

## CA Final "Advanced Auditing" - List of important Topics Quality Control and Engagement Standards

SQC 1	Engagement Performance.
SA 200	<ol style="list-style-type: none"> <li>1. Professional Skepticism.</li> <li>2. Scope of Audit</li> <li>3. Risk of Material Misstatements.</li> </ol>
SA 210	<ol style="list-style-type: none"> <li>1. Preconditions for an Audit</li> <li>2. Engagement letter in case of recurring audit.</li> <li>3. Acceptance of a change in terms of audit engagement.</li> </ol>
SA 220	<ol style="list-style-type: none"> <li>1. Acceptance and continuance of Client relationship and Audit Engagement.</li> <li>2. Engagement performance – Supervision, review and EOQR</li> </ol>
SA 230	<ol style="list-style-type: none"> <li>1. Factors affecting Form, content and Extent of Audit Documentation.</li> <li>2. Ownership of Working papers.</li> </ol>
SA 240	<ol style="list-style-type: none"> <li>1. Possible Sources of Misstatement.</li> <li>2. Fraud Risk factors.</li> <li>3. Auditor's duties w.r.t. prevention and detection of fraud.</li> <li>4. Risk Assessment procedures – Inquiring management and others within entity.</li> </ol>
SA 250	<ol style="list-style-type: none"> <li>1. Management Responsibility for compliance with laws and Regulation.</li> <li>2. Auditors consideration of compliance with laws and regulation.</li> <li>3. Audit procedure when noncompliance is identified or suspected.</li> <li>4. Reporting of identified or suspected noncompliance.</li> <li>5. Indicators to be considered while verifying compliance with laws and regulations.</li> </ol>
SA 260	<ol style="list-style-type: none"> <li>1. Matters to be communicated.</li> <li>2. Factors affecting mode of communication</li> </ol>
SA 265	<ol style="list-style-type: none"> <li>1. Identification of deficiencies in internal control.</li> <li>2. Indicators of significant deficiencies.</li> <li>3. Communication of deficiencies in internal control and content of communication.</li> </ol>
SA 299	<ol style="list-style-type: none"> <li>1. Responsibility of Joint Auditors</li> <li>2. Reporting Responsibilities.</li> </ol>
SA 300	<ol style="list-style-type: none"> <li>1. Planning – A Continuous Process.</li> <li>2. Establishing Audit Strategy.</li> <li>3. Changes to Planning Decisions.</li> <li>4. Additional Considerations in Initial Audit Engagement.</li> </ol>
SA 315	<ol style="list-style-type: none"> <li>1. RAP – Understanding required of Entity and its environment.</li> <li>2. Assessment of Risk of Material Misstatement – At F.S. level.</li> <li>3. Risks that require Special Consideration.</li> <li>4. Areas to be examined for deficiencies and risk identification in IT Environment.</li> <li>5. Risk to Internal Control imposed by IT.</li> </ol>
SA 320	<ol style="list-style-type: none"> <li>1. Use of Benchmark in determining Materiality.</li> <li>2. Revision as Audit progresses.</li> <li>3. Materiality and Audit risk.</li> </ol>
SA 330	<ol style="list-style-type: none"> <li>1. Auditor's procedures responsive to Assessed RMM.</li> <li>2. Factors warranting re-test of controls.</li> <li>3. Areas where external confirmation may be used.</li> <li>4. Factors assisting the auditor in determining use of external confirmation.</li> </ol>
SA 402	<ol style="list-style-type: none"> <li>1. Understanding of services provided by Service Organisation.</li> <li>2. Information w.r.t. controls at a Sub-service organisation.</li> </ol>
SA 450	<ol style="list-style-type: none"> <li>1. Causes of Misstatement.</li> <li>2. Consideration of identified misstatements and evaluating the effect of uncorrected misstatements.</li> </ol>
SA 500	<ol style="list-style-type: none"> <li>1. Evaluation of Work of Management Expert.</li> <li>2. Audit procedures and methods of obtaining audit evidence.</li> <li>3. Reliability of Audit evidence.</li> </ol>
SA 501	Audit procedures w.r.t. Inventory – complete topic
SA 505	<ol style="list-style-type: none"> <li>1. External Confirmation procedures.</li> <li>2. Audit procedures in Special Circumstances – all situations.</li> </ol>
SA 510	Audit procedures and reporting – Opening Balances.
SA 520	Auditor's procedure.

SA 530	<ol style="list-style-type: none"> <li>1. Sampling Risk.</li> <li>2. Sample Design, size and selection.</li> <li>3. Methods of Sample selection, Toleration misstatement and tolerable rate of deviation.</li> </ol>
SA 540	<ol style="list-style-type: none"> <li>1. Examples of fair value accounting estimates.</li> <li>2. Examples of estimates with low and high estimation uncertainties.</li> <li>3. Risk Assessment procedure and Related Activities.</li> </ol>
SA 550	<ol style="list-style-type: none"> <li>1. Risk Assessment Procedure and Related Activities – complete topic</li> <li>2. Responses to Assessed Risks – complete topic.</li> <li>3. Possible sources for identification of related party information.</li> </ol>
SA 560	<ol style="list-style-type: none"> <li>1. Auditors procedures w.r.t. Events occurring between the date of financial statements and the date of Auditor's Report.</li> <li>2. Specific inquiries to be made from management.</li> </ol>
SA 570	<ol style="list-style-type: none"> <li>1. Additional Audit procedures when events or conditions are identified.</li> <li>2. Auditor's conclusions.</li> <li>3. Implications for Auditor's report.</li> <li>4. Events or conditions that may cast doubt about going concern assumption.</li> </ol>
SA 580	Auditor's duties when reliability of WR is doubtful or request WR not provided.
SA 600	Principal Auditor's procedure, reporting consideration and division of responsibility.
SA 610	<ol style="list-style-type: none"> <li>1. Scope of Internal Audit Function.</li> <li>2. Evaluating Internal Audit Function.</li> <li>3. Factors affecting objectivity, competency and approach.</li> <li>4. Determining whether, in which area and to what extent internal auditor can be used to provide direct assistance.</li> </ol>
SA 620	<ol style="list-style-type: none"> <li>1. Matters where auditor can use expert work.</li> <li>2. Factors suggesting need for detailed and written agreement with auditor's expert.</li> <li>3. Evaluating adequacy of expert's work.</li> <li>4. Reference to auditor's expert in the auditor's report.</li> </ol>
SA 700	Elements of Audit report.
SA 705	Circumstances in which modified opinion can be expressed and types of modified opinion.
SA 706	Meaning and Requirements of EOM Para.
SA 710	Corresponding Figures – Meaning, Audit Procedure and Reporting.
SA 720	Other Information – Meaning and Auditor's procedure.
SA 800	Engagement Acceptance Consideration. Considerations in Planning and Performing an Audit.
SA 805	Planning and performance Consideration.
SA 810	Engagement Acceptance Consideration. Nature of Procedures.
SRE 2400	<ol style="list-style-type: none"> <li>1. Engagement Level Quality Control</li> <li>2. Factors Affecting Acceptance and Continuance of Client Relationship.</li> <li>3. Preconditions for accepting a review Engagement.</li> <li>4. Designing and Performing procedures while performing Review Engagement.</li> <li>5. Practitioner Report.</li> </ol>
SRE 2410	<ol style="list-style-type: none"> <li>1. Procedures performed to update the understanding of entity and its environment.</li> <li>2. Examples of Analytical procedures that auditor may consider when performing review of IFI</li> </ol>
SAE 3400	<ol style="list-style-type: none"> <li>1. Acceptance of Engagement.</li> <li>2. Examination Procedures.</li> <li>3. Considerations in assessing the presentation and disclosure of PFI.</li> <li>4. Evidences to be obtained for reporting on PFI.</li> </ol>
SAE 3402	<ol style="list-style-type: none"> <li>1. Agreeing the terms of engagement - Acceptance and Continuance</li> <li>2. Assessing the suitability of Criteria.</li> <li>3. Elements of Assurance report.</li> </ol>
SAE 3420	<ol style="list-style-type: none"> <li>1. Engagement Acceptance</li> <li>2. Evaluating the presentation of Pro Forma Financial Information.</li> </ol>
SRS 4400	-
SRS 4410	<ol style="list-style-type: none"> <li>1. Objectives of Compilation Engagement</li> <li>2. Engagement Level Quality Control.</li> <li>3. Engagement Acceptance and Agreeing the terms of engagement.</li> <li>4. Performing the Engagement – Compiling the financial information.</li> <li>5. Practitioner Report.</li> </ol>

# Chapter 1 "Quality Control and Engagement Standards"

## SQC – 1 "Quality Control for Firms that Perform Audits & Reviews of Historical Financial Information, and Other Assurance & Related Services Engagements"

All firms to have system of quality control that provides reasonable assurance that: (a) Firm & personnel comply with professional standards, regulatory & legal requirements, and (b) Reports issued by firm or partners are appropriate in the circumstances.

Leadership Responsibilities for Q. C.	Ethical requirements	Independence	Client Acceptance/Continuance	Human Resources	Engagement Performance	Monitoring
<p>(a) Promote internal culture w.r.t.:</p> <ul style="list-style-type: none"> <li>essential of quality in engagements.</li> <li>Compliance with professional standards, regulatory / legal requirements.</li> <li>Issue of reports appropriate in circumstances.</li> </ul> <p>(b) Require CEO/ managing partner to assume ultimate responsibility for QC.</p> <p>(c) Recognise &amp; reward high quality work.</p>	<p>Establish policies &amp; procedures to reasonable assure that Firm &amp; personnel comply with relevant ethical requirements of</p> <ol style="list-style-type: none"> <li>Integrity.</li> <li>Objectivity.</li> <li>Professional competence &amp; due care.</li> <li>Confidentiality.</li> <li>Professional behaviour.</li> </ol>	<p>Policies &amp; procedures should enable:</p> <ul style="list-style-type: none"> <li>Communication of independence requirements to personnel &amp; others.</li> <li>Identification of circumstances threatening independence.</li> <li>Take appropriate action for elimination of threats / withdrawal from engagement.</li> <li>Resolution of breaches of independence.</li> </ul> <p><b><u>Maintenance of independence of personnel</u></b></p> <ul style="list-style-type: none"> <li>Engagement partners to provide firm with relevant information about client.</li> <li>Prompt notification of threats to independence.</li> <li>Accumulation &amp; communication of relevant information to appropriate personnel.</li> </ul>	<p>Establish policies/ procedures to reasonable assure that clients are accepted/ continued only where:</p> <ul style="list-style-type: none"> <li>Client integrity has been considered.</li> <li>Firm is competent to perform engagement w.r.t. capability, time &amp; resources.</li> <li>firm can comply with ethical requirements.</li> </ul>	<p>Establish policies / procedures to reasonable assure that:</p> <ul style="list-style-type: none"> <li>Firm has sufficient personnel with capabilities, competence &amp; commitment to ethical principles &amp;</li> <li>Responsibility of engagement partner clearly defined &amp; communicated to him/ her.</li> </ul>	<p>Establish policies / procedures to reasonable assure w.r.t.:</p> <ul style="list-style-type: none"> <li>Compliance with professional standards.</li> <li>Compliance with laws/ regulations.</li> <li>Engagement partner issues reports that are appropriate in the circumstances.</li> </ul> <p><b>Important aspects of engagement performance</b></p> <ul style="list-style-type: none"> <li>Supervision.</li> <li>Review.</li> <li>Consultation.</li> <li>Differences of opinion.</li> <li>Engagement Q. C. review.</li> <li>Engagement documentation.</li> </ul>	<p>Establish Policies &amp; procedures to reasonable assure that QC policies/ procedures are:</p> <ul style="list-style-type: none"> <li>Relevant.</li> <li>Adequate.</li> <li>Operating effectively.</li> <li>Complied with in practice.</li> </ul>

## SRE 2400 (Revised) "Engagements to Review Historical Financial Statements"

**Scope of SRE 2400:** It deals with practitioner responsibilities when engaged to perform a review of Historical F.S. when the practitioner is the auditor of the entity.  
**Objectives of Practitioner:** to obtain limited assurance primarily by performing Inquiry and Analytical Procedures about whether the F.S. as a whole are free from material misstatements.

### Acceptance Considerations

- |          |  |
|----------|--|
| <b>1</b> | <b>Factors affecting acceptance</b>  |
|          | <p>Unless required by law or regulation, the practitioner shall not accept review engagement if:</p> <ul style="list-style-type: none"> <li>(a) The practitioner is not satisfied that there is a rational purpose for the engagement.</li> <li>(b) Practitioner has reason to believe that relevant ethical requirements, including independence, will not be satisfied;</li> <li>(c) Practitioner's preliminary understanding of the circumstances indicates that information needed to perform the review engagement is likely to be unavailable or unreliable;</li> <li>(d) The practitioner has cause to doubt management's integrity such that it is likely to affect proper performance of the review; or</li> <li>(e) Management or TCWG impose a limitation on the scope of the practitioner's work.</li> </ul>   |
| <b>2</b> | <b>Preconditions for accepting review engagement</b>   |
|          | <p>Before acceptance, the practitioner shall:</p> <ul style="list-style-type: none"> <li>(a) Determine whether the FRF applied in the preparation of the F.S. is acceptable.</li> <li>(b) Obtain agreement of mngt. that it acknowledges &amp; understands its responsibilities:                             <ul style="list-style-type: none"> <li>(i) For preparation of the F.S. as per FRF;</li> <li>(ii) For necessary internal control to enable the preparation of F.S. that are free from material misstatement; and</li> <li>(iii) To provide the practitioner with:                                     <ul style="list-style-type: none"> <li>a. Access to all information which is relevant to the preparation of F.S.;</li> <li>b. Additional information that he may request from mngt. for review; and</li> <li>c. Unrestricted access to persons within the entity from whom he determines it necessary to obtain evidence.</li> </ul> </li> </ul> </li> </ul> |

### Procedures to be performed

- The practitioner's inquiries of management and others within the entity, shall include the following:
- (a) How management makes the significant accounting estimates required under the applicable FRF;
  - (b) Identification of related parties & related party transactions, including purpose of those transactions;
  - (c) Whether there are significant, unusual or complex transactions, that may affect the entity's F.S., including:
    - (i) Significant changes in entity's business activities;
    - (ii) Significant changes to the terms of contracts;
    - (iii) Significant journal entries or other adjustments;
    - (iv) Significant transactions occurring near the end of the reporting period;
    - (v) Uncorrected misstatements identified; and
    - (vi) Effects or possible implications of transactions or relationships with related parties;
  - (d) The existence of any actual, suspected or alleged:
    - (i) Fraud or illegal acts affecting the entity; and
    - (ii) Non-compliance with laws and regulations;
  - (e) Whether mngt. has identified events occurring between date of F.S. and the date of the practitioner's report that require adjustment or disclosure;
  - (f) Basis for management's assessment of the entity's ability to continue as a going concern;
  - (g) Events or conditions that appear to cast doubt on the entity's ability to continue as a going concern;
  - (h) Material commitments, contractual obligations or contingencies; and
  - (i) Material non-monetary transactions or transactions for no consideration.
- In designing analytical procedures, the practitioner shall consider whether the data from the entity's accounting system and accounting records are adequate for the purpose of performing the analytical procedures.

