

CNK & Associates LLP

Audit under
Companies Act 2013
– An update

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Audit Reporting for Companies

- The Companies Act lays down various provisions for reporting by statutory auditors
 - Sec 143 of Companies Act, 2013 – sub sections 1 to 15 lay down the reporting requirements
- The actual format in which reporting is to be done is governed by the applicable Standards on Auditing (SAs) issued by ICAI (to be notified by NFRA)
 - *SAs are primarily based on ISAs with very few modifications*

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Appointment,
Disqualifications,
Responsibilities as per
Companies Act, 2013

Companies Act requirements for Auditors appointment, etc. (sec. 139 – 148)

Appointment of auditors

- Appointment to be done once for 5 years – no requirement for ratification to be done every year
- Mandatory retirement after 5 / 10 years for individuals / firms
- First appointment of auditors – to be done by BoD within 30 days – in such case rotation maybe after 1+5+5 years
- No rotation for Small Companies and OPCs

Appointment of Auditors...

- Rotation – Rules lay down retrospective applicability as under:
 - Applicable to all Listed Companies
 - For Unlisted Public Companies if share capital ≥ 10 crores
 - For Private Companies if share capital ≥ 50 crores
 - For other companies with capital below above limits if public borrowings (from FIs, banks, public deposits) ≥ 50 crores
 - Cooling period for 5 years
- *As per SQC1, rotation of audit engagement partner needs to be done every 7 years (some exceptions for proprietorships with conditions)*

Eligibility and Qualification Of Auditors

- Chartered Accountant in Practice
- Firm / LLP where majority of partners are practicing in India are qualified as Cas
- The following are not eligible for appointment:

Financial Interest Test

A person who or his **relative** or partner –

- Is holding any security in the company / subsidiary / holding / associate company in excess of (***face value of Rs. 1 lakh – corrective action within 60 days***)
- Is indebted or has given guarantee to the company / subsidiary / holding / associate ***in excess of Rs. 1 lakh***

Eligibility and Qualification Of Auditors ...

Business Relationship Test

- Disqualified if auditor has business relationship with company / subsidiary / holding / associate company
- Such relationships will be construed as transaction for commercial purposes **except**:
 - Professional services permitted to be rendered by auditor under the Act or CA Act (incl. rules and regulations);
 - *Commercial transactions in ordinary course of business at arms' length price like a customer with those doing business of telecom, airlines, hospitals, hotels, or similar businesses.*

Eligibility and Qualification Of Auditors ...

Limit on number of Audits

- Not to exceed 20 companies per partner
- Limit applicable for Public Companies and Private Companies having share capital > 100 crores

Do the limits apply overall for the firm i.e. in a firm of 3 partners, can 1 partner sign 60 audit reports?

Disqualification Of Auditors – Prohibited Services

- Besides audit, only such services can be provided as approved by Board of Directors or Audit Committee.
- The following services are however *specifically not permitted*:
 - Accounting and book keeping services;
 - Internal audit;
 - Design / implementation of any financial information system;
 - Actuarial services,
 - Investment advisory / banking services;
 - Outsourced financial services and
 - *Management services, (NFRA has recently interpreted this)*
 - Other kind of services to be prescribed

Disqualification Of Auditors – Prohibited Services...

- Restrictions apply to Audit firm, its partners, its parent, subsidiary or associate company or any other entity in which the firm or any of its partner has significant influence / control or whose name / trade name / brand is used by the firm or any of its partners.
- IFAC Code of Ethics defines 'management services' as '*assistance for carrying out such services for the company which are the responsibilities of the management*'.

NFRA defines (interprets) Management Services

- Amongst the prohibited services listed in **Section 144**, the one entry that is the **most widely defined is that of “Management Services”**. This is also not confined to the functional areas of finance and accounting to which all the other entries at clauses (a) to (g) are clearly related.
- There is no definition of “Management Services” provided in the Act; hence it is to be understood in its literal meaning.
- “Management Services” has to be taken as services (performed by the Statutory Auditor) for the management, either:
 - in the form of doing actions/functions that would otherwise have to be done/undertaken by the management;
 - **providing any kind of support (inclusive of analysis, research, advice etc.) that is required by management for the performance of those actions / functions**
- Since Code of Ethics does not contain specific definition of ‘management services’, NFRA ignored all submissions

Auditor's Rights

- Access to books of accounts kept at registered office and at any other place in India.
- Auditor of holding company shall also have the right of access to the subsidiaries' books of accounts so far as it relates to the consolidation. No such provision currently.

Remuneration of Auditors

- For 1st year to be decided by BoD
- Subsequently, to be decided at AGM of Company
- Expenses incurred by auditor in conduct of audit to be additional
- Any facility extended to him by company for conduct of audit also additional
- For other services rendered (as permissible), no approval at AGM
- *Resolution for auditors' remuneration should be very explicit and clear – else the fees paid can amount to an advance / loan and subsequent disqualification*

Removal of Auditors (Sec. 140)

Removal of Auditor
before the expiry of
the term



- Special Resolution of the Company and
- Prior approval of Central government.

Resignation of
Auditor



- Auditor to intimate to company and file in prescribed form with the Registrar within 30 days indicating reasons and facts.

Appointing as
auditor a person
other than a
retiring auditor



- Special Notice is required for resolution
- To send a copy of special notice to Auditor.
- Retiring auditor's right to make representation which should be sent along with notice to the members or read out in the meeting.

