section 122
 (B)Section 123
 (C)Section 124
 (D)Section 125
- Statutory Auditor is appointed by the shareholder in the
 (A)General Meeting
 (B)Statutory Meeting
 (C)EGM
 (D)Board Meeting



4. Statutory Auditor can be removed by the
(A) Shareholders
(B) Audit committee
(C) BOD
(D) None of the above.
5. Internal Auditor is appointed by the
(A) Board
(B) Audit committee
(C) Shareholder
(D) None of the above

[Answer: B, B, A, A, A]