

# Company Law - Statutory Audit

CA Students Orientation Programme  
Chamber of Tax Consultants

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# AGENDA



Agenda!

- \* Regulatory Framework for Financial Statements
- \* Appointment, Powers and duties of Auditors (Sec 139-144)
- \* Accounting Standards
- \* Auditing Standards
- \* Audit Approach
- \* Auditors Report
- \* CARO

# Regulatory Framework for Financial Statements

# REGULATORY FRAMEWORK

Section	Particulars
134(1)	Financial statements including CFS should be approved by BOD before they are being signed by Appropriate Authority ( Chair person, 2 Directors , Chief Executive Director , Chief Financial Officer , Company Secretary)
134(2)	The auditors' report shall be attached to every financial statement
134(3)	Board of Directors Report should be attached before the Statements are laid before the general meeting
134(4)	In case of a One Person Company, mean a report containing explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made by the auditor in his report
134(5)	The Directors' Responsibility Statement
134(6)	The Board's report and any annexures shall be signed by its chairperson of the company or at least two directors ( one should be managing director)
134(7)	A signed copy of every financial statement shall be circulated or published
134(8)	Lays down the fine and penalty for any contravention of the provisions :

# Corporate Social Responsibility

Section	Particulars
135(1)	Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.
135(2)	Board's report shall disclose the composition of the Corporate Social Responsibility Committee.
135(3)	Corporate Social Responsibility Committee
135(4)	approve the Corporate Social Responsibility Policy; ensure that the activities as are included in Corporate Social Responsibility
135(5)	The Board shall ensure that the company spends, in every financial year, at least two per cent. of the average net profits of the company made during the three immediately

# Requirements of Companies Act for Financial Statements

Section	Particulars
136	Right of member to copies of audited financial statement.
137	Copy of financial statement to be filed with Registrar.
138	Internal audit.

# Appointment, Powers and duties of Auditors



# Powers and Duties of Auditor

Section	Particulars
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 may be prescribed:
139(2)	No listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint :- <ul style="list-style-type: none"><li>✓ an individual as auditor for more than one term of five consecutive years; and</li><li>✓ an audit firm as auditor for more than two terms of five consecutive years:</li></ul>



# Powers and Duties of Auditor

Section	Particulars
139(3)	<p>Subject to the provisions of this Act, members of a company may resolve to provide that—</p> <ul style="list-style-type: none"><li>✓ 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</li><li>✓ the audit shall be conducted by more than one auditor.</li></ul>
139(4)	<p>The Central Government may, by rules, prescribe the manner in which the companies shall rotate their auditors in pursuance of sub-section (2)</p>
139(5)	<p>in the case of a Government Company 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 and eighty days from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.</p>

# Powers and Duties of Auditor

Section	Particulars
139(6)	Manner of Appointment of First Auditors
139(7)	in the case of a Government Company 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 and eighty days from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.
139(8)	Any casual vacancy in the office of an auditor shall— <ul style="list-style-type: none"><li>✓ Company not required to conduct audit by auditor appointed by CAG , be filled by BOD with in 30 days.</li><li>✓ 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</li></ul>

# Powers and Duties of Auditor

Section	Particulars
139(9)	<p>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—</p> <ul style="list-style-type: none"><li>✓ he is not disqualified for re-appointment</li><li>✓ he has not given the company a notice in writing of his unwillingness to be reappointed;</li><li>✓ 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.</li></ul>
139(10)	<p>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.</p>
139(11)	<p>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.</p>

# Removal, resignation of auditor and giving of special notice

Section	Particulars
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 prescribed manner
140(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 with the company and the Registrar
140(3)	If the auditor does not comply with sub-section (2), he or it shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees.
140(4)	Special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor.