Auditor Resignation

- Appointment of an 'auditor;' is for a period of 5 years
 -
- Several cases of auditor resignations before end of term – In many cases, resignations were given after year end and towards conclusion of the audit
- MCA has issued notices in several such cases to audit firms
- ICAI has in Dec 2018 issued “Implementation Guide on resignation or withdrawal from an engagement to perform audit of FS”
- In case of resignation, specific reasons to be communicated

ICAI Implementation Guide on Auditor Resignation

•Implementation Guide on resignation or withdrawal from an engagement to perform audit of FS – ICAI (Dec 2018)

- May depend on stage of completion of the audit
- If the audit is substantially completed, he may decide to disclaim an opinion and explain the scope of limitation
- The auditor should describe the circumstances while giving the reasons for resignation suitably, instead of mentioning ambiguous reasons such as other pre-occupation or personal reasons or administrative reasons or health reasons or mutual consent or unavoidable reasons.

ICAI IG on Auditor Resignation ...

- **As per IG of ICAI, some valid reasons could be:**

- Non payment of fees
 - inability to obtain sufficient appropriate audit evidence,;
 - Possible effects on the FS of undetected misstatements, if any, could be both material and pervasive;
 - If the matter is related to a material misstatement of the FS that relates to specific amounts in the FS (including quantitative disclosures), the auditor should include a description and quantification of the financial effects of the misstatement, unless impracticable
 - Cannot legally continue as auditor
-
- **Legal advice maybe sought, if required**

Sec 146: Auditor to attend AGM

- As per above section, notice for 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.
- This applies also to private limited companies
To avoid this, preferable to include in Engagement Letter that auditor is exempted from attending general meetings.

Mandatory Joint Audits: FDI Policy announced on 5th January 2018 (extract)

Prohibition of restrictive conditions regarding audit firms:

The extant FDI policy does not have any provisions in respect of specification of auditors that can be appointed by the Indian investee companies receiving foreign investments.

It has been decided to provide in the FDI policy that wherever the foreign investor wishes to specify a particular auditor/audit firm having international network for the Indian investee company, then audit of such investee companies should be carried out as joint audit wherein one of the auditors should not be part of the same network

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Audit Reporting
provisions as per
Companies Act, 2013

Audit Reporting under Companies Act, 2013

- Section 143 is the relevant section
- Section 143 consists of 15 sub sections
- *For sub sections 143(1), 143(3)(f) and 143(3)(h) reporting only if there are adverse or negative observations*
- For other sections reporting in all cases (i.e. even if no adverse observations)
- **Reporting under section 143 also applies to Audit Report on CFS**

Reporting under section 143(1)

To make inquiries and report on following matters if answer is in negative or adverse:

- (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 co;
- (c) where the company not being an investment / 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**;
- (d) whether **loans and advances** made by the company have been shown as **deposits**;

Reporting under section 143(1) ...

- (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.

Reporting under section 143(2)

- The auditor shall make a report to the members of the company on the accounts examined by him and on every FS 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,
- FS 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 *other matters as may be prescribed ***

** refers to CARO*

*** none so far*

Reporting under section 143(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 u/ss (8)** by a person other than the company's auditor has been sent to him 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 FS comply with the accounting standards;***

Reporting under section 143(3) ...

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

As per ICAI GN:

- **Such observations / comments would ordinarily lead to Modification or an EoM in the AR on FS;**
- **The phrase 'observations / comments' should be construed to have same meaning as referring to modification or EoM in the AR,**
- **The 'observations / comments' in AR cannot have any adverse effect on the functioning of the company, but it might contain matters which might have an adverse effect**
- **Act does not specify meaning of the phrase “adverse effect on functioning of the company” – hence cannot be interpreted to cover all events (like revocation of license), but only events that may impact the FS under audit**

Reporting under section 143(3) ...

143(3)(f) ... As per ICAI GN ...

- Because of inclusion of (f), there is no change in scope of audit and auditor's role as contemplated under SAs and other ICAI pronouncements;
- **However auditor has to now evaluate if subject matters leading to modification or EoM in AR may have an adverse effect on functioning of the company;**
- In case of matters that are pervasive in nature, can significantly impact the operations of the company e.g. EoM on 'Going Concern' assumption.
- In such cases, the Auditor should report under 143(3)f)

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

Reporting under section 143(3) ...

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

As per ICAI GN:

- Matters that cause modification in AR can have consequential effects (or possible effects) on books maintained and other matters connected therewith;
- Sec 128 requires every company to prepare and keep its books of account and FS that give a 'true and fair' view;
- Sec 129(1) requires that FS should comply with notified AS;
- Sec 2(13) defines 'books of account';
- 143(3)(b) also requires reporting on 'books of account'
- Auditor needs to report under this clause any matter of modification in AR, if it can have effect on 'books of account' maintained by company;

Reporting under section 143(3) ...

(i) whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls; [IFC defined in 134(5)]