### Practitioner's Report

- It shall be in writing, and shall contain the following elements:
- (a) Title, indicating report of independent practitioner for a review engagement;
  - (b) The addressee(s).
  - (c) Introductory paragraph that identifies F.S. reviewed & states that F.S. have been reviewed;
  - (d) Description of responsibility of management for the preparation of F.S.
  - (e) If the F.S. are special purpose F.S., a description of the purpose for which the F.S. are prepared and the intended users.
  - (f) Description of practitioner responsibility to express a conclusion on the F.S.
  - (g) Description of review of F.S. & its limitations, & the following statements:
    - review engagement under this SRE is a limited assurance engagement;
    - Practitioner performs procedures, consisting of making inquiries of mngt. and others and applying analytical procedures. and
    - The procedures performed are substantially less than those performed in an audit and accordingly, the practitioner does not express an audit opinion;
  - (h) "Conclusion" that contains:
    - (i) The practitioner's conclusion on the financial statements as a whole, as appropriate; and
    - (ii) A reference to the applicable FRF used to prepare the F.S.
  - (i) The date of the practitioner's report;
  - (j) The practitioner's signature; and
  - (k) The place of signature.

## SRE 2410 (Revised) "Review of Interim Financial Information performed by Independent Auditor of the Entity"

**Scope of SRE 2410:** It deals with auditor responsibilities when engaged to perform a review of Interim financial information (IFI) of the entity.

**Objectives of Auditor:** to express a conclusion whether on the basis of review anything has come to his attention that causes him to believe that IFI is not prepared in all material respects in accordance with applicable FRF.

### Procedures performed to update the understanding of the entity

1. Reading documentation, to the extent necessary, of the preceding year's audit and reviews of prior interim period(s) of the current year and corresponding interim period(s) of the prior year, to enable the auditor to identify matters that may affect the current-period IFI.
2. Reading the most recent annual and comparable prior period IFI.
3. Considering any significant risks, including the risk of management override of controls, that were identified in the audit of the prior year's FS.
4. Considering materiality with reference to the applicable FRF as it relates to IFI to assist in determining nature and extent of procedures to be performed and evaluating effect of misstatements.
5. Considering the nature of any corrected material misstatements and any identified uncorrected immaterial misstatements in the prior year's FS.
6. Considering significant financial accounting & reporting matters that may be of continuing significance such as material weaknesses in I.C.
7. Considering results of any audit procedures performed with respect to the current year's FS.
8. Considering results of any internal audit performed and the subsequent actions taken by management.
9. Inquiring of management about the results of management's assessment of the risk that the IFI may be materially misstated as a result of fraud.
10. Inquiring of management about the effect of changes in the entity's business activities.
11. Inquiring of management about any significant changes in internal control and the potential effect of any such changes on the preparation of IFI.
12. Inquiring of management of the process by which the IFI has been prepared and the reliability of the underlying accounting records to which the IFI is agreed or reconciled.

### Examples of Analytical procedures that may be performed in review of IFI

1. Comparing the IFI with the IFI information of the immediately preceding interim period.
2. Comparing current IFI with anticipated results, such as budgets or forecasts
3. Comparing current IFI with relevant non-financial information.
4. Comparing the recorded amounts, or ratios developed from recorded amounts, to expectations developed by the auditor.
5. Comparing ratios and indicators for the current interim period with those of entities in the same industry.
6. Comparing relationships among elements in the current IFI with corresponding relationships in the IFI of prior periods, for example, expense by type as a %age of sales, assets by type as a percentage of total assets, and percentage of change in sales to percentage of change in receivables.
7. Comparing disaggregated data. Examples are:
  - By period, for example, revenue or expense items disaggregated into quarterly, monthly, or weekly amounts.
  - By product line or source of revenue.
  - By location, for example, by component.
  - By attributes of the transaction.

**Compiled by: CA. Pankaj Garg**

# SAE 3400 "Examination of Prospective Financial Information (PFI)"

## Meaning and Types of PFI

<b>1</b>	<b>Meaning of PFI</b>
	<ul style="list-style-type: none"> <li>Financial information based on assumptions about events that may occur in the future.</li> <li>Highly subjective in nature &amp; requires judgment in preparation.</li> </ul>
<b>2</b>	<b>Types of PFI</b>
<b>Forecast</b>	PFI prepared on the basis of assumptions as to future events which management expects to take place. (Best-estimate assumptions).
<b>Projection</b>	PFI prepared on basis of hypothetical assumptions about future events which are not necessarily expected to take place or a mixture of best-estimate & hypothetical assumptions.
<b>3</b>	<b>Management Responsibility</b>
	<p>Mngt is responsible for preparation of PFI including</p> <ul style="list-style-type: none"> <li>Identification and disclosure of PFI;</li> <li>The basis of forecast;</li> <li>Underlying assumptions.</li> </ul>
<b>4</b>	<b>Auditor's Responsibility</b>
	<ul style="list-style-type: none"> <li>To examine and report on PFI.</li> <li>Related to events &amp; actions that have not yet occurred and might not occur.</li> <li>Evidence are future oriented and thus speculative.</li> <li>Auditor is not in a position to express opinion as to whether the results shown in PFI will be achieved.</li> <li>He can provide only moderate assurance (Negative assurance)</li> </ul>

## Acceptance of Engagement

Before accepting an engagement to examine PFI, the auditor would consider, amongst other things:

1. the intended use of the information;
2. whether the information will be for general or limited distribution;
3. the nature of the assumptions, that is, whether they are best-estimates or hypothetical assumptions;
4. the elements to be included in the information; and
5. the period covered by the information.

Auditor should not accept, or should withdraw from, an engagement when assumptions are clearly unrealistic or when auditor believes that PFI will be inappropriate for its intended use.

## Examination Procedures

When determining NTE of examination procedures, auditor should consider matters such as:

1. knowledge obtained during any previous engagements;
2. Mngt competence regarding preparation of PFI;
3. the likelihood of material misstatement;
4. the extent to which PFI is affected by mngt judgment;
5. the sources of information considered by the mngt for the purpose, their adequacy, reliability of the underlying data, including data derived from third parties, to support the assumptions;
6. the stability of entity's business; and
7. the engagement team's experience with the business and the industry in which the entity operates and with reporting on prospective financial information.

## Considerations in assessing the presentation and disclosure of PFI

When assessing presentation & disclosure of PFI, the auditor will need to consider whether:

1. presentation of PFI is informative and not misleading;
2. accounting policies are clearly disclosed in notes to PFI;
3. the assumptions are adequately disclosed in the notes;
4. the date as of which the PFI was prepared is disclosed;
5. the basis of establishing points in a range is clearly indicated; and
6. there is any change in the accounting policy of the entity from that disclosed in the most recent historical F.S. and whether reason for the change and the effect of such change on the PFI has been adequately disclosed.

## Evidences to be obtained for reporting on PFI

Auditor should document matters, which are important in providing evidence to support his report on examination of PFI, and evidence that such examination was carried out. Audit evidence in form of working papers will include:

- (1) the sources of information,
- (2) basis of forecasts,
- (3) the assumptions made in arriving the forecasts,
- (4) hypothetical assumptions, evidence supporting assumptions,
- (5) Mngt representations regarding intended use & distribution of the information, completeness of material assumptions,
- (6) Mngt acceptance of its responsibility for the information,
- (7) audit plan,
- (8) NTE of examination procedures performed, and,
- (9) in case the auditor expresses a modified opinion or withdraws from the engagement, the reasons forming the basis of such decision.

**Compiled by: CA. Pankaj Garg**

## SAE 3402 "Assurance Reports on Controls at a Service Organisation"

**Scope of SAE 3402:** It deals with assurance engagement undertaken by a member of ICAI to provide a report on controls at a service organization (SO) for use by user entities & their auditors. It complements SA 402.

**Objectives:** To obtain reasonable assurance w.r.t. description, design and operating effectiveness of controls established in the service organization.

### Acceptance Considerations

Before agreeing to accept, service auditor shall:

- (a) Determine whether:
  - (i) He has the capabilities and competence to perform the engagement;
  - (ii) Criteria to be applied by the SO to prepare the description of its system will be suitable and available to user entities and their auditors; and
  - (iii) Scope of engagement and SO description of its system will not be so limited that they are unlikely to be useful to user entities & their auditors.
- (b) Obtain the agreement of the SO that it acknowledges and understands its responsibility:
  - (ii) For preparation of the description of its system;
  - (iii) To have a reasonable basis for the SO assertions accompanying the description of its system;
  - (iv) For stating in the assertions, the criteria it used to prepare the description of its system;
  - (v) For stating in the description of its system, the control objectives and party who specified them;
  - (vi) For identifying the risks that threaten achievement of the control objectives and designing and implementing controls to provide reasonable assurance that those risks will not prevent achievement of the control objectives; &
- (vii) To provide the service auditor with:
  - (a) Access to all relevant information;
  - (b) Additional information that the service auditor may request from the SO; and
  - (c) Unrestricted access to persons within the SO from whom he determines it necessary to obtain evidence.

### Assessing the Suitability of Criteria

**Criteria:** Benchmarks used to evaluate or measure a subject matter.

In assessing the suitability of criteria to evaluate the SO description of its system, the service auditor shall determine if the criteria encompass, at a minimum:

- (a) Whether the description presents how the SO system was designed & implemented, including, as appropriate:
  - The types of services provided.
  - The procedures, by which services are provided.
  - The related records and supporting information, including accounting records, supporting information and specific accounts that are used to initiate, record, process and report transactions.
  - How the SO system deals with significant events and conditions, other than transactions;
  - The process used to prepare reports and other information for user entities;
  - The specified control objectives and controls designed to achieve those objectives;
  - Complementary user entity controls contemplated in the design of the controls; and
  - Other aspects of the SO control environment, risk assessment process, information system and communication, control activities and monitoring controls that are relevant to the services provided.
- (b) In the case of a type 2 report, whether the description includes relevant details of changes to the SO system during the period covered by the description.
- (c) Whether the description omits or distorts information relevant to scope of SO system being described, while acknowledging that the description is prepared to meet the common needs of a broad range of user entities.

### Elements of Assurance Report (Type 2)

Report on description, design and operating effectiveness of controls (Commonly known as Type 2 Report) includes:

- (a) A title that clearly indicates the report is an independent service auditor's assurance report.
- (b) An addressee.
- (c) Identification of SO description of its system.
- (d) Identification of the criteria, and the party specifying the control objectives.
- (e) A statement that the report is intended only for user entities and their auditors.
- (f) A statement that the SO is responsible for preparing the description of its system, including the completeness, accuracy & method of presentation of that description.
- (g) A statement that the service auditor's responsibility is to express an opinion on the SO description, design and operating effectiveness of those controls.
- (h) A statement that the engagement was performed in accordance with SAE 3402.
- (i) Summary of procedures to obtain reasonable assurance.
- (j) A statement of the limitations of controls.
- (k) The service auditor's opinion, expressed in the positive form, on whether, in all material respects, based on suitable criteria:
  - The description fairly presents the SO system that had been designed and implemented throughout the specified period;
  - The controls related to the control objectives stated in the SO description of its system were suitably designed throughout the specified period; and
  - The controls tested, which were those necessary to provide reasonable assurance that the control objectives stated in the description were achieved, operated effectively throughout the specified period.
- (l) The date of the service auditor's assurance report.
- (m) Practitioner's Signature.
- (n) The place of signature.

# SAE 3420 "Assurance Engagements to report on the Compilation of Pro Forma Financial Information included in a Prospectus"

**Scope of SAE 3420:** It deals with reasonable assurance engagements undertaken by a practitioner to report on the responsible party compilation of pro forma financial information (PFI) included in a prospectus.

**Objectives:** To obtain reasonable assurance about whether the PFI has been compiled in all material respects on the basis of applicable criteria.

## Acceptance Considerations

- Before accepting an engagement, practitioner shall:
- Determine his capabilities & competence to perform the engagement;
  - Determine the suitability of applicable criteria;
  - Evaluate the wording of the opinion prescribed by the relevant L & R, if any, to determine that the practitioner will likely be able to express the opinion so prescribed;
  - Where the sources from which the unadjusted financial information have been extracted, have been audited or reviewed and a modified audit opinion or review conclusion has been expressed, consider whether or not the relevant L & R permits reference in the practitioner's report to, the modified audit opinion or review conclusion w.r.t. such sources;
  - If entity's historical financial information has not been audited or reviewed, consider whether the practitioner can obtain a sufficient understanding of the entity and its accounting and financial reporting practices to perform the engagement;
  - Obtain the agreement of the responsible party that it acknowledges its responsibility for:
    - Adequately disclosing and describing the applicable criteria to the intended users;
    - Compiling the PFI on basis of applicable criteria; &
    - Providing the practitioner with:
      - Access to all information.
      - Additional information that the practitioner may request from the responsible party;
      - Access to those within the entity.

## Planning and Performing

- Assessing the Suitability of the Applicable Criteria.**  
Practitioner shall assess suitability of applicable criteria & in particular determine that they include, at a minimum, that:
  - The unadjusted financial information be extracted from an appropriate source;
  - The pro forma adjustments be:
    - Directly attributable to the event or transaction;
    - Factually supportable; and
    - Consistent with the entity's applicable FRF; and
  - Appropriate presentation be made & disclosures be provided to enable the intended users to understand the information conveyed.
- Obtaining an understanding of how Responsible Party has Compiled the PFI.**
- Obtaining Evidence about appropriateness of Source from which Unadjusted Financial Information has been extracted**
- Obtaining Evidence about Appropriateness of the Pro Forma Adjustments**
- Obtaining Evidence about the Calculations within the PFI**
- Evaluating the Presentation of the PFI**  
It shall include consideration of:
  - Overall presentation and structure of the PFI, including whether it is clearly labeled to distinguish it from historical or other financial information;
  - Whether the PFI & related explanatory notes illustrate the impact of the event or transaction in a manner that is not misleading;
  - Whether appropriate disclosures are provided with the PFI to enable the intended users to understand the information conveyed; and
  - Whether the practitioner has become aware of any significant events subsequent to the date of the source from which the unadjusted financial information has been extracted that may require reference to, or disclosure in, the pro forma financial information.