# Removal, resignation of auditor and giving of special notice

Section	Particulars
140(5)	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:

# Eligibility, qualifications and disqualifications of auditors.

Section	Particulars
141(1)	A person shall be eligible for appointment as an auditor of a company only if he is a chartered accountant:
141(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 authorized to act and sign on behalf of the firm.
141(3)	<p>The following persons shall not be eligible for appointment as an auditor of a company, namely:—</p> <ul style="list-style-type: none"><li>✓ a body corporate other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008</li><li>✓ an officer or employee of the company;</li><li>✓ person who is a partner, or who is in the employment, of an officer or employee of the company</li><li>✓ a person who, or his relative or partner—<ul style="list-style-type: none"><li>▪ is holding any security of or interest</li><li>▪ is indebted to the company</li><li>▪ has given a guarantee or provided any security in connection with the indebtedness of any third person to the company,</li></ul></li></ul>

# Eligibility, qualifications and disqualifications of auditors.

Section	Particulars
141(4)	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	Particulars
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:
142(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 and auditing standards.

Section	Particulars
143(1)	right of access at all times to the books of account and vouchers of the company <b>including any Subsidiary and Associate.</b>
143(2)	<p>In discharging his duties the Auditor shall specifically inquire into the following</p> <ul style="list-style-type: none"><li>• Whether loans and advances have been properly secured and whether the terms and conditions are prima facie not prejudicial.</li><li>• Whether transaction represented by mere book entries are not prejudicial to the interests of the company.</li><li>• Whether Investments are sold below the price at which they were purchased</li><li>• Whether loans and advances are shown as deposit</li><li>• Whether personal expenses are charged to revenue account</li><li>• Whether actual cash is received where the shares are allotted for cash.</li></ul>

# Powers and duties of auditors and auditing standards.

Section	Particulars
143(2)	The auditor shall make a report to the members of the company on the accounts examined by him and on every financial statements after considering the accounting and auditing standards and other matters specifically required to be reported under sub-section (11)
143(3)	The auditor's report shall also state— <ul style="list-style-type: none"><li>✓ 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</li><li>✓ 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;</li><li>✓ the report on the accounts of any branch office</li><li>✓ 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;</li></ul>

# Powers and duties of auditors and auditing standards.

Section	Particulars
143(3)	<ul style="list-style-type: none"><li>✓ the financial statements comply with the accounting standards;</li><li>✓ the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;</li><li>✓ whether any director is disqualified from being appointed as a director under subsection (2) of section 164;</li><li>✓ any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith</li><li>✓ whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls;</li><li>✓ such other matters as may be prescribed.</li></ul>
143(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.

# Powers and duties of auditors and auditing standards.

Section	Particulars
143(5)	In the case of a Government company, 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.
143(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,— <ul style="list-style-type: none"><li>✓ conduct a supplementary audit</li><li>✓ comment upon or supplement such audit report</li></ul>
143(7)	the Comptroller and Auditor- General of India may if he considers necessary, by an order, cause test audit to be conducted of the accounts of such company

# Powers and duties of auditors and auditing standards.

Section	Particulars
143(8)	Where a company has a branch office the accounts of that office shall be audited either by the auditor appointed for the company under this Act or by any other person qualified for appointment as an auditor of the company
143(9)	Every auditor shall comply with the auditing standards.
143(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 (38 of 1949), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority:
143(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.

# Powers and duties of auditors and auditing standards.

Section	Particulars
143(12)	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 may be prescribed, 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 may be prescribed
143(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.
143(14)	The provisions of this section shall mutatis mutandis apply to— <ul style="list-style-type: none"><li>✓ the cost accountant in practice</li><li>✓ the company secretary in practice</li></ul>
143(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.

# Auditor not to render certain services (Sec 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 may be, 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:

# Accounting Standards





# Accounting Standards

There are 2 sets of Accounting standards applicable as on date ;

- \* Companies (Indian Accounting Standards) Rules, 2015  
- INDAS
- \* Companies ( Accounting Standards ) Rules, 2006

# IndAs- Phase I

The Indian Accounting Standards (Ind AS) shall be applicable to the companies as follows:

- \* On voluntary basis for financial statements for accounting periods beginning on or after April 1, 2015, with the comparatives for the periods ending 31st March, 2015 or thereafter
  
- \* On mandatory basis for the accounting periods beginning on or after April 1, 2016, with comparatives for the periods ending 31st March, 2016, or thereafter, for the companies specified below
  - (a) Companies whose equity and/or debt securities are listed or are in the process of listing on any stock exchange in India or outside India and having net worth of Rs. 500 Crores or more.
  