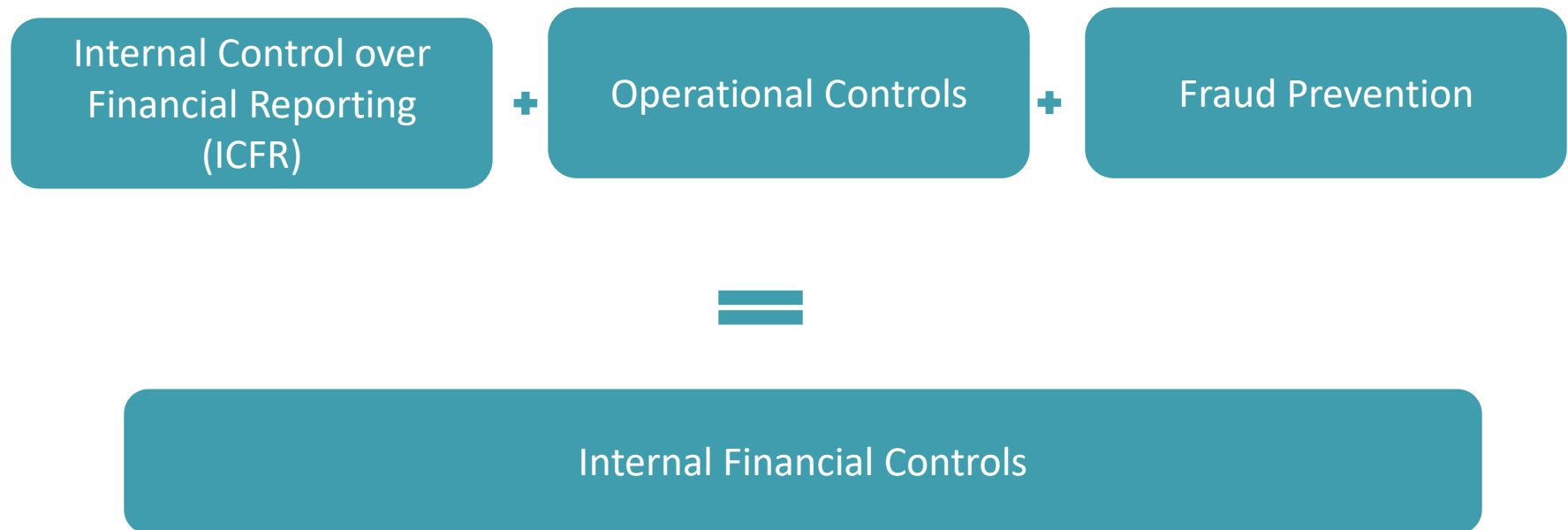
- As per sec 134(5)(e), “ internal financial controls” means the policies and procedures adopted by the company for:
 - ensuring the orderly and efficient conduct of its business, including
 - adherence to company’s policies,
 - the safeguarding of its assets,
 - the prevention and detection of frauds and errors,
 - the accuracy and completeness of accounting records, and
 - the timely preparation of reliable financial information.

Reporting under section 143(3) ...

- Definition as per 134(5)(e) is very wide since it related to reporting by directors
- ICAI however, in its GN on “Reporting under IFC” restricted the responsibility of auditors to only those controls related to FS
- Companies Amendment Act 2017 has amended sec 143(3) to now require auditors to state “whether the company has adequate internal financial controls in place with reference to financial statements and the operating effectiveness of such controls”

Internal Financial Controls thus means ...

‘IFC’ means the policies and procedures adopted by the company for ensuring the orderly and efficient conduct of its business, including adherence to company’s policies, the safeguarding of its assets, the prevention and detection of frauds and errors, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.



Reporting under section 143(3) ...

(j) such other matters as may be prescribed (as under)

Other matters to be included in AReport u/s 143(3): Rule 11

- Whether company has disclosed impact, if any, of *pending litigations* on its financial position in its FS.
- Whether company has provided for *material foreseeable losses*, if any, on long term contracts including derivative contracts.
- Whether there has been any delay in *transferring amounts to IEPF*.

Reporting under section 143(3) ...

Other matters to be included in auditors report u/s 143(3): Rule 11

- **Whether company has disclosed impact, if any, of *pending litigations* on its financial position in its FS.**
 - *To be cross referred to Notes in FS – if no such note then separate annexure for the same*
 - *Whether show-cause notice can be construed as litigation?*
 - *AS 29 chart to be followed*

- **Whether company has provided for *material foreseeable losses*, if any, on long term contracts including derivative contracts.**
 - Can become difficult for auditor to comment
 - To consider all long term contracts

- **Whether there has been any delay in transferring amounts to IEPF**
 - Factual reporting

Reporting under section 143(4) to (10)

- **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.
 - *Requirement of highlighting adverse observations/comments in audit report in thick/bold type or italics omitted.*
- **Sec 143(5) to 143(7): Reporting to C&AG by auditors of PSUs**
 - Similar to report issued u/s 619 of Companies Act, 1956
 - Additional reporting instructions from CAG
- **Sec 143(8): Reporting by Branch Auditors to main auditor**
 - same responsibility as per sec 143(1) to 143(4), 143(12).
- **Sec 143(9) / (10): Auditor to comply with Auditing Standards**
 - To be notified by NFRA – till that time, Standards on Auditing (SAs) issued by ICAI shall be deemed to be auditing standards.

Reporting under section 143(11)

Statement to be included in report on matters specified

- **Companies (Auditor's Report) Order, 2016 (CARO, 2016)**
- **Applies to every company including a foreign company, except:**
 - banking company
 - insurance company
 - company licensed to operate under section 8 (with charitable objects) of the Companies Act;
 - One Person Company and Small Companies (turnover upto 2 crs and capital 50 lakhs)
 - private limited company (*not being subsidiary / holding co of public co*) which has:

Paid up capital and reserves	Not > Rs. 1 crore on BS date AND
Loan o/s from any bank/FI	Not > Rs. 1 crore at any point of time AND
Turnover	Not > Rs. 10 crores

Reporting under section 143(11) ... CARO 2016...

Reporting on 16 items – some important reporting clauses:

- Fixed Asset related
- Loans, etc. to related parties
- Whether any loans covered u/s 185 / 186
- Deposits u/s 73
- Timely payment of PF dues, etc.
 - *Advance Tax, GST shortfall may need to be reported*
- Default in repayment of loans to FIs, banks, etc.
- Fraud
- Managerial remuneration u/s 197
- Related party transactions u/s 177 /188
- Whether required to be registered with RBI?

Audit reporting under Companies Act, 2013...