## Elements of Assurance Report (Type 2)

- The practitioner's report shall include:
- A title – indicating independent assurance report;
  - An addressee(s), as agreed;
  - Introductory paragraphs that identify:
    - The pro forma financial information;
    - Source of unadjusted financial information;
    - The period covered by, or the date of, PFI; and
    - A reference to the applicable criteria;
  - A statement that the responsible party is responsible for compiling the PFI;
  - A description of the practitioner's responsibilities, w.r.t. expressing an opinion about whether the PFI has been compiled, on the basis of the applicable criteria;
  - A statement that the engagement was performed in accordance with SAE 3420.
  - Statements that:
    - Engagement involves performing procedures to assess whether the applicable criteria used provide a reasonable basis for presenting the significant effects directly attributable to the event or transaction;
    - The procedures selected depend on the practitioner's judgment; and
    - The engagement also involves evaluating the overall presentation of the PFI;
  - Practitioner's opinion using one of the following phrases, which are regarded as being equivalent:
    - The PFI has been compiled, in all material respects, on the basis of the (applicable criteria); or
    - The PFI has been properly compiled on the basis stated;
  - The practitioner's signature;
  - The date of the report; and
  - The place of signature.



## SRS 4400 "Engagements to perform Agreed Upon Procedures"

**Scope of Engagement:** In an engagement to perform agreed-upon procedures, the auditor is engaged by the client to issue a report of factual findings, based on specified procedures performed on specified subject matter of specified elements, accounts or items of a financial statement.

**Objective of Engagement:** To carry out procedure of audit nature, to which auditor, entity & any appropriate third parties have agreed & to report on factual finding thereon.

### General Principles of Engagement

Auditor should comply with Code of Ethics issued by ICAI. Ethical Principles are:

- (i) Integrity;
- (ii) Objectivity
- (iii) Professional competence and due care;
- (iv) Confidentiality;
- (v) Professional conduct; and
- (vi) Technical standard

**Note: Independence is not a requirement for agreed-upon procedures engagement, however, the terms or objective of the engagement may require the auditor to comply with the independence requirements of the Code of Ethics issued by the ICAI. Where the auditor is not independent, a statement to that effect should be made in the report of factual findings.**

### Defining the Terms of Engagement

There should be a clear understanding among the auditor, the client and other specified parties. The terms to be agreed include the following:

- (a) Nature of the engagement
- (b) Purpose
- (c) Identification of the financial information
- (d) Nature, timing and extent of the specific procedures
- (e) Limitation on distribution of the report of factual findings. If such limitation would be in conflict with the legal requirements, the auditor would not accept the engagement.

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### Reporting

The report of factual findings should contain:

- (a) Title;
- (b) Addressee
- (c) Identification of specific financial or not-financial information to which the agreed-upon procedures have been applied
- (d) A statement that the procedures performed were those agreed-upon with the recipient.
- (e) A statement that the engagement was performed in accordance with this standard & terms of engagement.
- (f) Identification of the purpose.
- (g) A listing of the specific procedures performed
- (h) A description of the auditor's factual findings including sufficient details of errors and exceptions found
- (i) A statement that the procedures performed do not constitute either an audit or a review and, as such, no assurance is expressed.
- (j) A statement that the report is restricted to those parties that have agreed to the procedures to be performed.
- (k) A statement (when applicable) that the report relates only to the elements specified and that it does not extend to the entity's F.S. as a whole
- (l) Date of the report
- (m) Place of signature
- (n) Auditor's signature.

**Report should be signed by the auditor in his personal name. Where the firm is appointed, the report should be signed in the personal name of the auditor and in the name of the firm. Also mention the membership number.**

## SRS 4410 "Compilation Engagement"

**Scope of SAE 4410: It deals with practitioner's responsibilities when engaged to assist management with the preparation and presentation of historical financial information without obtaining any assurance on that engagement.**

### Compilation Engagement

- It is an engagement in which a practitioner applies accounting and financial reporting expertise to assist management in the preparation and presentation of financial information of an entity in accordance with an applicable FRF, and reports as required by this SRS.
- The practitioner's objectives under this SRS are to:
  - (a) Apply accounting & financial reporting expertise to assist management in the preparation and presentation of financial information in accordance with an applicable FRF based on information provided by management; and
  - (b) Report in accordance with requirements of this SRS.
- Since a compilation engagement is not an assurance engagement, a compilation engagement does not require the practitioner to verify the accuracy or completeness of the information provided by management for the compilation, or otherwise to gather evidence to express an audit opinion or a review conclusion on preparation of the financial information.

### Mngt. Responsibility for Compilation Engagement

- While drafting letter of engagement, the practitioner shall include responsibilities of management for:
- (a) The financial information, and for the preparation and presentation thereof, in accordance with a FRF that is acceptable in view of the intended use of the financial information and the intended users;
  - (b) Design, implementation & maintenance of such internal control as mngt determines is necessary to enable the preparation of F.S. that are free from material misstatement, whether due to fraud or error;
  - (c) Accuracy & completeness of records, documents, explanations & other information provided by management for the compilation engagement; and
  - (d) Judgments needed in the preparation and presentation of the financial information.

### Quality control and Performing the Engagement

- 1 Engagement Level Quality Control**  
The engagement partner shall take **responsibility** for:
  - (a) Overall quality of engagement to which that partner is assigned; &
  - (b) Performing engagement in accordance with firm's quality control policies and procedures, by:
    - (i) Following appropriate procedures regarding the acceptance and continuance of client relationships and engagements;
    - (ii) Being satisfied that ET collectively has competence & capabilities to perform the compilation engagement;
    - (iii) Being alert for indications of non-compliance by members of the ET with relevant ethical requirements, and determining the appropriate action if matters come to the EP attention indicating that members of ET have not complied with relevant ethical requirements;
    - (iv) Directing, supervising and performing engagement in compliance with professional standards; and
    - (v) appropriate engagement documentation being maintained.
- 2 Performing the Engagement**
  1. Practitioner shall compile financial information using records, documents, explanations & other information, provided by mngt.
  2. If, practitioner becomes aware that records, documents, explanations or other information, are incomplete, inaccurate or not unsatisfactory, he practitioner shall bring that to the attention of management and request additional or corrected information.
  3. If mngt. failed to provide necessary information, as requested, he shall withdraw from the engagement and inform mngt and TCWG of the reasons for withdrawing.
  4. If the practitioner becomes aware that:
    - (a) The compiled financial information does not adequately refer to or describe the applicable FRF;
    - (b) Amendments to compiled financial information are required; or
    - (c) The compiled financial information is otherwise misleading, he shall propose the appropriate amendments to management.
  5. If mngt. declines, or does not permit him to make the proposed amendments to the compiled financial information, he shall withdraw and inform mngt/TCWG of the reasons for withdrawing.

### Practitioner Report

- Report shall be in writing, and include the following elements:
- (a) The report title;
  - (b) The addressee as required by terms;
  - (c) Statement that practitioner has compiled financial information based on information provided by mngt;
  - (d) Description of responsibilities of mngt, or TCWG, in relation to the compilation engagement, and financial information;
  - (e) Identification of the applicable FRF;
  - (f) Identification of the financial information, including the title and the date or the period to which it relates;
  - (g) Description of practitioner's responsibilities, including that the engagement was performed in accordance with this SRS.
  - (h) Explanations that:
    - Since compilation engagement is not an assurance engagement, the practitioner is not required to verify the accuracy or completeness of the information provided by management for the compilation; &
    - Accordingly, the practitioner does not express an audit opinion or a review conclusion.
  - (i) The date of the practitioner's report;
  - (j) The practitioner's signature; and
  - (k) The Place of signature.

## SA 200 (Revised) "Overall Objectives of the Independent Auditor & Conduct of audit in accordance with SAs"



- (a) To obtain reasonable assurance about whether the F. S. as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the F.S. are prepared, in all material respects, in accordance with an applicable FRF.
- (b) To report on the F.S. and communicate as required by the SAs, in accordance with the auditor's findings.



Aspects to be considered by Auditor while performing Audit					Other Explanation
Ethical Requirements	Professional Skepticism	Professional Judgement	Sufficient Appropriate audit Evidence	Conduct of Audit in accordance with SAs	
<ul style="list-style-type: none"> <li>• Comprise Code of Ethics issued by ICAI including independence.</li> <li>• The fundamental principles are:                             <ol style="list-style-type: none"> <li>1. Integrity</li> <li>2. Objectivity</li> <li>3. Professional competence &amp; due care</li> <li>4. Confidentiality, &amp;</li> <li>5. Professional behavior</li> </ol> </li> <li>• Independence comprises both independence of mind and independence of appearance.</li> </ul>	Attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.	<ul style="list-style-type: none"> <li>• The application of relevant training, knowledge and experience,</li> <li>• within the context provided by auditing, accounting and ethical standards,</li> <li>• in making informed decisions about the courses of action</li> <li>• that are appropriate in the circumstances of the audit engagement.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Sufficiency</b> refers to quantum and <b>Appropriateness</b> refers to quality.</li> <li>• <b>Purpose:</b> to reduce audit risk to an acceptably low level and thereby enable the auditor to draw reasonable conclusions on which to base the auditor's opinion.</li> <li>• <b>Audit Risk:</b> Risk that the auditor expresses an inappropriate audit opinion when the F.S. are materially misstated.</li> <li>• Audit Risk is a function of the RMM and detection risk.</li> </ul>	<ul style="list-style-type: none"> <li>• The auditor shall <b>comply with All SAs</b> relevant to the audit.</li> <li>• Compliance with SA is to be specified in Audit report only in case of actual compliance.</li> <li>• To achieve overall objectives of audit, use the <b>objective stated in Individual SAs</b>.</li> <li>• In case <b>Entire SA is not relevant</b> due to non existence of prescribed conditions, comply with relevant requirements.</li> <li>• In case of failure to achieve an objective determine the need of modified opinion or withdrawal.</li> </ul>	<b>Scope of Audit</b>
	Alertness is required w.r.t.	It is required w.r.t.: <ul style="list-style-type: none"> <li>• Materiality &amp; audit risk.</li> <li>• NTE of audit procedures.</li> <li>• Evaluating sufficiency &amp; appropriateness of audit procedures.</li> <li>• Evaluating mngt judgment in applying applicable FRF.</li> <li>• Drawing conclusions based on audit evidence.</li> </ul>			<b>Preparation of F.S.</b>
	<ol style="list-style-type: none"> <li>1. Contradictory audit evidence.</li> <li>2. Reliability of documents.</li> <li>3. Conditions indicating possible frauds.</li> <li>4. Circumstances requiring audit procedures in addition to those suggested in SAs.</li> </ol>				<ul style="list-style-type: none"> <li>• is the duty of Mngt./TCWG.</li> <li>• Duty of management also includes to make accounting estimates and selection and application of appropriate accounting policies.</li> </ul>
					<b>Inherent Limitations for an audit</b>
					<ul style="list-style-type: none"> <li>(a) <b>Nature of Financial reporting:</b> involves judgment by Mngt. based on facts and circumstances.</li> <li>(b) <b>Nature of audit Procedures:</b> directed towards obtaining reasonable assurance.</li> <li>(c) <b>Balance between benefit and cost:</b> user expectation to get AR within a reasonable period and at reasonable cost.</li> </ul>

## SA - 210 (Revised) - "Agreeing the Terms of Engagement"

**Objective of Auditor: To accept or continue an audit engagement only when the basis upon which it is to be performed has been agreed with the client.**

### Agreeing the terms of audit Engagement

#### At the Beginning of Audit

#### During the Course of Audit

#### Initial audit Engagement

#### Recurring Audit

Mngt. request for changes in terms

Limitations Imposed by mngt.

No Limitations Imposed by Mngt.

Determine requirements w.r.t.:

Determine its effect on Level of Assurance & reasonable Justification

Do not accept unless required by law

Ascertain existence of **Preconditions\***

- (a) Revision of terms of Engagement; &
- (b) Remind the entity of existing terms

#### Preconditions for an audit

1. Determine whether the FRF is acceptable.
2. Obtain agreement of mngt that it understands its responsibilities for:
  - (a) Preparation of F.S.
  - (b) Exercising necessary Internal Controls to enable the preparation of F.S. that are free from material misstatements.
  - (c) To provide the auditor:
    - Access to all relevant info.
    - Additional info that auditor requests from mngt.
    - Unrestricted access to persons within the entity.

Exist

Not Exist

Required

Not Required

Auditor Satisfied

Not Satisfied

Accept Audit

Discuss matter with mngt.

Send New Engagement Letter

No Further Duty

Record New Terms in Engagement Letter

Do not accept the changes

Do not accept audit in case of:

- (a) Unacceptable FRF
- or
- (b) Mngt. does not agree with responsibilities

#### CIRCUMSTANCES REQUIRING REVISION IN TERMS

- Indications that the entity misunderstands the objective and scope of the audit.
- Revised or special terms of engagement.
- Recent change of senior management.
- Significant change in ownership.
- Significant change in nature or size of the entity's business.
- Change in legal or regulatory requirements.
- Change in FRF adopted in the preparation of the F.S.
- A change in other reporting requirements.

Mngt. not permit the auditor to continue

Withdraw & Report to appropriate authority

**Compiled by: CA. Pankaj Garg**

## SA – 220 (revised) "Quality Control for an audit of F.S."

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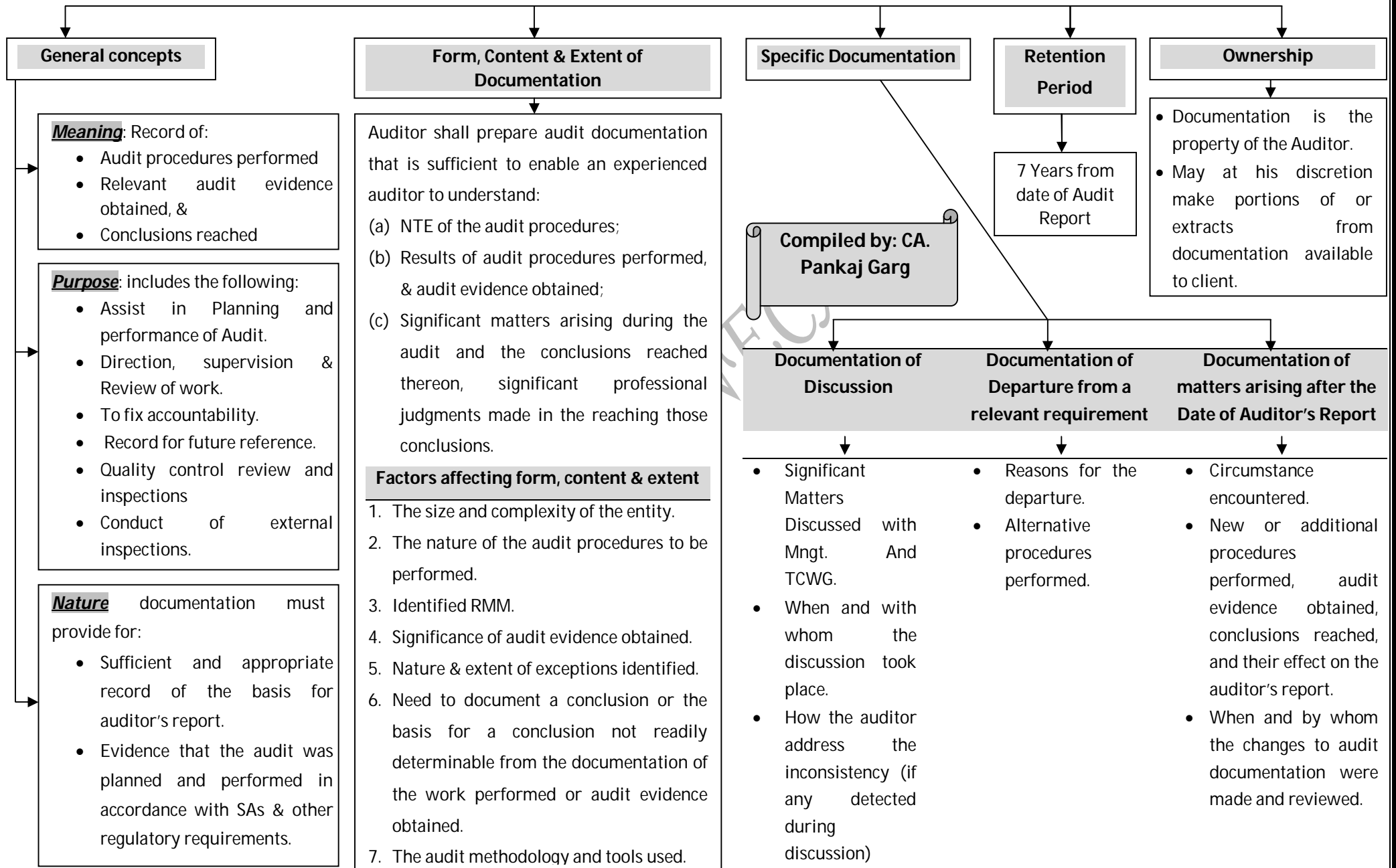
**Objective: Implement QC Policies that provide Reasonable Assurance that audit complies with professional standards and audit report issued is appropriate**