  - (b) Companies other than those covered in (ii) (a) above, having net worth of Rs. 500 Crores or more.
  
  - (c) Holding, subsidiary, joint venture or associate companies of companies covered under (ii) (a) and (ii) (b) above.

# IndAs- Phase II

- \* On mandatory basis for the accounting periods beginning on or after April 1, 2017, with comparatives for the periods ending 31st March, 2017, or thereafter, for the companies specified below
  - (a) Companies whose equity and/or debt securities are listed or are in the process of being listed on any stock exchange in India or outside India and having net worth of less than rupees 500 Crores.
  - (b) Companies other than those covered in paragraph (ii) and paragraph (iii)(a) above that is unlisted companies having net worth of rupees 250 crores or more but less than rupees 500 Crores.
  - (c) Holding, subsidiary, joint venture or associate companies of companies covered under paragraph (iii) (a) and (iii) (b) above.
- \* However, Companies whose securities are listed or in the process of listing on SME exchanges shall not be required to apply Ind AS. Such companies shall continue to comply with the existing Accounting Standards unless they choose otherwise.
- \* Companies not covered by the above roadmap shall continue to apply existing Accounting Standards prescribed in Annexure to the Companies (Accounting Standards) Rules, 2006

# IGAAP

- \* All companies to whom IndAs is not applicable, will continue to apply existing Accounting Standards prescribed in Annexure to the Companies (Accounting Standards) Rules, 2006
- \* IGAAP : For the purpose of applicability of Accounting Standards, enterprises are classified into Small and Medium Sized Companies and Others

All Accounting Standards are applicable to a NON – SMC company

# Auditing Standards



# Auditing Standards

- \* S. 143(9) – Every auditor shall comply with the auditing standards.
- \* Classification of Standards on Auditing

Standards	Category
100-199	Introductory Matters
200-299	General Principles and Responsibilities
300-499	Risk Assessment and Response to Assessed Risks
500-599	Audit Evidence
600-699	Using Work of Others
700-799	Audit Conclusions and Reporting
800-899	Specialized Areas
2000-2699	Standards on Review Engagements (SREs)

# Auditing Standards

## **200-299 General Principles and Responsibilities**

- \* [SA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing](#)
- \* [SA 210, Agreeing the Terms of Audit Engagements](#)
- \* [SA 220, Quality Control for an Audit of Financial Statements](#)
- \* [SA 230, Audit Documentation](#)
- \* [SA 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements](#)
- \* [SA 250, Consideration of Laws and Regulations in an Audit of Financial Statements](#)
- \* [Revised SA 260, Communication with Those Charged with Governance](#)
- \* [SA 265, Communicating Deficiencies in Internal Control to Those Charged with Governance and Management](#)
- \* [Revised SA 299, Joint Audit of Financial Statements](#)

# Auditing Standards

## **300-499 Risk Assessment and Response to Assessed Risks**

- \* SA 300, Planning an Audit of Financial Statements
- \* SA 315, Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment
- \* SA 320, Materiality in Planning and Performing an Audit
- \* SA 330, The Auditor's Responses to Assessed Risks
- \* SA 402, Audit Considerations Relating to an Entity Using a Service Organisation
- \* SA 450, Evaluation of Misstatements Identified During the Audit



# Auditing Standards

## **500-599 Audit Evidence**

- \* [SA 500, Audit Evidence](#)
- \* [SA 501, Audit Evidence-Specific Considerations for Selected Items](#)
- \* [SA 505, External Confirmations](#)
- \* [SA 510, Initial Audit Engagements – Opening Balances](#)
- \* [SA 520, Analytical Procedures](#)
- \* [SA 530, Audit Sampling](#)
- \* [SA 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures](#)
- \* [SA 550, Related Parties](#)
- \* [SA 560, Subsequent Events](#)
- \* [Revised SA 570, Going Concern](#)
- \* [SA 580, Written Representations](#)