➤ Sec 143(12) - Reporting of frauds

If an auditor of a company, in the course of the performance of his duties as auditor,

- has 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 immediately report the matter to the CG within the time prescribed.
- In case of frauds involving amounts **lesser than amount specified **** he shall report to the Audit Committee or Board
- Frauds reported only to Audit Committee and Board to be disclosed in Directors' Report

**** Rs. 1 crore**

Fraud reporting under CARO, 2016 vis-a-vis Section 143(12)

Points	Clause (xii) of CARO, 2016	Section 143(12) Of Companies Act, 2013
Frauds on the company	To be reported by the auditor irrespective of whether committed by employees or officers or by third parties	To be reported by the auditor if committed by employees or officers
Frauds by the company	To be reported by the auditor	Not to be reported
Reporting by auditor to	Members of the company as part of auditor's report	Reporting to Central Government, not part of audit reporting to members

Fraud reporting under CARO, 2015 vis-a-vis Section 143(12)

Points	Clause (xii) of CARO, 2016	Section 143(12) Of Companies Act, 2013
Frauds detected by whom to be reported	Frauds noticed or reported (not necessarily by auditor) to be reported	Frauds detected by auditor in course of performance of duties to be reported
Materiality of frauds detected-whether relevant	No express provisions on materiality aspect.	Materiality affects speed and manner of reporting under section 143(12) and Rule 10.10
Companies in respect of which obligations cast on auditor	Obligations on auditors only in respect of companies to which CARO, 2016 is applicable	Obligations on auditors in respect of all companies

Audit reporting under Companies Act, 2013...

- **Sec 143(13)** - No duty of auditor w.r.t. fraud reporting to be deemed as having been contravened, if it is done in good faith.
- **Sec 143(14)** – Provisions u/s 143(12) shall *mutatis mutandis* apply to
 - Cost Accountant in practice
 - Company Secretary in practice
- **Sec 143(15)** - If the auditor does not report the fraud committed or being committed, he shall be punishable with fine which shall be less than Rs. 1 lakhs but may extend to Rs. 25 lakhs.

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Audit Reporting
provisions as per
Standards on Auditing
(SAs)

How many Standards of Auditing are issued by ICAI?

- Standards on Quality Control (SQC) – SQC 1
- SA 100- SA 199 Introductory Matters
- SA 200-SA 299 General Principles and Responsibilities
- SA 300- SA 499 Risk Assessment and Response to Assessed Risks
- SA 500-SA 599 Audit Evidence
- SA 600- SA 699 Using Work of Others
- **SA 700-SA 799 Audit Conclusions and Reporting**
- SA 800- SA 899 Specialized Areas
- SREs 2000-SREs 2699 Standards on Review Engagements (SREs)
- SAEs 3000- SAEs 3699 Standards on Assurance Engagements (SAEs)
- SAEs 3000-SAEs 3399 Applicable to All Assurance Engagements
- SAEs 3400- SAEs 3699 Subject Specific Standards
- SRSs 4000-SRSs 4699 Standards on Related Services (SRSs)

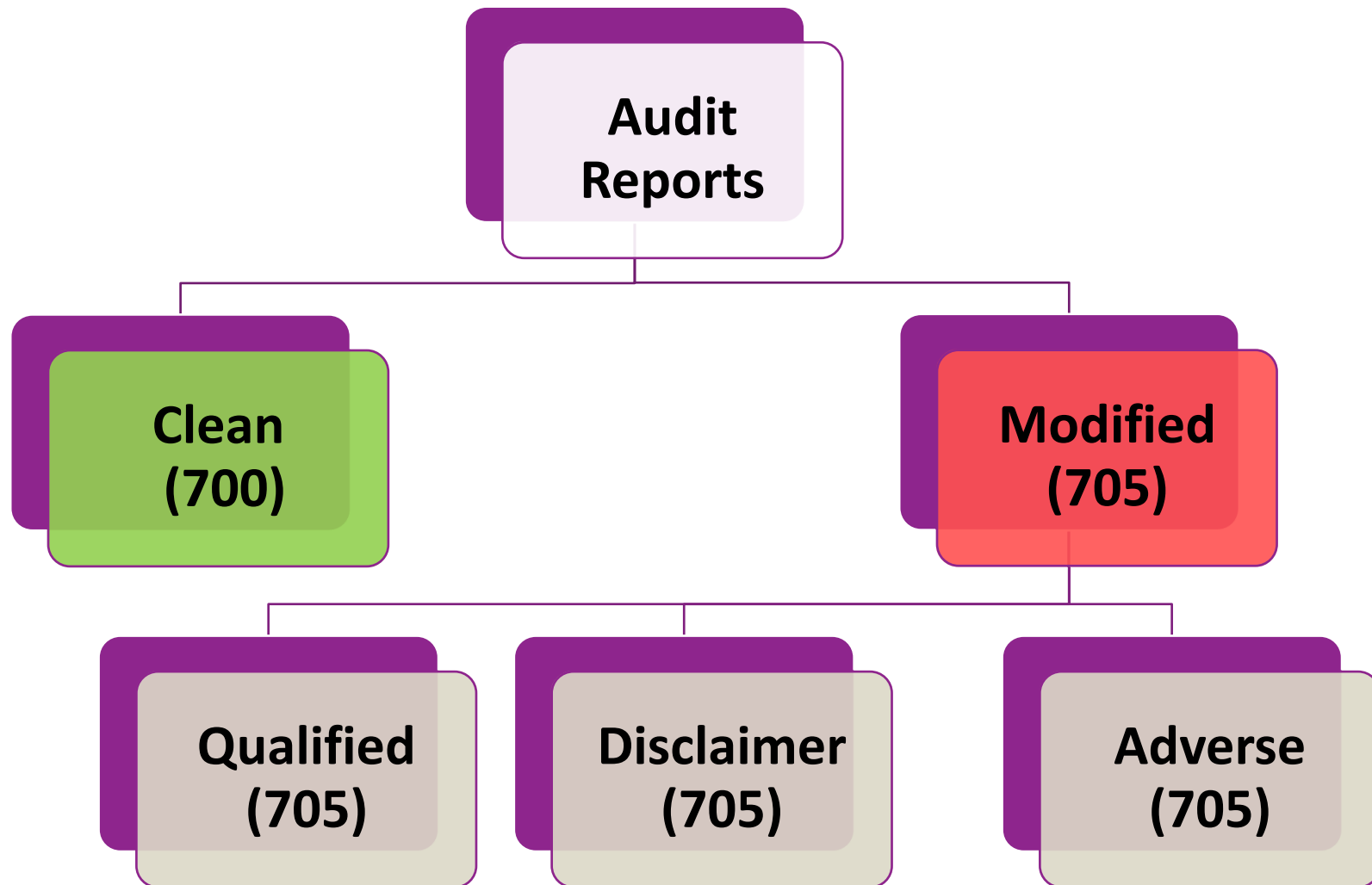
List of Standards on Auditing on Reporting