↓

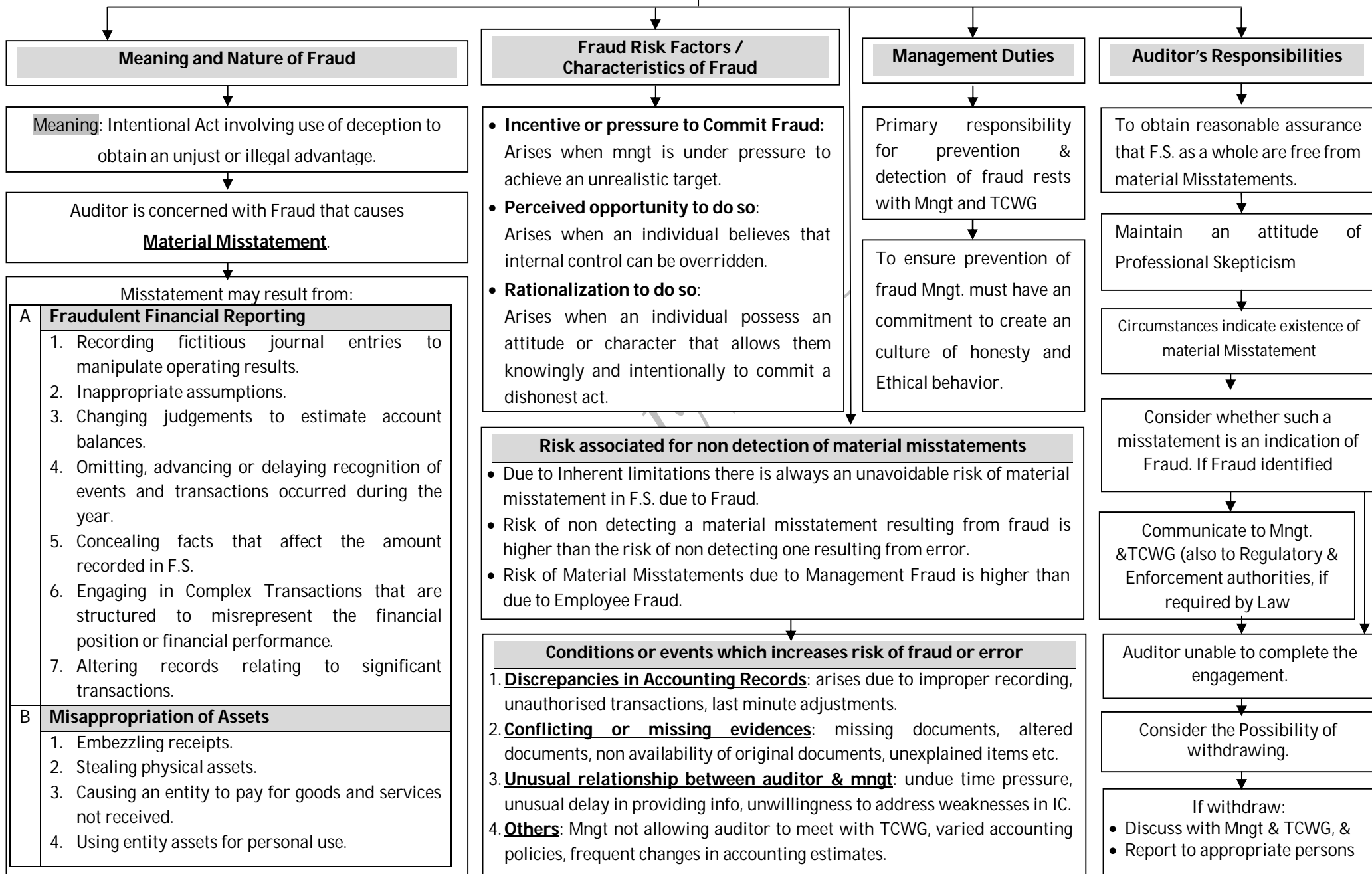
Leadership Responsibilities	Ethical Requirements	Independence	Acceptance / Continuance of Client relationship	Assignment of Engagement Team	Engagement Performance	Monitoring
<p>EP should emphasize the ET the following:</p> <ul style="list-style-type: none"> <li>• Compliance with professional Standards and legal requirements.</li> <li>• Compliance with firm's Quality Control Policies.</li> <li>• Issuance of appropriate audit report.</li> <li>• Ability to raise concerns without fear.</li> <li>• Quality is essential &amp; indispensable in engagement performance.</li> </ul>	<p>EP to remain alert for <b>evidence of non-compliance</b> with relevant ethical requirements by ET through:</p> <ul style="list-style-type: none"> <li>• Inquiry.</li> <li>• Observation.</li> </ul> <p>If there is an <b>indications</b> of non-compliance with relevant ethical requirements, EP should:</p> <ul style="list-style-type: none"> <li>• Consult others in the firm.</li> <li>• Determine appropriate action.</li> </ul>	<div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Form a conclusion on compliance with applicable independence</div> <p style="text-align: center;">↓</p> <div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Obtain relevant information from Firm</div> <p style="text-align: center;">↓</p> <div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Identify &amp; Evaluate circumstances &amp; Relationship that threatens independence</div> <p style="text-align: center;">↓</p> <div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Evaluate information on identified breaches.</div> <p style="text-align: center;">↓</p> <div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Determine if these threaten independence</div> <p style="text-align: center;">↓</p> <div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Take appropriate action to eliminate such threats</div> <p style="text-align: center;"><b>or</b></p> <div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;">Promptly report inability to take appropriate action to</div>	<ul style="list-style-type: none"> <li>• Be satisfied that appropriate procedures regarding client acceptance / continuance have been followed.</li> <li>• Determine whether conclusions reached are appropriate.</li> </ul> <p style="text-align: center;">↓</p> <p>If EP obtains <b>information</b> that would have caused firm to withdraw the engagement, communicate information promptly to firm</p>	<p>EP to be satisfied that ET &amp; Auditor's Expert not part of ET have appropriate competence &amp; capabilities to:</p> <ul style="list-style-type: none"> <li>➤ Perform audit engagement in accordance with professional standards and regulatory or legal requirements, and</li> <li>➤ Enable an AR that is appropriate in the circumstances.</li> </ul>	<p><b>1. Direction, Supervision and performance:</b></p> <ul style="list-style-type: none"> <li>• EP shall take the responsibility for directions, supervision &amp; performance of audit engagement in compliance with standards &amp; regulatory requirements, &amp;</li> <li>• to make an appropriate AR.</li> </ul> <p><b>2. Reviews:</b></p> <p>EP shall take the following responsibilities:</p> <ol style="list-style-type: none"> <li>Reviews are being performed in accordance with policies / procedures.</li> <li>Be Satisfied that SAAE has been obtained to support the conclusions reached and AR to be issued through                             <ul style="list-style-type: none"> <li>• Review of Audit Documentation.</li> <li>• Discussion with ET</li> </ul> </li> </ol> <p><b>3. Consultation:</b></p> <p>EP shall undertake consultation</p> <ul style="list-style-type: none"> <li>• wherever required.</li> <li>• Ensure its implementation</li> </ul> <p><b>4. Engagement Quality Control Review:</b></p> <p>required in case of listed entities.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p style="text-align: center; margin: 0;"><b>Matters to be evaluated by EQCR</b></p> <ul style="list-style-type: none"> <li>• Discussion of significant matters with ET.</li> <li>• Review of FS &amp; proposed audit report.</li> <li>• Review of selected audit documentation</li> </ul> </div> <p><b>5. Differences of Opinion:</b> follow the firm's policies &amp; procedures for dealing with and resolving differences of opinion.</p>	<p>Obtain reasonable assurance that firm's policies / procedures relating to QC are relevant, adequate, and operating effectively.</p> <p>Consider:</p> <ul style="list-style-type: none"> <li>• Results of firm's monitoring process.</li> <li>• Whether deficiencies noted may affect the audit engagement.</li> </ul>

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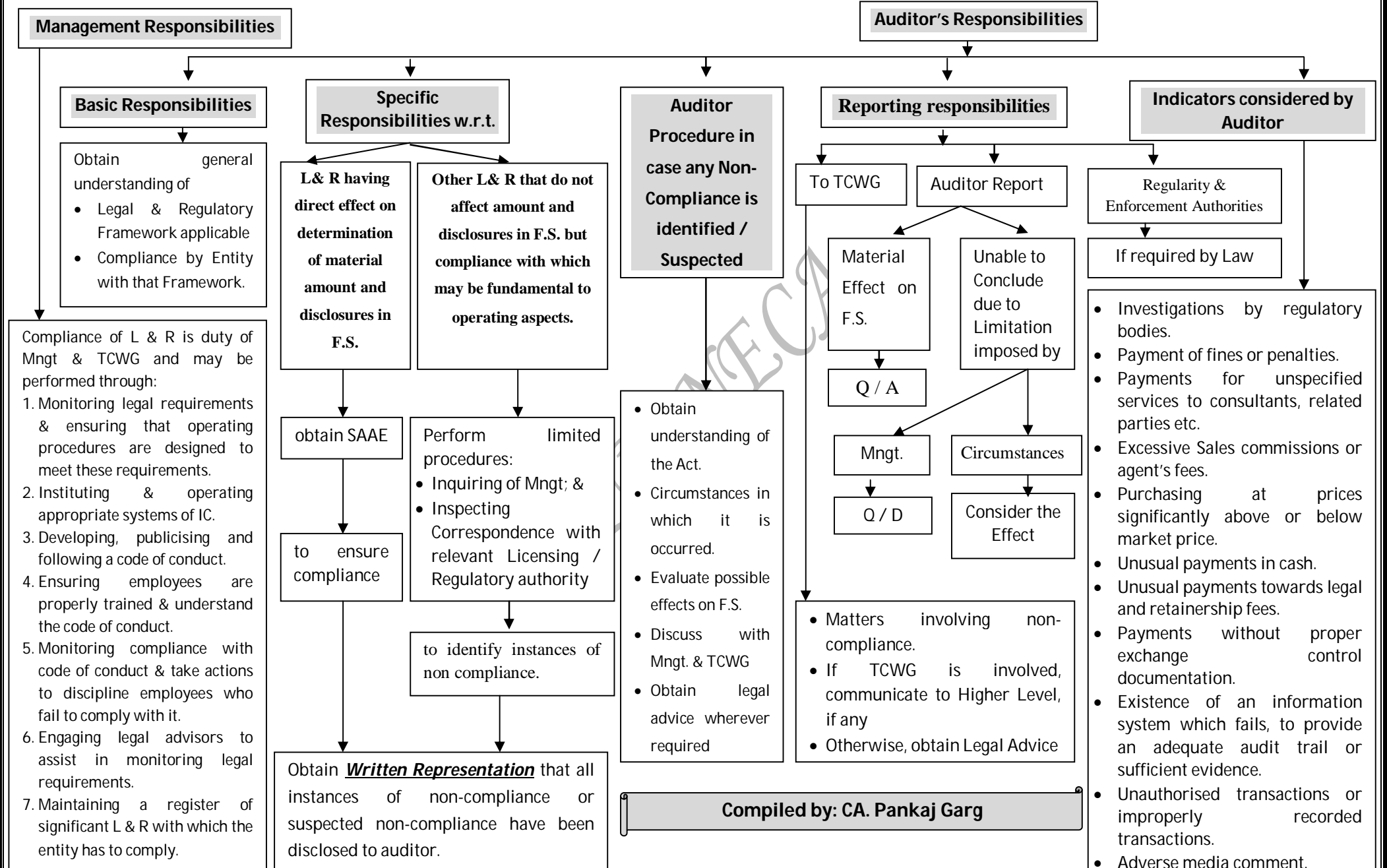
# SA – 230 (Revised) – Audit Documentation