# Auditing Standards

## **600-699 Using Work of Others**

- \* [SA 600, Using the Work of Another Auditor](#)
- \* [Revised SA 610, Using the Work of Internal Auditors](#)
- \* [SA 620, Using the Work of an Auditor's Expert](#)

## **700-799 Audit Conclusions and Reporting**

- \* [Revised SA 700, Forming an Opinion and Reporting on Financial Statements](#)
- \* [SA 701, Communicating Key Audit Matters in the Independent Auditor's Report](#)
- \* [Revised SA 705, Modifications to the Opinion in the Independent Auditor's Report](#)
- \* [Revised SA 706, Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report](#)
- \* [SA 710, Comparative Information—Corresponding Figures and Comparative Financial Statements](#)
- \* [Revised SA 720, The Auditor's Responsibilities Relating to Other Information](#)

# Audit Approach



# Audit Approach

## **General Audit Approach :**

- \* Planning Stage
- \* Execution Stage
- \* Reporting Stage
- \* File Compilation Stage

# Audit Approach

- \* Audit engagement letter
- \* Understand the business model
- \* Understand various policies and procedures
- \* Identify various risks associated at entity level and process level
- \* Identify significant account balances from the Trail balance / Financial statements (drill down / Top down approach)
- \* Identify significant disclosure items in the Financial statements
- \* Identify Significant class of Transactions [SCOT] and its flows (obtain process narrative in respect of those transactions)

# Audit Approach

- \* Conduct the Walkthrough
- \* Test the design of the controls (review process narratives)
- \* Test the controls (based on samples selected)
- \* Identify the risks associated & controls which address the risk of material misstatement
- \* Check whether any significant deficiency in control exist?
- \* Document the results of control testing
- \* Discuss the findings with the management / communicate significant deficiencies
- \* Obtain Management Representation letter
- \* Report

# MATERIALITY PLANNING

## Materiality in Planning and Performing an Audit – SA 320

- \* reasonable assurance by obtaining audit evidences to reduce audit risk to an acceptable low level
- \* audit risk and materiality should be considered for determining the nature, timing and extent of audit procedure
- \* expresses opinion in good faith and after exercise of reasonable care and judgement

# RISK ASSESSMENT

- \* Entity objectives to enable the identification and assessment of related risks
- \* Identifies and analyses risk related to the objectives
- \* Considers the potential for fraud
- \* Identifies and analyses significant changes that would impact the internal control system



# Auditors Report

# Standards pertaining to Audit Reports

<b>SA 700</b>	<b>Forming an Opinion and Reporting on Financial Statements - to be used only in case of unmodified opinion.</b>
<b>SA 705</b>	<b>Modifications to the Opinion in the Independent Auditor's Report - to be used only in case of modified opinion.</b>
<b>SA 706</b>	<b>Emphasis of Matter Paragraphs and Other Matter paragraphs in the Independent Auditor's Report - to be used if there is an emphasis of matter and it also deals with Other Matters</b>
<b>SA 701</b>	<b>Communicating Key Audit Matters in the Independent Auditor's Report</b>
<b>SA 720</b>	<b>The Auditor's Responsibilities Relating to Other Information</b>

**Applicable for Audit reports for periods beginning on or after April 1, 2018.**

**SA – 700 (Revised)**

# Forming an Opinion and Reporting on Financial Statements

# Changes in SA 700 ( Revised )

- \* The flow of the reporting has been changed substantially from the earlier SA-700
- \* The new Standard is applicable for audits of all the financial statement for accounting periods beginning on and after April 1, 2018
- \* This applies only to a complete set of General Purpose Financial Statement.