S.A. 700-799 “Audit Conclusions and Reporting”

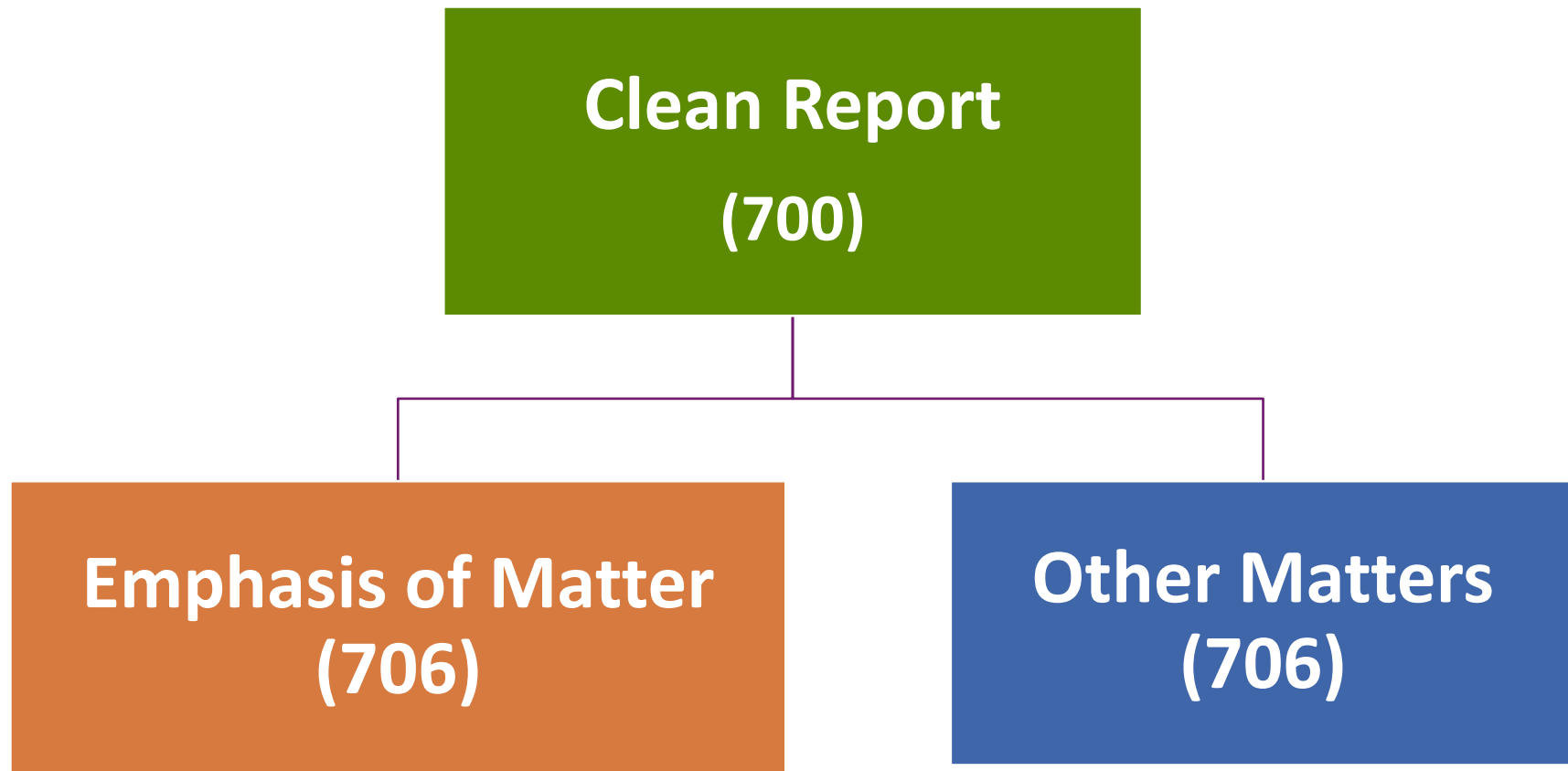
700 (R)	Forming an Opinion and Reporting on Financial Statements
701	Communicating Key Audit Matters in the Independent Auditors Report.
705 (R)	Modifications to the Opinion in the Independent Auditor’s Report
706 (R)	Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report
710	Comparative Information—Corresponding Figures and Comparative Financial Statements
720 (R)	The Auditor’s Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements

Effective for audits of FS for periods beginning on or after 1st April 2018. *(ICAI has issued Implementation Guide for 700, 701, 705, 706)*

Statutory Audit Reports



Statutory Audit Reports ...