# SA 240 (Revised) – The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements

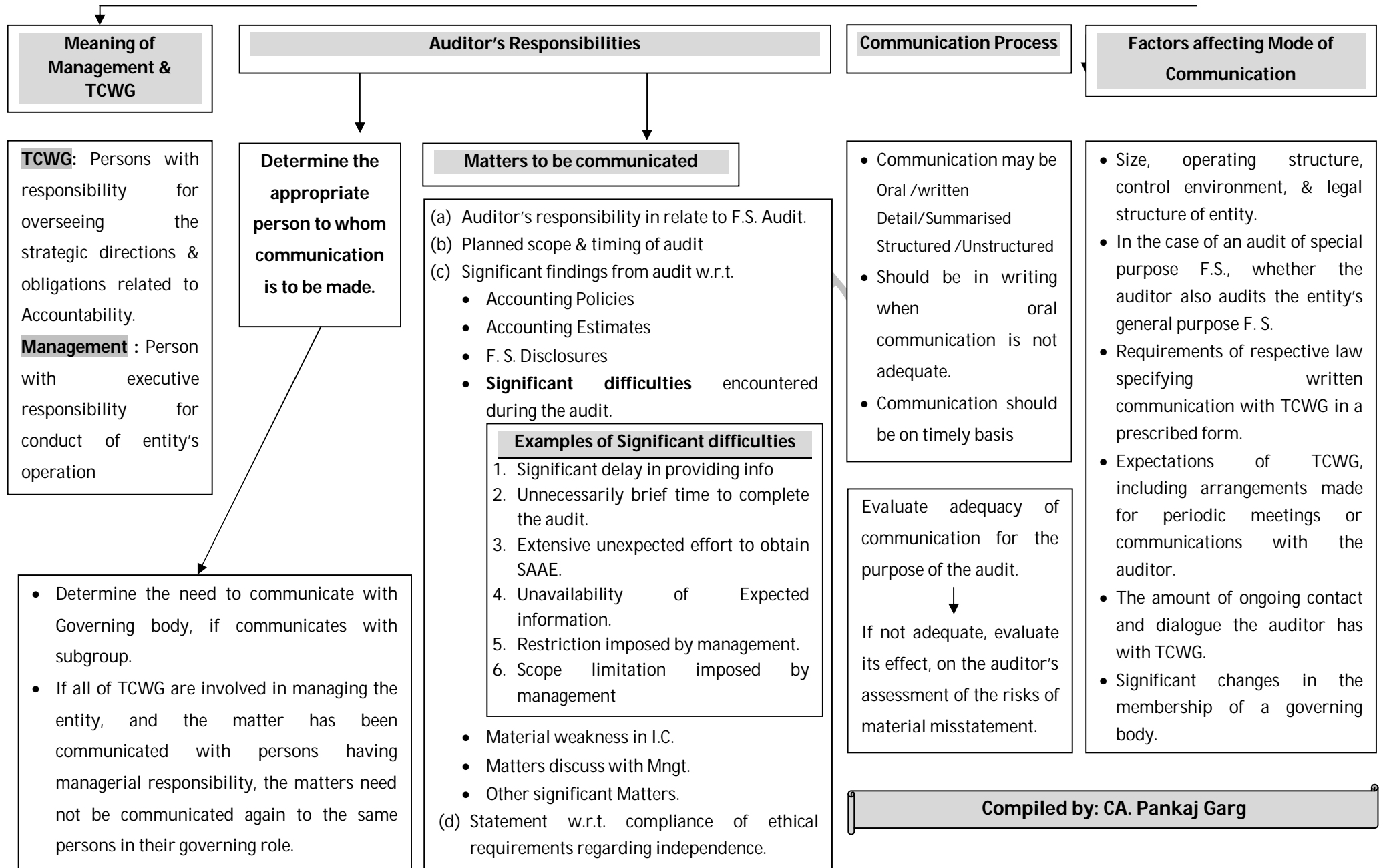


# SA 250 (Revised) "Consideration of Laws and Regulations in an Audit of F.S."





## SA 260 (Revised) – “Communication with TCWG”



### Meaning of Management & TCWG

**TCWG:** Persons with responsibility for overseeing the strategic directions & obligations related to Accountability.  
**Management :** Person with executive responsibility for conduct of entity's operation

- Determine the need to communicate with Governing body, if communicates with subgroup.
- If all of TCWG are involved in managing the entity, and the matter has been communicated with persons having managerial responsibility, the matters need not be communicated again to the same persons in their governing role.

### Auditor's Responsibilities

**Determine the appropriate person to whom communication is to be made.**

### Matters to be communicated

- Auditor's responsibility in relate to F.S. Audit.
  - Planned scope & timing of audit
  - Significant findings from audit w.r.t.
    - Accounting Policies
    - Accounting Estimates
    - F. S. Disclosures
    - **Significant difficulties** encountered during the audit.
- Examples of Significant difficulties**

  - Significant delay in providing info
  - Unnecessarily brief time to complete the audit.
  - Extensive unexpected effort to obtain SAAE.
  - Unavailability of Expected information.
  - Restriction imposed by management.
  - Scope limitation imposed by management
- Material weakness in I.C.
  - Matters discuss with Mngt.
  - Other significant Matters.
- Statement w.r.t. compliance of ethical requirements regarding independence.

### Communication Process

- Communication may be Oral /written Detail/Summarised Structured /Unstructured
- Should be in writing when oral communication is not adequate.
- Communication should be on timely basis

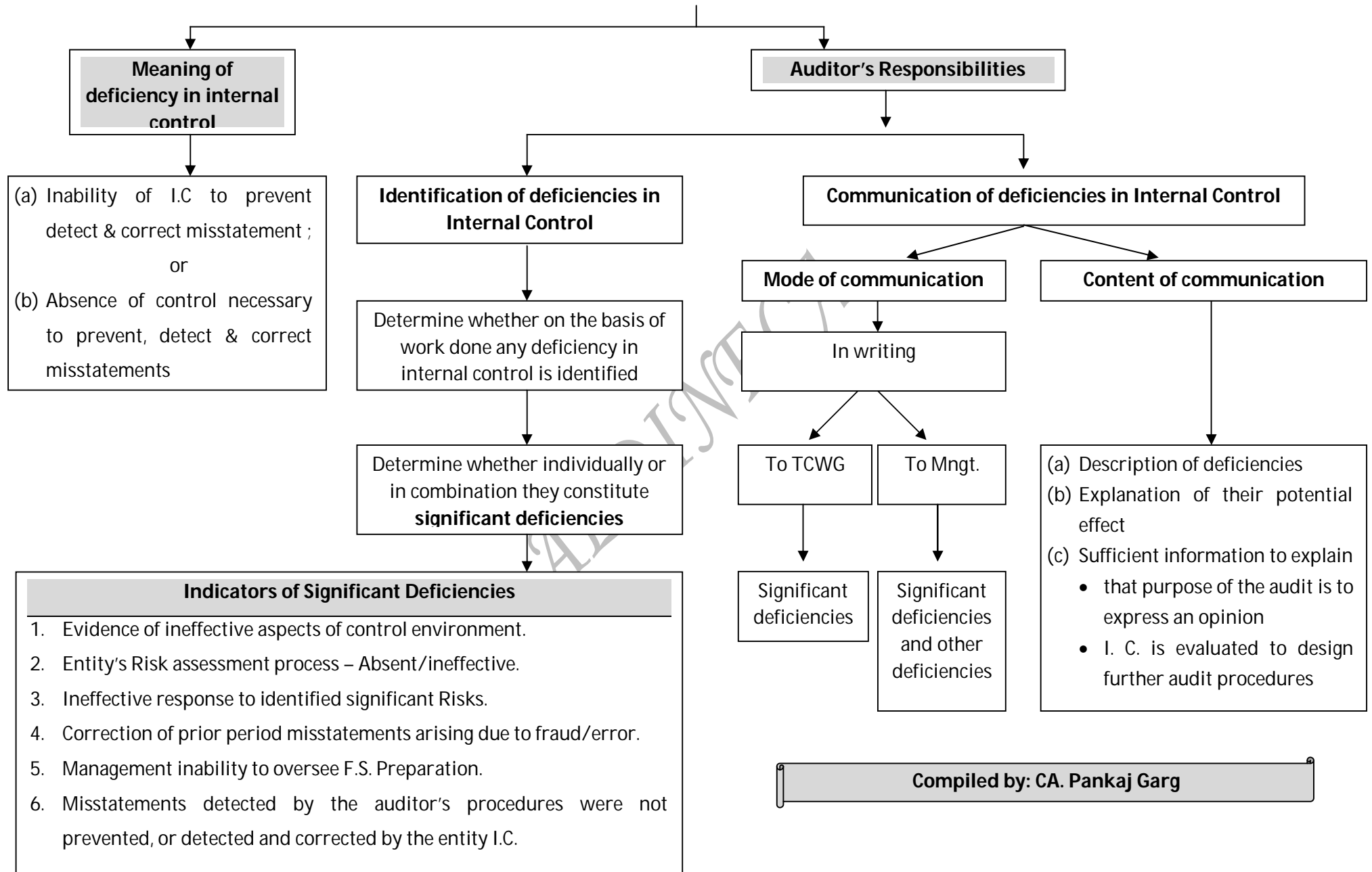
Evaluate adequacy of communication for the purpose of the audit.  
 ↓  
 If not adequate, evaluate its effect, on the auditor's assessment of the risks of material misstatement.

### Factors affecting Mode of Communication

- Size, operating structure, control environment, & legal structure of entity.
- In the case of an audit of special purpose F.S., whether the auditor also audits the entity's general purpose F. S.
- Requirements of respective law specifying written communication with TCWG in a prescribed form.
- Expectations of TCWG, including arrangements made for periodic meetings or communications with the auditor.
- The amount of ongoing contact and dialogue the auditor has with TCWG.
- Significant changes in the membership of a governing body.

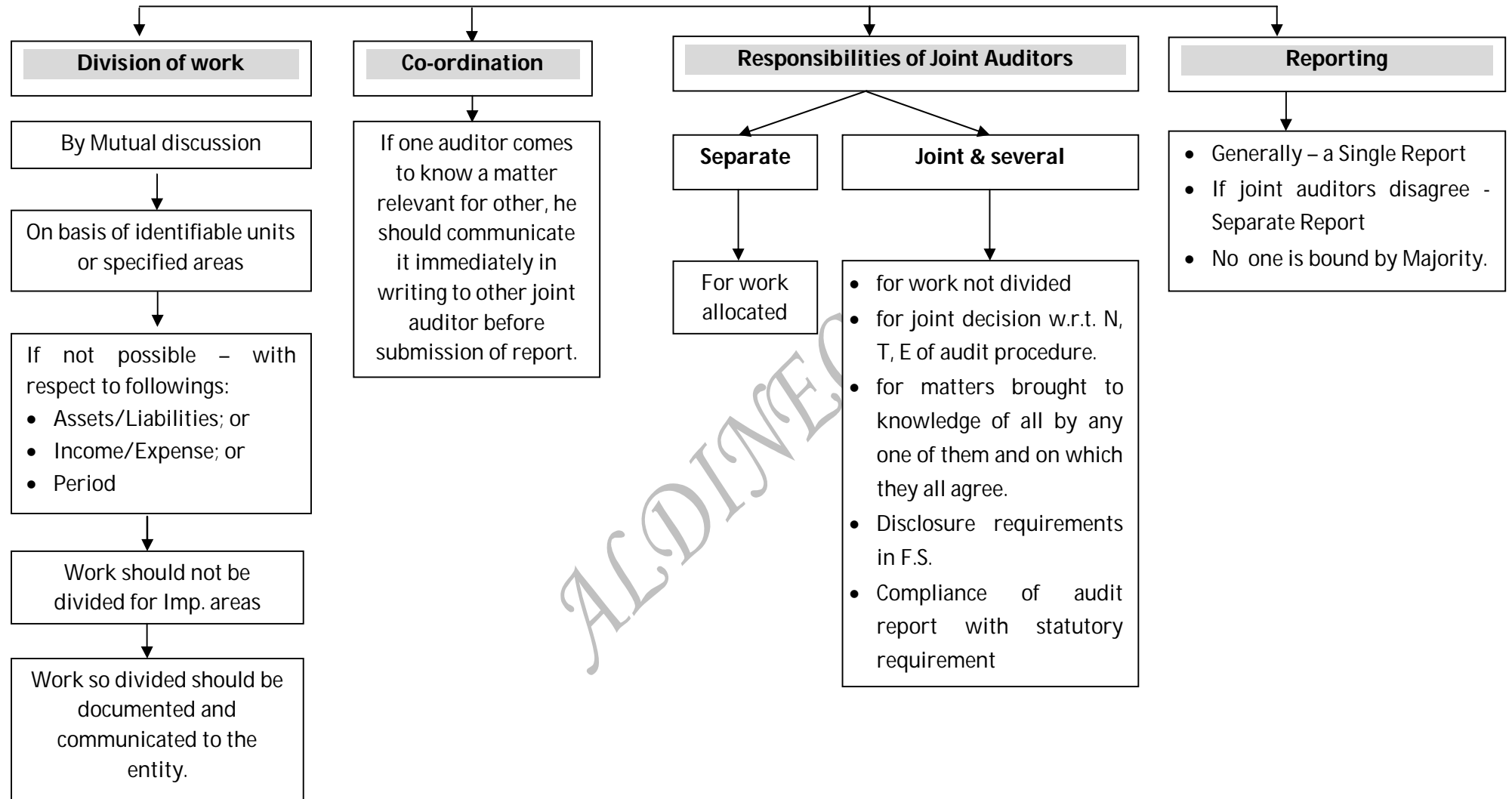
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## SA-265 "Communicating Deficiencies in Internal Control to TCWG & Management"



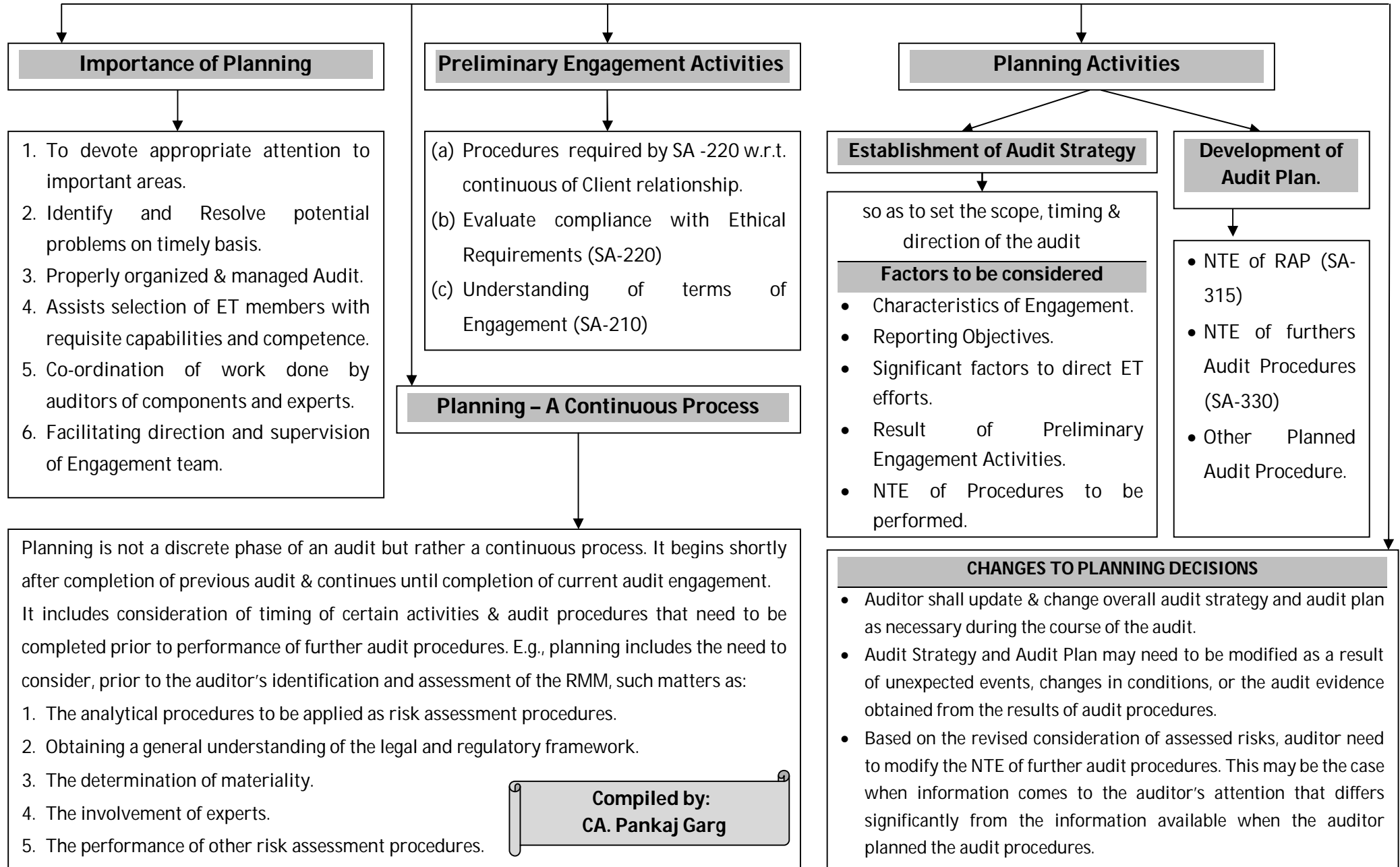
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## SA 299 "Responsibility of Joint Auditors"