# Flow of the report as per Revised SA-700

- \* Title
- \* Addressee
- \* Auditors' Opinion
- \* Basis for Opinion (to be given even for unmodified opinion)
- \* Going Concern (SA-570 - Revised)
- \* Key Audit Matter (SA-701 Revised)
- \* Emphasis of Matter (SA-706 Revised)
- \* Management Responsibility for Financial Statements
- \* Auditors' Responsibilities for the audit of financial statements
- \* Other Information (SA720 Revised)
- \* Reporting on other legal and regulatory matters (SA-706 Revised)
- \* Signature block
- \* Place and Date of Signing

# Audit opinion

- \* In order that the reader does not have to search for the opinion paragraph in the report, the first reporting paragraph is the opinion paragraph
- \* This is true whether it is an unmodified opinion or a modified opinion
- \* The basis for the opinion now follows the opinion paragraph.
- \* The Auditor's responsibility is now a more detailed paragraph detailing in a more specific manner the responsibilities of the Auditor

# Forming a Clean (Unmodified) Opinion

- The financial statements are prepared, in all ***material respects, in accordance with the applicable financial reporting framework*** including qualitative aspects of entity's accounting policies and possible bias in management's judgments.
- Has ***obtained reasonable assurance about whether the financial statements are free of material misstatements due to Fraud or Error based on : Sufficient and appropriate audit evidence;***
- Whether uncorrected ***misstatements*** are material, Individually or in aggregate in accordance with SA 450.
- ***Requirements of the reporting framework*** (eg., the Accounting Standards) have been materially complied with
- Disclose the ***accounting policies selected and applied and Consistency and appropriateness*** of those policies
- ***Reasonable estimates*** are used by the management
- Information presented in ***relevant, reliable, comparable and understandable***
- ***Disclosures are adequate*** to enable ***users to understand*** the ***effect of material transactions***
- ***Terminology*** used is appropriate.

SA-705 and SA 706

# Modification of the report and inclusion of other matters



# Introduction and Scope

- Deals with circumstances when the auditor concludes modification to the report is necessary.
- Types of modified opinions
  - ✓ **Qualified Opinion**
  - ✓ **Adverse Opinion**
  - ✓ **Disclaimer of Opinion**
- The decision on the type of opinion depends upon:
  - ✓ The ***nature of the matter*** giving rise to the modification i.e. whether the financial statements are materially misstated
  - ✓ ***Inability to obtain*** sufficient and appropriate audit evidence
  - ✓ Auditor's judgment about the ***pervasiveness*** of the effects or possible effects of the matter
- The auditor shall modify the opinion when:
  - ✓ He concludes that, ***based on audit evidence, the financial statements as a whole are NOT free of material misstatements***; or
  - ✓ The auditor is ***UNABLE to obtain sufficient appropriate audit evidence to conclude*** that the financial statements are free of material misstatements

# Modifications in the Report

## QUALIFIED OPINION

The auditor shall express qualified opinion when :

- ✓ He concludes that the misstatements, individually or in aggregate , ***are MATERIAL , BUT NOT PERVASIVE*** to the financial statements
- ✓ He is ***unable to obtain sufficient appropriate audit evidence*** but also concludes that the possible effects of undetected misstatements could be ***MATERIAL, BUT NOT PERVASIVE***

## ADVERSE OPINION

When the auditor concludes that ***having obtained sufficient appropriate audit evidence***, the misstatements, individually or in aggregate, are ***BOTH MATERIAL AND PERVASIVE***, he issues an adverse opinion.

## DISCLAIMER OF OPINION

- ❑ When the auditor is ***unable to obtain sufficient appropriate audit evidence*** and concludes that the possible effects of undetected misstatements are ***BOTH MATERIAL AND PERVASIVE***, he issues a disclaimer of opinion .
- ❑ In extremely ***rare circumstances*** , having obtained sufficient appropriate audit evidence, BUT due to multiple uncertainties , the auditor is not able to form an opinion , due to ***possible interaction of those uncertainties and their possible cumulative outcomes*** , he issues a disclaimer of opinion.