Auditor's Report

Elements of Audit Report:

- Title
- Addressee
- Introductory Paragraph
- Management's Responsibility for the FS
- Auditor's Responsibility
- Auditor's Opinion
- Other Reporting Responsibilities
- Signature of the Auditor
- Date of Auditor's Report
- Place of Signature

Some commonly observed errors in Audit reports

- Modified vs. Clean Reports
- Qualification vs. Disclaimer vs. Adverse opinion
- EoM vs. Modified opinion
- Modification or EoM should be self explanatory (should also refer to the appropriate note in FS)
- In case of any modification in the AR, the portion on “Report on Other Legal and Regulatory Requirements” will also need to be appropriately modified
- CARO Reporting should be specific (and not vague)
- ICFR Reporting should be specific – cannot have EoM or OM but can be a modified report

New and Revised Auditor's Reporting Standards

Umbrella Standard for Audit Reporting – SA 700 (Revised)

↕

New Key
Audit
Matters
section SA
701

↕

Modifications
to auditor's
opinions SA
705 (revised)

↕

Enhanced
auditor
reporting
related to
going concern
SA 570 revised

↕

New auditor
reporting on
other
information SA
720 (revised)

Revisions to SAs 260 and 706 as a result of SA 701, and related
conforming amendments to SAs 210, 220, 230, 510, 540, 600, 710

Key Amendments

- Prominent placement of the **“Auditor’s Opinion”** towards the beginning of the Auditor’s Report.
- New descriptions of **responsibilities relating to Going Concern** to be included in the respective sections for **Management Responsibility Paragraph** and **Auditors Responsibilities Paragraph**
- **Key Audit Matters**
- Under para “Basis of Opinion”; a statement that the **auditor is independent** of the entity in accordance with the relevant ethical requirements relating to the audit.
- Management Responsibility [**new clauses**]
- Auditors’ Responsibility [**new clauses**]
- *SA 700 Revised also applies to audits for which SA 800 or SA 805 apply.*

Presentation of Auditor's Report

SA 700 Revised (w.e.f. 1-4-2018)

- ✓ Title
- ✓ Addressee
- ✓ **Auditor's Opinion**
- ✓ Basis for Opinion
- ✓ **Going Concern**
- ✓ **Key Audit Matters**
- ✓ **Management's Responsibility**
- ✓ **Auditor's Responsibility**
- ✓ Other Reporting Responsibilities
- ✓ Date, Place of Signature

SA 700 (existing)

- ✓ Title
- ✓ Addressee
- ✓ Introductory Paragraph
- ✓ Management's Responsibility
- ✓ Auditor's Responsibility
- ✓ Auditor's Opinion-
- ✓ Other Reporting Responsibilities
- ✓ Date, Place of Signature

Auditor's Report

Basis of Opinion: *(earlier under auditor's responsibility statement)*

The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that:

- a) States that the audit was conducted in accordance with SAs
- b) Refers to the section of the auditor's report that describes the auditor's responsibilities under the SAs;
- c) Includes a statement that the auditor is independent of the entity in accordance with the relevant ethical requirements relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall refer to the Code of Ethics issued by ICAI*
- d) States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

Auditor's Report ...

Responsibilities of Management for the Financial Statements

- This section of the auditor's report shall describe management's responsibility for:
 - a) Preparing the financial statements in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
 - b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate.
- This section shall also identify those responsible for the oversight of the financial reporting process, when those responsible for such oversight are different from those who fulfill the responsibilities described as above.

Auditor's Report ...

Auditors' Responsibilities

- Shall state that the objectives of the auditor are to :
 - (a) obtain reasonable assurance about whether the financial statement as a whole are free from material misstatement, whether due to fraud or error.
 - (b) Issue an auditor's report that includes the auditor's opinion.
- State that reasonable assurance is a high level of assurance, **but is not a guarantee** that an audit conducted in accordance with SAs will always detect a material misstatement if it exists
- State that misstatements can arise from fraud or error, and either
 - describe that they are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users or
 - **provide a definition or description of materiality in accordance with the applicable financial reporting framework.**
- When SA 600 applies, further describe the auditor's responsibilities in a group audit engagement by stating:
"The division of responsibility for the financial information of the entity by indicating the extent to which the financial information of components is audited by the other auditors have been included in the financial information of the entity, e.g., the number of divisions/branches/subsidiaries or other components audited by other auditors"

Auditor's Report ...

Auditors' Responsibilities

- Shall state that the auditor exercises professional judgment and maintains **professional skepticism** throughout the audit.
- The auditor shall describe that the auditor's responsibilities are :
 - To identify and assess the risk of material misstatement
 - To design and perform audit procedures responsive to those risks
 - To obtain audit evidence that is sufficient and appropriate to provide basis for the auditor's opinion.
 - To obtain an understanding of internal control relevant to the audit
 - To evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
 - To conclude on the appropriateness of management's use of the going concern basis of accounting
 - To evaluate the overall presentation, structure and content of the financial statements, including the disclosures.

Auditor's Report ...

Auditors' Responsibilities

- State that the auditor communicates with those charged with governance regarding the planned scope and timing of the audit and significant audit findings, including any significant deficiencies identified in internal control.
- State that the auditor provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements
- For all such entities for which key audit matters are communicated in accordance with SA 701, state that, from the matters communicated with those charged with governance, the auditor determines those matters that were of most significance in the audit.