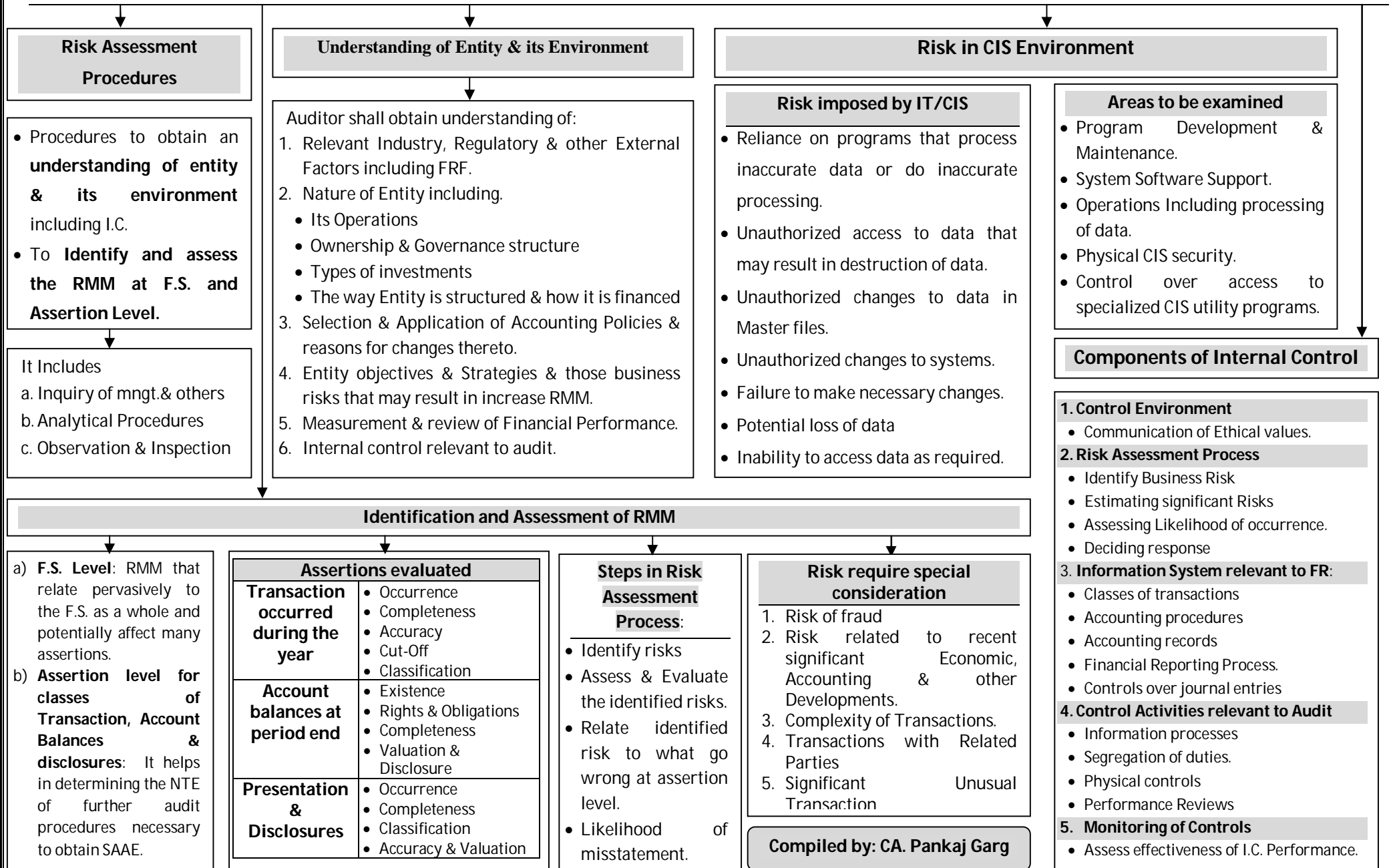


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# SA 300 (Revised) – Planning in an audit of Financial Statements



# SA 315 (Revised) – Identifying and Assessing the Risk of Material Misstatements through understanding the Entity and Its Environment.



## SA 320 (Revised) "Materiality in Planning and Performing an Audit"

### Concept of Materiality

Materiality is a subject of professional judgment and discussion presented in FRF provides a reference to the auditor in determining materiality.

If FRF does not include a discussion, following can be referred:

- (a) Misstatements including omissions expected to influence the economic decision of users.
- (b) Size or nature of misstatement & the surrounding circumstances.
- (c) Common financial information needs of the users as a group.

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Judgment of materiality provides a basis for:

- (a) Determination of NTE of RAP
- (b) Identifying and assessing RMM.
- (c) NTE of further audit procedures.

### Performance Materiality

- The amount set by auditor at
- less than materiality for F.S as a whole
- to reduce to an appropriately low level
- the probability that the aggregate of the uncorrected & undetected misstatement
- exceeds materiality for F. S. as a whole

### Revision of Materiality

- In event of becoming aware of information that would have caused auditor to have determined a different amount initially, auditor shall revise materiality for the F.S. as a whole & if required, for particular classes of transactions, account balances or disclosures.
- If the auditor concludes that a lower materiality than that initially determined is appropriate, the auditor shall determine whether it is necessary to revise performance materiality, and whether the NTE of the further audit procedures remain appropriate.

### Auditor's Duties

- (a) Upon establishing the overall audit strategy, the auditor shall determine the materiality for the F. S. as a whole.
- (b) Determine the materiality level for specific transactions for which misstatements of lower amount be expected to influence the economic decisions of users.
- (c) Determine the performance materiality for purpose of assessing the RMM and determining the NTE of further audit procedures.

### Use of benchmark in determining Materiality

A %age is often applied to a chosen benchmark as a starting point in determining materiality for the F.S. as a whole.

#### Factors affecting identification of appropriate benchmark

1. The elements of the financial statements;
2. Items on which the attention of the users of the particular entity's financial statements tends to be focused;
3. The nature of the entity, where the entity is at in its life cycle, and the industry and economic environment in which the entity operates;
4. The entity's ownership structure and the way it is financed; and
5. The relative volatility of the benchmark.

# SA – 330 “Responses to Assessed Risks”

Objective: To obtain Sufficient and Appropriate Audit Evidence about Assessed Risk of Material Misstatement through design and implementing Appropriate Responses

## Tests of Controls

Procedures designed to evaluate the operating effectiveness of controls in preventing, detecting or correcting material misstatements at assertion level.

Obtain audit evidences w.r.t. (a) Application of controls (b) Consistency of application  
(c) By whom & by what means they applied

Evaluate the audit evidences

Material weaknesses identified

Communicate to Mngt. & TCWG – on timely basis

## Substantive Procedures

Procedures designed to detect material misstatements at assertion level.

It comprises of:

- a) Test of details (of classes of transactions, Account Balances and Disclosures); &
- b) Substantive Analytical Procedures

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<b>External Confirmation (EC) procedures as substantive procedures</b>	<p>Auditor shall consider whether EC procedures are to be performed as substantive audit procedures.</p> <p>Factors that may assist the auditor are:</p> <ol style="list-style-type: none"> <li>1. Confirming party knowledge of Subject Matter.</li> <li>2. Ability or Willingness of intended confirming part to respond.</li> <li>3. Objectivity of Intending Party.</li> </ol>
<b>Closing Process</b>	<ul style="list-style-type: none"> <li>• Reconciling F.S. with underlying A/cing Records</li> <li>• Examine Material Journal Entries &amp; other adjustments made during the course of preparing the F.S.</li> </ul>
<b>Significant Risks</b>	Procedures that are specifically responsive to that risk needs to be applied

Timing: When Substantive procedures are applied for interim period, the auditor shall cover remaining period by appropriate procedures

### Special Considerations

#### **Using Audit Evidence obtained in Interim Period:**

- Obtain audit Evidence for significant changes subsequent to Interim Period.
- Determine the additional Evidence to be obtain for remaning period.

#### **Using Audit Evidence obtained during previous audits:**

- Establish Continuing relevance of that evidence by determining significant changes subsequent to previous audit
- Changes occurs: Test the controls in current audit
- No Change Occurs: Test the controls once in three audits

### Factors warranting re-test of controls

1. Deficient control environment.
2. Deficient monitoring of controls.
3. Significant manual element to relevant controls.
4. Personnel changes that significantly affect the application of control.
5. Changing circumstances that indicate the need for changes in the control.
6. Deficient general IT-controls.

# SA 402 (Revised) – Audit Considerations relating to an Entity Using a Service Organisation

## Auditor's Objective

- Obtain an understanding of nature & significance of service provided by the S.O. and their effect on the user's entity internal control relevant to the audit, sufficient to identify and assess the RMM.
- To design and perform audit procedures responsive to those risks.

## Obtaining understanding of services provided by service Organisation (S.O.)

- The user auditor shall obtain an understanding of how user entity uses the services of a service organization in the user entity operation, including:
- (a) Nature of service provided by the S.O. and significance of services to user entity.
  - (b) Nature and materiality of the transactions processed or financial reporting processes affected by service organizations.
  - (c) Degree of interaction between activities of S.O. and those of the user entity.
  - (d) The nature of relationship between user entity and the service organization.

**User Auditor:** An auditor who audits and Reports on the financial statements of a user entity.

**User Entity:** An Entity that uses a service organization and whose financial statements are being audited.

**Type 1 Report:** Report on the description and design of internal controls at a service organization for a specified date.

**Type 2 Report:** Report on the description, design and operating effectiveness of controls at a service organization for a specified period.