# Modifications in the Report( Contd..)

## Auditors ' Report Modification Matrix:

Nature of matter giving rise to the modification	Auditor's Judgment about the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but not pervasive	Material and Pervasive
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

# Material Misstatements

A misstatement is the difference between the amount of classification, presentation, or disclosure reported in the financial statements and the classification, presentation, or disclosure required as per the applicable financial reporting framework.

This may arise in relation to :

**1. Appropriateness of the selected accounting policies**

- ✓ Selected accounting policies are not consistent with the applicable financial reporting framework ;
- ✓ Financial statements , including notes thereon , do not represent underlying transactions and events that achieves fair presentation

**2. Application of selected accounting policies**

- ✓ When accounting policies are not applied consistently , including consistency between periods , similar transactions and events ;
- ✓ Method of application is erroneous

# Material Misstatements (Contd..)

3. Appropriateness or adequacy of disclosures in the financial statements :
  - ✓ Financial statements **do not include all disclosures** required by the applicable financial reporting framework
  - ✓ Disclosures are **not presented in accordance with the applicable financial reporting frame work**
  - ✓ The financial statements **do not provide the disclosures necessary to achieve fair presentation**

# Revision in SA 706

- \* Similarly excepting for the reporting of Going concern paragraph separately in a paragraph titled “material uncertainty relating to going concern”
- \* The other reporting of “Emphasis of Matter” and “Other Matters” or the “other legal and regulatory requirements” paragraphs are substantially the same as the previous SA-706 except that there are some rules to be followed relating to Key Audit Matters which is dealt with separately

# Emphasis of Matter Paragraph

- ❑ An emphasis of matter paragraph is useful when the auditor, **having formed an opinion, intends to draw the attention of the users** to :
  - ✓ A matter, though **appropriately presented** and disclosed, is of fundamental importance to the users to understand the financial statements;
  - ✓ Any other matter relevant to the **users' understanding** of the audit, auditor's responsibility or Auditor's Report.
  - ✓ Where an emphasis of matter paragraph **is required by any other auditing standard**, the disclosure shall be as per this SA.
  
- ❑ Such a paragraph shall refer **to information presented and disclosed in financial statements.**
  
- ❑ The auditor should have **obtained sufficient appropriate audit evidence** that the matter is not materially misstated.

# Emphasis of Matter Paragraph (Contd..)

- ❑ The emphasis of matter paragraph shall be **placed immediately after the Opinion** paragraph in the Auditor's Report under the heading "Emphasis of Matter Paragraph"
- ❑ Include a **clear reference** to the matter being emphasized and to the relevant disclosures
- ❑ Indicate that the **Auditor's opinion is NOT modified by using words like "Without qualifying our opinion" or "Our report is not qualified on this account"**



SA – 701 Revised

**Communicating Key Audit Matters  
in the Independent Auditor's  
Report**

# Key Audit Matter - KAM

## What is Key Audit Matter??

- \* Are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period.
- \* Key audit matters are selected from matters communicated with those charged with governance
- \* **KAM is required to be Disclosed by All Listed Entities and those entities that are components to a Listed Entities Consolidated Financial Statements as the Holding Company Auditor may request for mention of KAM in his Component Auditor letter.**
- \* There is however no bar on including KAM in an unlisted entity not covered by above situation also as it is the Auditors Prerogative to mention and report matters that he considers significant to the reader of the Audit Report.

# Why should it be reported

- \* The objective of reporting is to determine key audit matters and having formed an opinion on the financial statements , communicate those matters by describing them in the auditors' report.
- \* The purpose of communicating key audit matters is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed
- \* Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgment in the audited financial statements

# What needs to be covered as KAM

- \* They are primarily issues that are reported to those charged with Governance
- \* They are areas or matters that required significant Auditor attention.
- \* Areas of higher risk of material misstatement or any significant risk identified as per SA315
- \* Areas requiring significant auditor and management judgement including accounting estimates involving significant estimation by management like Impairment testing
- \* The effect on the audit of significant events or transactions during the period

# KAM Importance

- \* KAM is not a substitute to modification of report ie. The Auditor cannot make a KAM reporting instead of issuing a modified report.
- \* Similarly a matter of material uncertainty relating to going concern needs to be specifically reported in accordance with SA-570 revised and not made a Key Audit matter for reporting under SA-701.
- \* It is also not a substitute for disclosure of a particular matter in the financial statement.
- \* It is also not a separate opinion on individual matter.