Note: The description of the auditor's responsibilities shall be located:

- within the body of the auditor's report.
- Within an appendix to the auditor's report
- By a specific reference within the auditor's report to the location of such a description on a website of an appropriate authority

Applicability of SA 701

- Applicable in case of audits of complete sets of general purpose Financial Statement. **w.e.f. 1st April, 2018.** The FS should be general purpose **Financial Statements** and complete set of **Financial Statement**.
- SA 701 is **mandatorily** applicable in case of audits of **listed entities**.
- Also **applicable in case of audits of unlisted entities in following situations:**
 - Where auditor decides to communicate KAM voluntarily or at the request of TCWG / Management;
 - Where auditor is required by law or regulation to communicate KAM

What are Key Audit Matters (KAM)

Definition:

- Those matters which in the auditor's **Professional Judgement**, were of most **significance** in the audit of FS of the current period
- KAMs are **selected** from the matters communicated with TCWG

Determining KAMs:

- Those matters which required significant auditor attention in performing the audit
- Areas of **higher RMM assessed or significant risks** identified as per SA 315
- Effect of **significant events/ transactions** on audit
- Significant auditor judgments relating to areas that involved **significant management judgments**

Decision – making framework for KAM



What are KAM ...

Step 1:

- Matters communicated with those charged with governance
SA 260-265

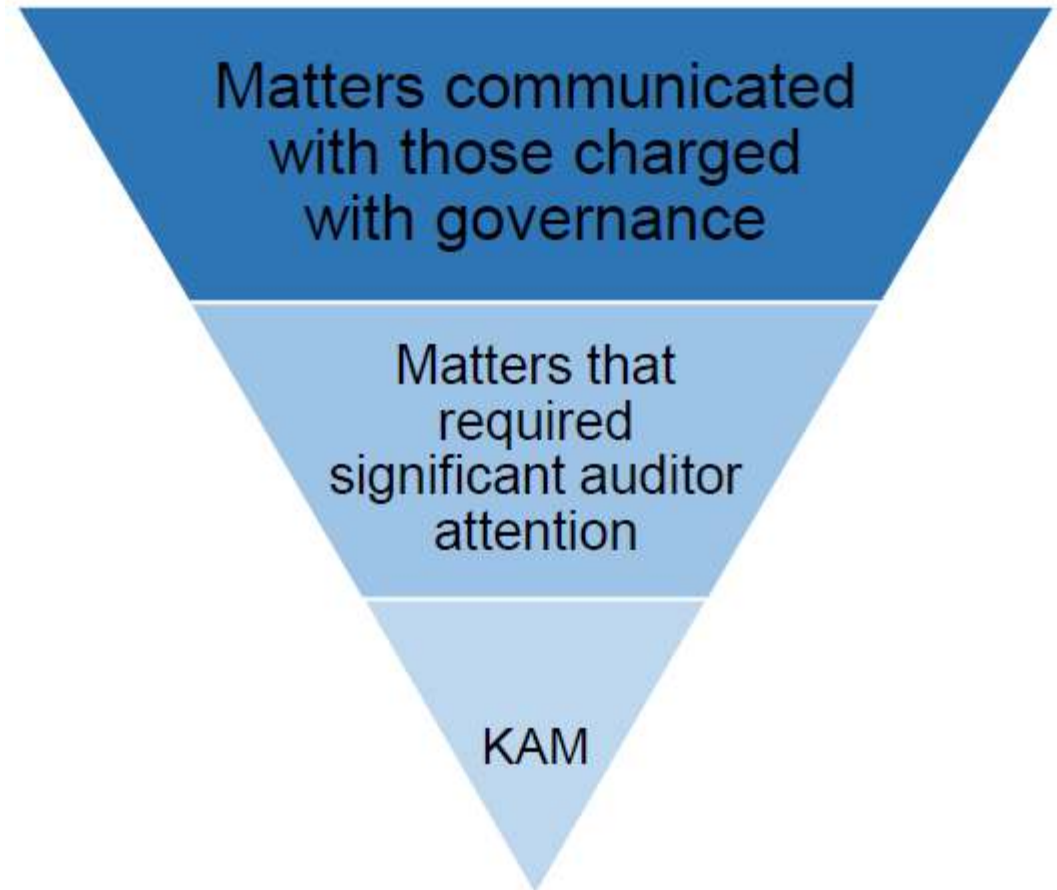
Step 2:

- Matters that required significant auditor attention **SA 315**

Step 3:

- Matters that were of most significance in the audit of the current period.

Selection of KAM-Funnel Approach



What are KAMs ...

Communicating KAM not a substitute for:

- Disclosures required in the FS as per the applicable financial reporting framework.
- Disclosures necessary to achieve fair presentation of the FS.
- Requirement of expressing modified opinion in accordance with revised SA 705.
- Requirement of reporting about material uncertainty relating to going concern in accordance with revised SA 570.

What are KAMs ...

How to Communicate KAM

- Using an appropriate sub-heading “KAM the auditor shall describe each KAM with reference to the related disclosures and explain:
- Why the matter was considered to be one of the most significant ;and
- How the matter was addressed in the audit

Illustrative paragraph of key audit matters:

“Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.”

[Description of each key audit matter in accordance with SA 701]

What are KAMs ...

Description of Individual KAM:

- Key Audit Matters – Manner in which described in the Audit Report
- Adequacy of description of a KAM is matter of Professional judgement
- **Description of each KAM should cover following 3 aspects:**
 - reference to the related disclosures(if any) in FS
 - Why matter was considered to be one of most significance in audit and therefore determined as KAM
 - How the matter was addressed in the audit
- **In description of how the matter was addressed, auditor may cover following aspects:**
 - auditor's response or approach to address the matter
 - A brief overview of procedures performed
 - An indication of the outcome of the auditor's procedures
 - Auditor's Key observations with respect to the matter

Illustrations of KAM ...