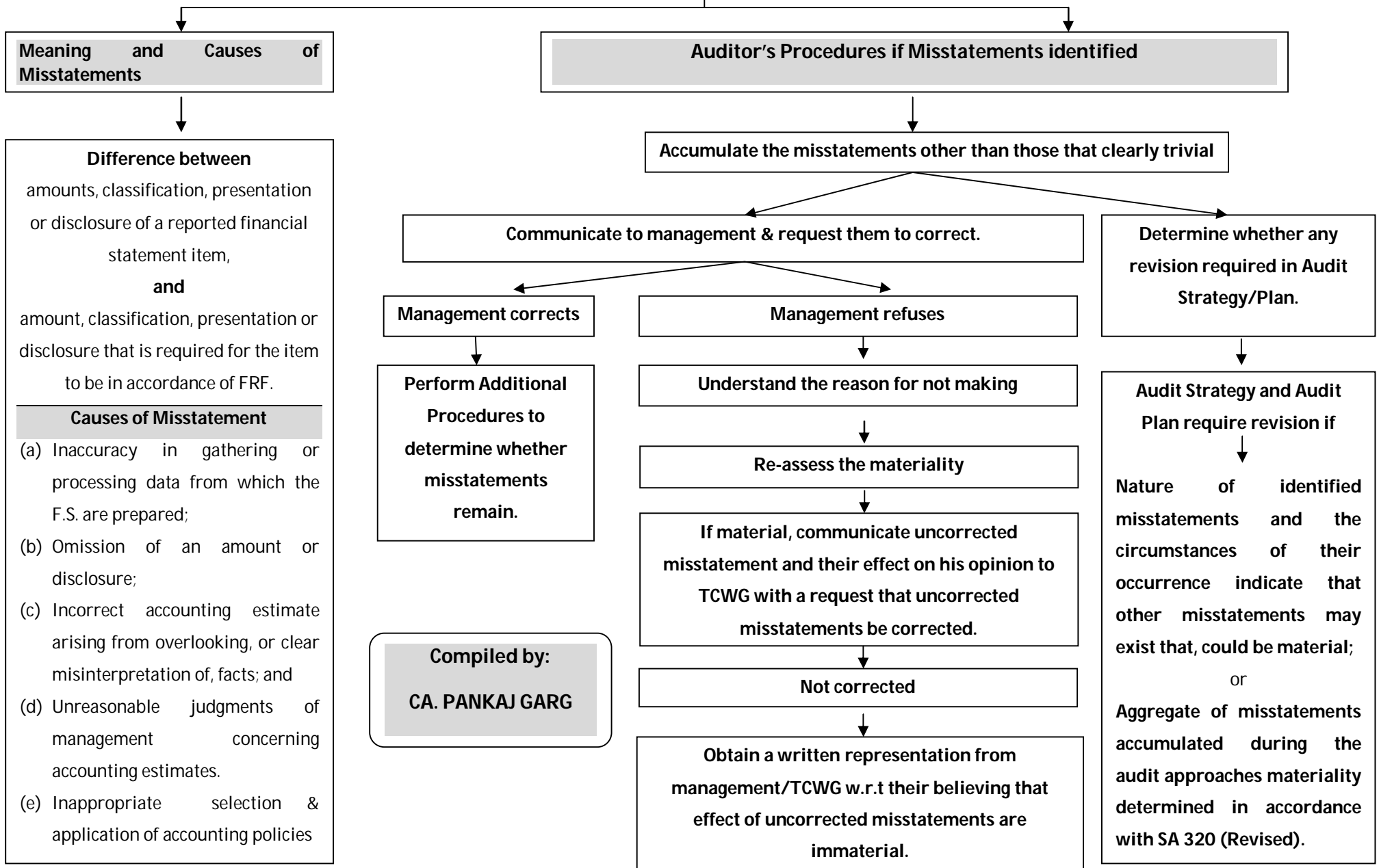
## Auditor's considerations

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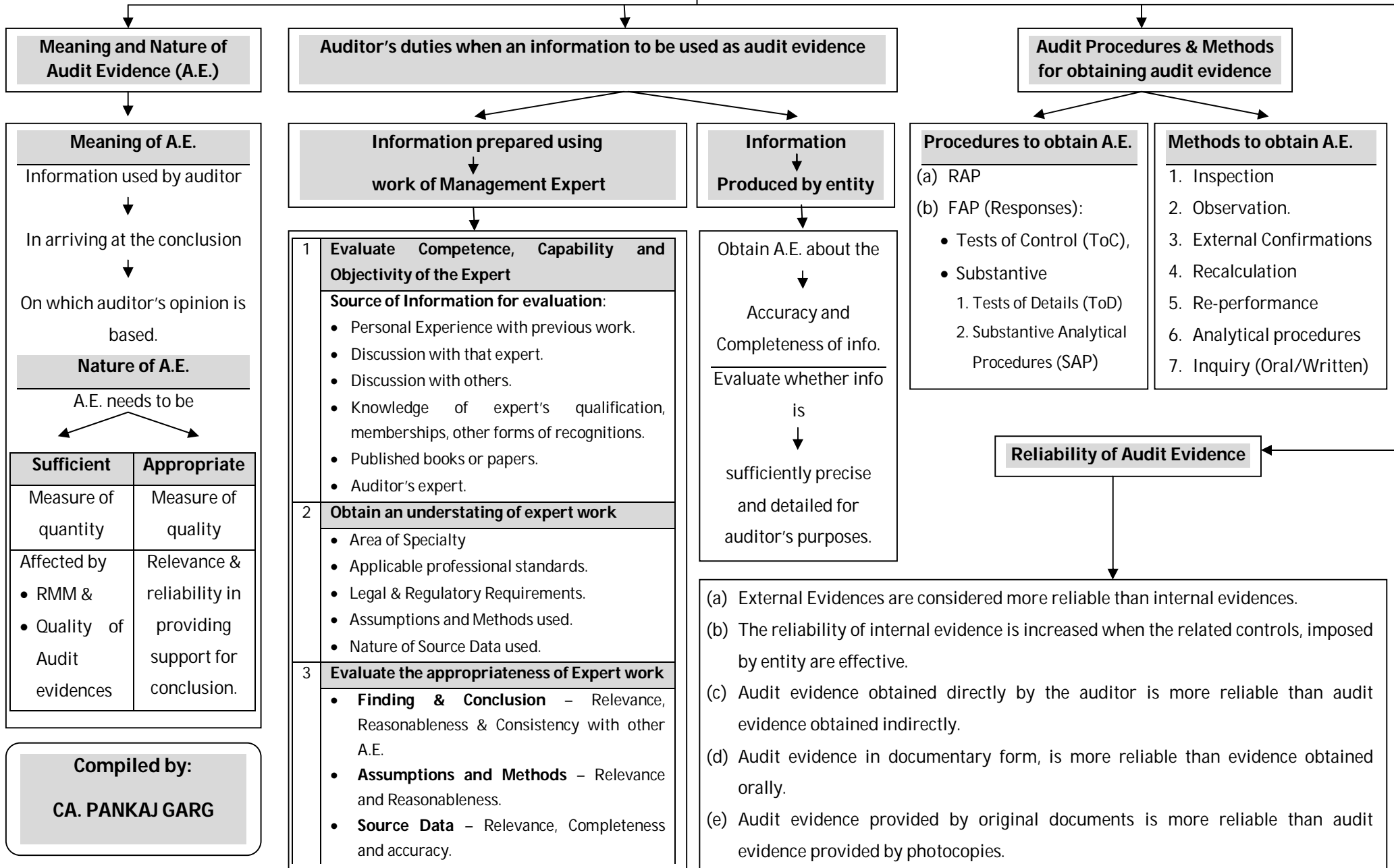
- User auditor shall *evaluate the design and implementation of relevant controls of user entity* that relate to the services provided by service organization.
  - User auditor shall *determine whether a sufficient understanding of nature and significance of services provided by service organization* and their effect on the user entity internal control relevant to the audit has been obtained.
  - If user auditor is *unable to obtain a sufficient understanding from the user entity*, user auditor shall obtain that understanding from the following procedures:
    - (a) Obtaining a Type 1 or Type 2 Report, if available.
    - (b) Contacting the service organization, through the user entity.
    - (c) Visiting the service organization.
    - (d) Using another auditor to perform procedures that will provide the necessary information about the relevant controls at the S.O.
- If a S.O. uses subservice organisation, the service auditor's report may either include or exclude the subservice organisation's relevant control objectives & related controls in the service organisation's description of its system & in the scope of service auditor's engagement. These two methods of reporting are known as the inclusive method and the carve-out method, respectively.**
- If Type 1 or Type 2 report excludes the controls at a subservice organisation, and the services provided by the subservice organisation are relevant to the audit of the user entity's financial statements, the user auditor is required to apply the requirements of this SA in respect of the subservice organisation.
  - Nature and extent of work to be performed by the user auditor regarding the services provided by a subservice organisation depend on the nature and significance of those services to the user entity and the relevance of those services to the audit.



# SA 450 "Evaluation of Misstatements Identified during the Audit"



# SA 500 "Audit Evidence"



**Compiled by:**  
**CA. PANKAJ GARG**

# SA 501 "Audit Evidence – Specific Considerations for Selected Items"

## Inventory – Existence & Condition

Compiled by: CA. Pankaj Garg

### General Procedures

When inventory is material to the F.S.

↓

the auditor shall obtain SAAE

↓

regarding **existence & condition** by

↓

(a) Attendance at physical inventory counting, unless impracticable, to:

- Evaluate mngt. instructions & procedures for recording & controlling the results of the entity's physical inventory counting;
- Observe the performance of management's count procedures;
- Inspect the inventory;
- Perform test counts;

(b) Performing audit procedures over the entity's final inventory records to determine whether they accurately reflect actual inventory count results.

### Special Procedures

1	<p><b>Inventory counting conducted at date other than B/S date</b></p> <p>Perform audit procedures to obtain audit evidence</p> <p>↓</p> <p>about whether changes in inventory between the count date and the date of the F.S. are properly recorded.</p>
2	<p><b>Auditor unable to attend Inventory Count</b></p> <p>Make or observe some physical counts on an alternative date,</p> <p>↓</p> <p>and perform audit procedures on intervening transactions</p>
3	<p><b>Attendance at inventory count is impracticable</b></p> <p>Perform alternative audit procedures to obtain S.A.A.E. regarding existence and condition of inventory.</p> <p>↓</p> <p>If it is not possible to do so, modify the opinion in the auditor's report in accordance with SA 705.</p>
4	<p><b>Inventory under custody and control of Third Party</b></p> <p>Obtain S.A.A.E by performing the following:</p> <p>(a) Request confirmation from third party.</p> <p>(b) Perform Inspection/other audit procedure.</p>

## Litigation & Claims – Completeness

Auditor is required to identify litigation and claims by following procedures:

- **Inquiry:** of Mngt. & others within entity, including in house legal counsel.
- **Review** – minutes of meetings of TCWG, communication between entity & external legal counsel.
- **Review** – legal expenses account.

If management refuses to permit auditor to communicate with legal counsel / external legal counsel refuses / auditor unable to collect SAAE by performing alternate procedures

↓

**Modify Opinion in accordance with SA 705**

## Segment Reporting – Presentation & Disclosures

Obtain SAAE regarding presentation & disclosure of segment information in accordance with the applicable FRF by:

(a) Obtaining an understanding of the methods used by management in determining segment information, and

- Evaluate whether such methods are likely to result in disclosure in accordance with the applicable FRF; and
- Where appropriate, testing the application of such methods; and

(b) Performing analytical procedures or other audit procedures appropriate in the circumstances.

# SA – 505 “External Confirmation”

The objective of the auditor, when using external confirmation procedures, is to design and perform such procedures to obtain relevant and reliable audit

## Meaning & Type of E.C.

Audit Evidence obtained as a direct written response to auditor from 3<sup>rd</sup> Party in Paper/Electronic/Other form.

### 2 Types

+ ve Request	- ve request
Request that 3 <sup>rd</sup> Party respond directly to auditor	Request that 3 <sup>rd</sup> Party respond directly to auditor
indicating whether it agrees or disagrees	only if it disagrees
With the info in request or providing requested info.	with the information in the request

### Areas where External Confirmation may be obtained:

- Bank balance & Other confirmation from bankers
- Account Receivable/Account Payable Balances
- Stock Lying with Third Parties
- Property Title Deed held by third parties
- Investments Purchased but delivery not taken.
- Loan from Lenders
- Terms of agreement or Transaction with Third Parties

## External Confirmation Procedures

Determining the information to be confirmed.  
 ↓  
 Selecting the Appropriate Third Party.  
 ↓  
 Designing the confirmation request.  
 ↓  
 Sending the request including follow up.

### Factors to be considered while designing E.C. request:

- Assertions being addressed.
- Specific identified RMM.
- Layout and presentation of request.
- Prior Experience of audit.
- Method of Communication.
- Management Authorization.
- Ability of confirming party to provide the requested information

## Audit Procedures in Special Circumstances

### Mngt. refuses to allow the auditor to send request

- Inquire the reasons
- Evaluate the implications on RMM
- Perform Alternative Audit procedure.

- Refusal appears to be unreasonable
- Unable to collect audit evidence
- Communicate to TCWG.
- Determine its affect on Opinion

### Responses to E.C. request

• Creates Doubt	Obtain Further Evidences
• Not Reliable	Consider its affect on NTE of other procedures
• No Response	Perform Alternative procedure
• Unable to collect evidence	Determine its affect on Opinion
• Exception occurs	Investigate to determine misstatement

Compiled by: CA. Pankaj Garg

## Limited use of –ve Request

As it provides less persuasive evidence than the positive Confirmation request.

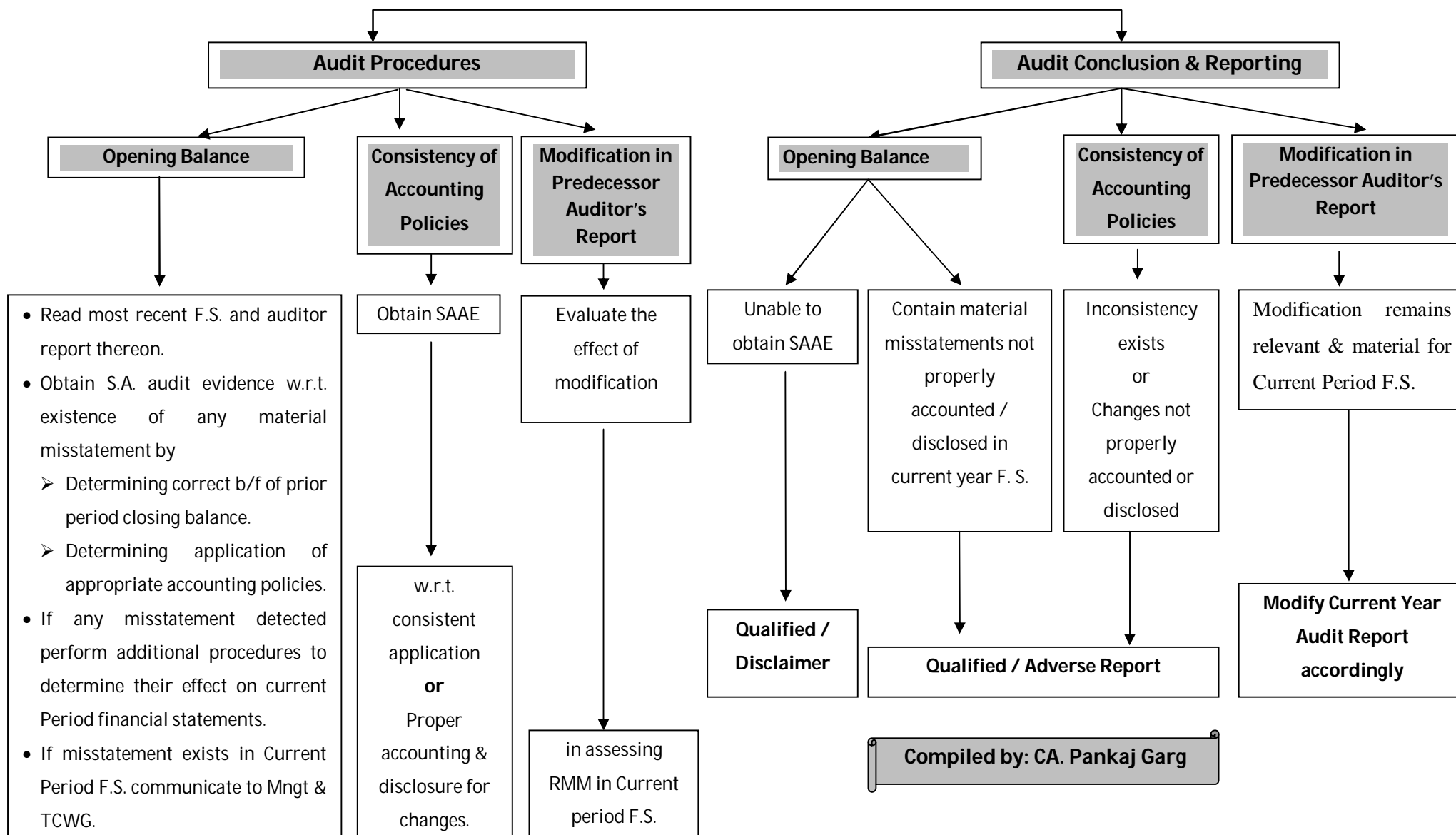
### Circumstances in which negative request may be used as sole substantive procedure:

- Low RMM.
- Population consists of large no. of small, homogenous account balances.
- Expectation of low exception rate.
- Auditor not aware of circumstances that 3<sup>rd</sup> party disregard request.

# SA – 510 “Initial Audit Engagements – Opening Balances”

**Meaning of Initial Audit Engagement:** An Engagement in which financial statements for prior period are not audited or were audited by predecessor auditor.

**Meaning of Opening balance –** A/c balance that exist at beginning of period & also includes disclosures exists at beginning of period.



**Compiled by: CA. Pankaj Garg**

# SA 520 "Analytical Procedures"

## Meaning and Nature of Analytical Procedures

Evaluation of financial information  
↓  
through analysis of relationships  
↓  
among both financial and non-financial data.  
**AND**  
also encompass such investigation as is necessary of  
identified fluctuations or relationships that are  
inconsistent with other relevant information or that  
differ from expected values by a significant amount.