# KAM disclosure and Modification of opinion paragraphs

- \* Matters that are part of Audit opinion modification either as qualification or adverse opinion or a disclaimer of opinion do not need mention once again as a KAM although these by their nature are Key Audit matters.
- \* They need to be disclosed as per the Applicable SA namely SA 705
- \* Similarly a Material uncertainty relating to Going Concern being disclosed in accordance with SA-570 revised does not need a separate mention once again as KAM.
- \* In such situation it is advised that the KAM paragraph mention that apart from the matters forming basis of qualified opinion the following are the other KAM.

*SA 720*

# The Auditor's Responsibilities Relating to Other Information

# What does SA 720 require an Auditor to do.

- \* This standard deals with the Auditors' responsibility with respect to other information included in the entity's annual report.
- \* Every Auditor is required to read all the contents in the Annual report which includes the financial statement.
- \* The auditor is also required to mention in his audit report that he has read and has not noticed any material inconsistency between the audit evidence and his understanding on the basis of his he formed his opinion nor is there any material misstatement.



# What if there is a material inconsistency or material misstatement

- \* The auditor is required to inform of such material inconsistency or material misstatement to the people charged with governance to make suitable correction before the same is circulated.
- \* If the said corrections are not carried out then the Auditor is required to take such steps as may be necessary as per the Standards on Auditing if the opinion of the Auditor will undergo a change pursuant to such matter.
- \* If the opinion does not change, then the auditor is required to report the errors noticed by him which are material in nature.

# What if the other information is not made available when the audit report is issued

- \* If the other information to be included in the annual report is not made available he has to make a specific mention of that fact in the audit report.
- \* Even if part of the information is not available the mention of sections or portions not read are to be mentioned.
- \* This does not absolve the auditor from reading in case of a listed Company.
- \* The auditor is still required to read such matter, when they are ready, to check if there are any material inconsistency or material misstatement in such other information.

CARO 2016

# *Applicability of CARO*

Every Report made by the auditor under section 143 of the 2013 would include [CARO 2016 and](#) CARO 2016 is applicable for Financial Year 2015-16, Financial Year 2016-17 and subsequent years. It would be applicable to every company (except some companies) including a foreign company defined under section 2(42) of the 2013 Act.

The CARO, 2016 would not be applicable to the auditor's report on consolidated financial statements.

# Companies not covered under CARO 2016

1. Banking Companies as defined under section 5(c) of the Banking Regulation Act, 1949
2. Insurance Company as defined under the Insurance Act, 1938
3. Companies Incorporated with Charitable objects etc, i.e. companies licensed to operate under section 8 of Act 2013
4. One company as defined under section 2(62) of the 2013 Act
5. **Small Company** as defined under 2(85) of the 2013 Act
6. Private company not being a holding or a subsidiary company of a public company:
  - ✓ with a paid a paid up capital and reserves and surplus not more than INR 1crore
  - ✓ does not have total borrowings exceeding INR 1crore from any bank or any financial institution at any point of time during the FY and
  - ✓ does not have total revenue as defined in schedule III, to the 2013 Act (including revenue from discontinuing operations) exceeding INR 10 crore during the financial year as per the financial statements.

# Report on Internal Financial Controls

# IFC with reference to Financial Statements

- \* Apart from the report on Caro, the Auditor is also required to report on Internal Financial Controls with reference to Financial Statements.
- \* Generally it is annexed as a separate Annexure to the Main Audit report after the report on CARO.
- \* However Private Limited Company having turnover less than 50 crores or borrowing less than 25 crores are exempted from IFC reporting.
- \* There has been change to the nomenclature of the IFC report as it is now with reference to Financial Statements.

Thank You