Subject matters covered by KAMs	No. of Companies Reported KAM	Percentage to Total 180 companies
Assets Impairments (other than goodwill)	162	90%
Revenue (not mentioning fraud)	102	57%
Allowance for doubtful debts	95	53%
Goodwill impairment	90	50%
Taxation, including deferred tax	88	49%
Investments	87	48%
Financial instruments	84	47%
Valuation of inventories	80	44%
Property valuation	79	44%
Insurance	55	31%
Fixed assets, including depreciation	41	23%
Acquisitions and disposals	39	22%

Illustrations of KAM ...

Subject matters covered by KAMs	No. of Companies Reported KAM	Percentage to Total 180 companies
Going Concern	34	19%
Legal Provisions	31	17%
IT-related issues	29	16%
Provisions other than legal	29	16%
Accounting for long-term contracts	26	14%
Mining/Oil & Gas accounting	18	10%
Equity and capital	17	9%
Management override / related parties	17	9%
Fraud in revenue recognition	16	9%
Development Costs	12	7%
Pensions	12	7%
Biological assets	10	6%

Illustrations of KAM ...

Subject matters covered by KAMs	No. of Companies Reported KAM	Percentage to Total 180 companies
Leases	10	6%
Consolidation Issues	9	5%
Assets held for sale	8	4%
Contingent liabilities	8	4%
Hyper inflation	6	3%
Restatement / re-presentation	5	3%
Share-based payments	5	3%
Controls / Regulations	4	2%
Change in accounting policy	4	2%
Supplier Rebates, discounts, incentives	4	2%
Exceptional	3	2%
Accruals	3	2%

Auditors Reporting

ICAI Advisory on Auditor's Reporting on Section 197(16) of the Companies Act, 2013 dated 9th September 2019

- Section 197(16) of the Companies Act, 2013 requires that *'The auditor of the company shall, in his report under Section 143, make a statement as to whether the remuneration paid by the company to its directors is in accordance with the provisions of this Section, whether remuneration paid to any director is in excess of the limit laid down under this Section and give such other details as may be prescribed'*.
- The aforesaid reporting requirement for auditors of public companies needs to be covered in auditor's report under the Section "Report on Other Legal and Regulatory Requirements". Accordingly, auditors of public companies are advised to comply with the aforesaid reporting requirements in their auditor's reports.
- This Advisory **came into force from immediate effect**

Use of Electronic Signatures

- Announcement of AASB of ICAI dated 13 April 2020
 - Paragraph 46 of SA 700(Revised), “Forming an Opinion and Reporting on Financial Statements”. Para A57 containing application guidance of SA 700(Revised) states as under: *“In some cases, law or regulation may allow for the use of electronic signatures in the auditor’s report.”*
 - AASB also examined provisions of the Information Technology Act, 2000
 - *Accordingly, the members of ICAI may use electronic signature for signing audit reports, all reports issued pursuant to any attestation engagement and certificates.*
 - However, the members need to ensure compliance with all the requirements relating to signature prescribed in the relevant law or regulation, Standards on Auditing and relevant announcements/ clarifications issued by ICAI on the matter including the requirement to mention UDIN.
 - *Requirement to mention UDIN is applicable both for manually and digitally signed reports/certificates including certificates uploaded online.*

Communication with retiring auditor

- **Announcement dated 1st May 2020**
 - Due to the existing constraint of communication through abovementioned modes, it has been decided that the members may **communicate with the Retiring Auditor vide E-mail, provided an acknowledgement of such communication is received from the Retiring Auditor's E-mail address registered with the Institute or his last known official E-mail address.**
 - Such acknowledgement of communication would be deemed as valid evidence of positive delivery of communication.

Advisories issued by ASB and AASB for impact of Covid-19 on financial reporting and auditing

Date	Particulars
27 March 2020	Impact of Novel Corona Virus (COVID-19) on Audit of Financial Statements for the FY ending March 31, 2020
April 2020	COVID-19 FAQs on Ind AS
6 May 2020	Advisory for Statutory Bank Branch Auditors
10 May 2020	Going Concern - Key Considerations for Auditors amid COVID-19
13 May 2020	Physical Inventory Verification – Key Audit Considerations amid COVID-19
17 May 2020	Auditor's Reporting - Key Audit Considerations amid COVID-19
23 May 2020	Subsequent Events - Key Audit Considerations amid COVID-19

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Auditing aspects

Development in Standards on Auditing

- Implementation Guide (IG) to SA 720 (revised) “The Auditors’ Responsibilities relating to other information” (Aug 2019)
- IG to SA 570 (revised) “Going Concern” (Aug 2019)
- MCQs on Engagement and Quality Control Standards (June 2020) (Covers all 46 SAs)

Auditing aspects to consider due to Covid-19

- Inventory
 - Property, Plant and Equipment
 - Borrowing Costs
 - Impairment of Non-financial assets
 - Provisions, contingent liabilities and contingent assets
 - Financial Instruments – MTM, ECL, Impairment of investments, etc.
 - Leases
 - Revenue Recognition (cut-off dates, etc.);
 - Income Taxes
 - Employee benefits – esp. retirement benefits
 - Subsequent events
 - Government Grants
 - Exceptional items
 - Going Concern
-
- WFH related scope limitations

Thank you!

A close-up photograph of a hand holding a black marker, completing the cursive phrase 'Thank you!' on a white surface. The hand is positioned on the right side of the frame, with the index and thumb fingers visible, gripping the marker. The marker's tip is just finishing the exclamation mark. The background is a plain, bright white.

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