### Analytical Procedures

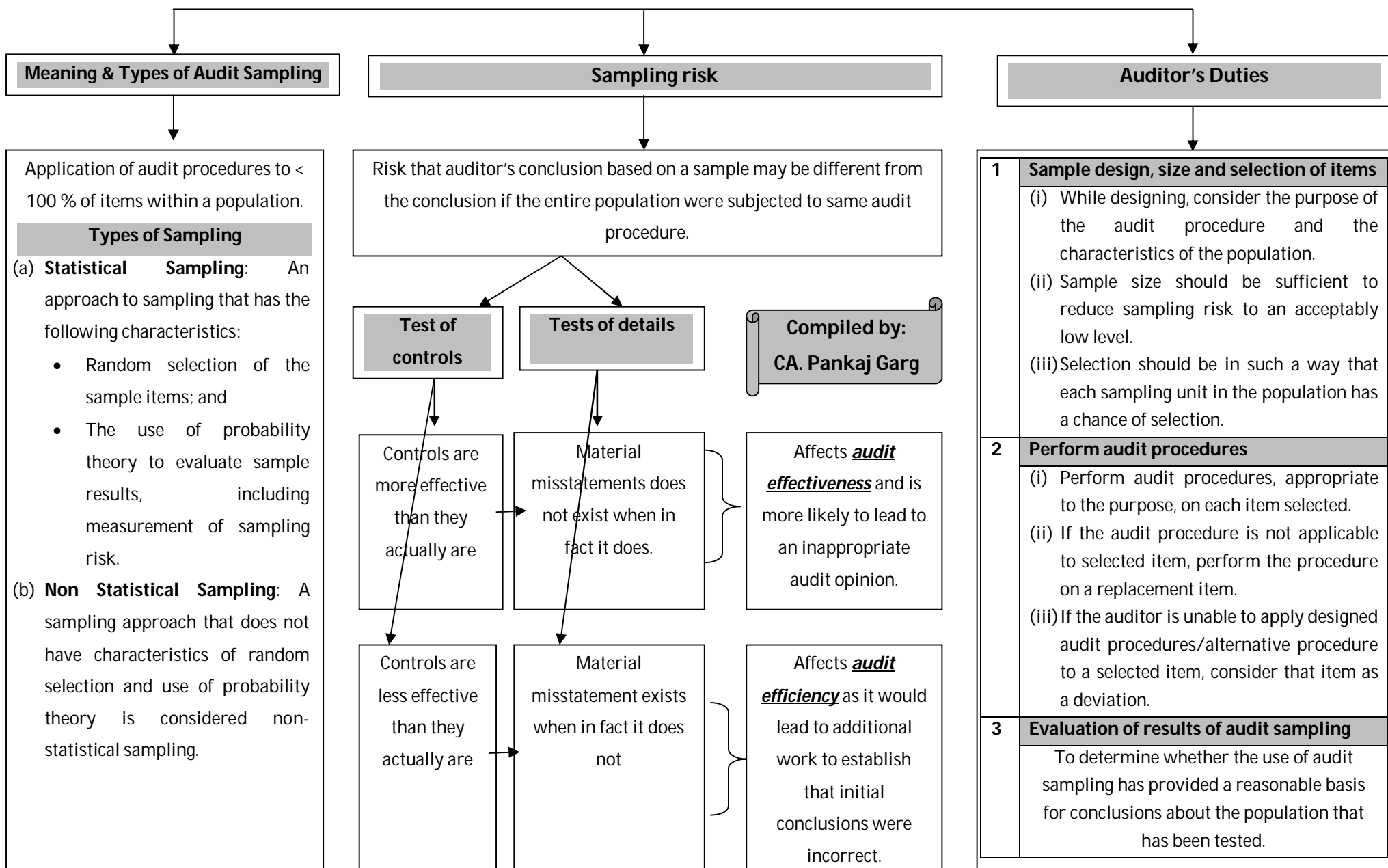
Consideration of Comparisons of Financial Information	Consideration of relationships among
with comparable information for prior periods.  <b>or</b> with anticipated results of the entity  <b>or</b> Auditor's expectations  <b>or</b> Similar industry information.	Elements of financial information  <b>or</b> Financial information and relevant non-financial information.

## Auditor's Procedures

- 1 Determine the suitability of particular substantive analytical procedures (SAP)**  
 Following factors requires consideration:
  1. SAPs more suitable to large volumes of transactions tending to be predictable over time.
  2. But suitability of AP influenced by:
    - Nature of assertion.
    - Auditor's assessment of APs effectiveness to identify material misstatement.
  3. In some cases unsophisticated predictive models may be useful.
  4. Different types of APs provide different levels of assurance.
  5. Particular SAP may be considered suitable when ToD are performed on same assertion.
- 2 Evaluate the reliability of data**  
 Following factors affects the reliability:
  - Source of the information available.
  - Comparability of the information available.
  - Nature and relevance of the information available, and
  - Controls over the preparation of the information
- 3 Develop an expectation of recorded amounts or ratios** and evaluate whether the expectation is sufficiently precise to identify material misstatement.
- 4 Determine the amount of any difference of recorded amounts from expected values** that is acceptable without further investigation.
- 5 Investigating Results of Analytical Procedures**  
 If auditor identified fluctuations or relationships that are inconsistent with other relevant information or differ from expected values by a significant amount, the auditor shall investigate such differences by:
  - (a) Inquiring of management; and
  - (b) Performing other audit procedures as necessary in the circumstances.

**Compiled by: CA. Pankaj Garg**

# SA – 530 (Revised) “AUDIT SAMPLING”



# SA – 540 (Revised) “Auditing Accounting Estimates(AE), including Fair Value Accounting Estimates and Related Disclosures”

Objective of Auditor: To obtain SAAE whether (a) AE including Fair Value AE are reasonable; and (b) related disclosures in the F.S. are adequate.

Compiled by: CA. Pankaj Garg

## Meaning & Nature of Accounting Estimates

- **Accounting estimate:**  
“An approximation of a monetary amount in the absence of a precise means of measurement”. This term is used for an amount measured at fair value where there is estimation uncertainty.
- **Estimation Uncertainty:**  
The susceptibility of an accounting estimate & related disclosures to an inherent risk of precision in its measurement.
- **Examples of Accounting Estimates**
  - Provision for Bad Debt,
  - Inventory loss,
  - Warranty Obligations,
  - Depreciation,
  - Provision against carrying amount of investments, etc.
- **Examples of Fair Value A.E.**
  - Share Based Payments,
  - Assets held for disposal,
  - Financial Instruments,
  - Assets acquired in business combinations

## Auditor’s Duties

### Risk Assessment Procedures & Related Activities

1. Obtain an understating of:
  - Requirements of applicable FRF
  - How management identifies transactions, events and conditions that give rise to need for accounting estimates.
  - Estimation making process adopted by mngt. and data on which they are based.

#### Estimation making process

- Methods/Model used in making Accounting estimates.
  - Relevant Controls
  - Use of Management Expert.
  - Changes in the methods from the prior period along with reasons.
  - Assessment of effect of estimation uncertainties.
2. Review of outcome of accounting estimates of prior period.

### Responses to Assessed Risks

Based on assessed RMM, auditor shall determine:

- Whether management has appropriately applied the applicable FRF.
- Whether the methods are appropriate and have been applied consistently.

#### General Responses to Assessed RMM

1. Determine whether events occurring upto date of auditor’s report provide audit evidence regarding AE.
2. Test how management made the accounting estimate and the data on which it is based.
3. Test the operating effectiveness of the controls.
4. Develop a point estimate or a range to evaluate management’s point estimate.

#### Specific Responses to Significant Estimation Uncertainties

1. Evaluate the following:
  - How management has considered alternative assumptions or outcomes,
  - How management has addressed estimation uncertainty in making the accounting estimate.
  - Whether the significant assumptions used by management are reasonable.
  - Management’s intent to carry out specific courses of action and its ability to do so.
2. If in auditor’s judgement, management has not adequately addressed the effects of estimation uncertainty, the auditor shall develop a range with which to evaluate the reasonableness of the accounting estimates.



# SA 550 "Related Parties"

## Meaning of Related Party

**EITHER**

Related party as defined in applicable FRF (AS 18).

**OR**

Where applicable FRF establishes minimal or no RP requirements:

- a. A person/entity having control/ significant influence, over reporting entity;
- b. Entity over which reporting entity has control / significant influence, and
- c. Entity under common control with reporting entity, through:
  - Common controlling ownership
  - Owners who are close family members
  - Common key Mngt.

## Auditor's responsibilities in relation to RP

<b>General</b>	Obtain an understanding of RP Relation and Transactions: <ol style="list-style-type: none"> <li>a. To recognize Fraud Risk factors</li> <li>b. To conclude whether F.S. in so far as they are affected by those relations and transactions achieve                         <ul style="list-style-type: none"> <li>• true and fair presentation and</li> <li>• not misleading.</li> </ul> </li> </ol>
<b>Specific (FRF established accounting &amp; Disclosure requirements)</b>	<ul style="list-style-type: none"> <li>• Perform audit procedures to Identify, Assess &amp; Respond to RMM.</li> <li>• Evaluate whether Identified RP relationships &amp; Transactions have been appropriately accounted for &amp; disclosed as per FRF.</li> <li>• Obtain WR from Mngt./TCWG w.r.t.                             <ul style="list-style-type: none"> <li>→ Disclosure to auditor the identity of RP of which they are aware; and</li> <li>→ Appropriate accounting &amp; disclosure as per FRF.</li> </ul> </li> </ul>

## Auditor's Duties

### Risk Assessment procedures

### Responses to Assessed Risks

1	<b>Understanding the Entity's RP relationship and Transactions</b>																								
	a. Auditor to inquire management regarding: <ul style="list-style-type: none"> <li>• Identity of entity's RP, changes from prior period.</li> <li>• Nature of relationships between entity and RP.</li> <li>• Type &amp; purpose of transactions with RP.</li> </ul> b. Obtain understanding whether mngt has established controls to: <ul style="list-style-type: none"> <li>• Identify, account for &amp; disclose RP relationships &amp; transactions.</li> <li>• Authorise &amp; approve significant transactions with RP.</li> <li>• Authorise &amp; approve significant transactions outside normal course of business.</li> </ul>																								
2	<b>Maintaining Alertness for RP Information when Reviewing Records/Documents</b>																								
	<ul style="list-style-type: none"> <li>• Auditor to remain alert when inspecting records w.r.t. info indicating existence of RP relationships or transactions not previously identified or disclosed.</li> <li>• If auditor identifies significant transactions outside entity's normal course of business, inquire of mngt about (a) Nature of these transactions, and (b) Whether RP could be involved.</li> </ul> <p><b>Possible Sources for identification of RP Information:</b></p> <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td>1</td><td>Income Tax Returns</td><td>7</td><td>Shareholder's Register</td></tr> <tr> <td>2</td><td>Internal Audit Report</td><td>8</td><td>Life insurance Polcies</td></tr> <tr> <td>3</td><td>Contracts with Mngt</td><td>9</td><td>Statement of conflict of interest</td></tr> <tr> <td>4</td><td>Contracts outside normal course of business</td><td>10</td><td>Information supplied to regulatory authorities</td></tr> <tr> <td>5</td><td>Contracts re-negotiated</td><td>11</td><td>Specific Invoices from advisors</td></tr> <tr> <td>6</td><td>Register of Investments</td><td>12</td><td></td></tr> </table>	1	Income Tax Returns	7	Shareholder's Register	2	Internal Audit Report	8	Life insurance Polcies	3	Contracts with Mngt	9	Statement of conflict of interest	4	Contracts outside normal course of business	10	Information supplied to regulatory authorities	5	Contracts re-negotiated	11	Specific Invoices from advisors	6	Register of Investments	12	
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3	<b>Identifying Fraud risk factors</b>																								
	Domination of mgmt by a single person or small group without compensating controls is a fraud risk factor. <p><b>Indicators of dominant influence:</b></p> <ul style="list-style-type: none"> <li>• RP has vetoed significant business decisions taken by mgmt or TCWG.</li> <li>• Significant transactions are referred to RP for final approval.</li> <li>• No/ little debate among mgmt or TCWG regarding business proposal initiated by RP.</li> <li>• Transactions involving the RP are rarely independently reviewed / approved.</li> </ul>																								

1	<b>Identification of unidentified / undisclosed RP or RP transaction.</b>
	<ul style="list-style-type: none"> <li>• Communicate to other members of ET.</li> <li>• Request Mngt to identify the transactions with the newly identified RP.</li> <li>• Inquire reasons for mngt failure to identify RP or disclose RP relationship and transactions.</li> <li>• Reconsider the risk that other unidentified RP or undisclosed RP transactions may exist.</li> <li>• If non disclosure appears intentional, evaluate implications for audit.</li> </ul>
2	<b>Identified significant RP Transactions outside Entity's Normal course of Business.</b>
	<ul style="list-style-type: none"> <li>• Inspect underlying contracts to evaluate business rationale.</li> <li>• Examine the terms on which transactions takes place.</li> <li>• Collect evidences w.r.t. approval and authorisation of transaction.</li> <li>• Collect evidences for appropriate accounting &amp; disclosure in compliance of FRF.</li> </ul>
3	<b>Assertions that RP Transactions were conducted on arm Length price.</b>
	<ul style="list-style-type: none"> <li>• Collect SAAE w.r.t. mngt assertion of Arm's length transaction.</li> <li>• Compare transaction prices with the prices for identical transactions prevailing in ordinary course of business.</li> <li>• Engage expert to determine market value.</li> </ul>

# SA 560 "Subsequent Events"

Meaning – Events occurring between the date of F.S. and the date of Auditor's Report AND Facts that become known to auditor after the date of Auditor's report.

Auditor's Duties

Compiled by: CA. Pankaj Garg

## Events occurring between the date of F.S. and the date of Auditor's report

- (i) Perform procedures to obtain SAAE that all events which require adjustment / disclosure have been identified.
- (ii) For the purpose of determining nature and timing of procedures, auditor may:
  - (a) Obtain the **understanding of procedures** applied by mngt for identification of significant events.
  - (b) **Inquire the Management** as to Occurrence of subsequent events which may affect the F.S.
  - (c) Read the **Minutes of Meetings** that held after the B/S date.
  - (d) Study the **Interim Financial Statements**, if any.
- (iii) If auditor identifies any event which require any adjustment/disclosure, he should **ensure its appropriate treatment** in F.S.
- (iv) Obtain a **WR from the Mngt.** that all known events have been appropriately adjusted/disclosed, as the case may be.

### Specific Inquiries to be made from management

1. Whether new commitments, borrowings or guarantees have been entered into.
2. Whether sales or acquisitions of assets have occurred or are planned.
3. Whether there have been increases in capital or issuance of debt instruments.
4. Whether any assets have been appropriated by government or destroyed.
5. Whether there have been any developments regarding contingencies.
6. Whether any unusual accounting adjustments have been made.
7. Whether any events have occurred that will bring into question the appropriateness of accounting policies used in the F.S..
8. Whether any events have occurred that are relevant to the measurement of estimates or provisions made in the F.S.
9. Whether any events have occurred that are relevant to the recoverability of assets.

## Facts that become known to Auditor after date of Auditor's report

### Before issue of F.S.

1. In general Auditor has no obligation.
2. However, in case of significant matter
  - Discuss with Management
  - Determine need to amend F.S.
  - Inquire how mngt intends to address the matter in F.S.
3. If Mngt. amend the F.S. auditor shall
  - Extent procedures to date of new report, and
  - provide a new auditor report on amended F.S.

or

  - Amend the audit report to include an additional date restricted to that amendment and include an EOM/OMP.
4. If mngt refuses to amend the F.S.
  - Modify the report if not yet provided to entity.
  - If report already issued, notify to mngt and TCWG not to issue F.S. to third parties.
  - If mngt still issues F.S., take appropriate action to prevent reliance on auditor's report.

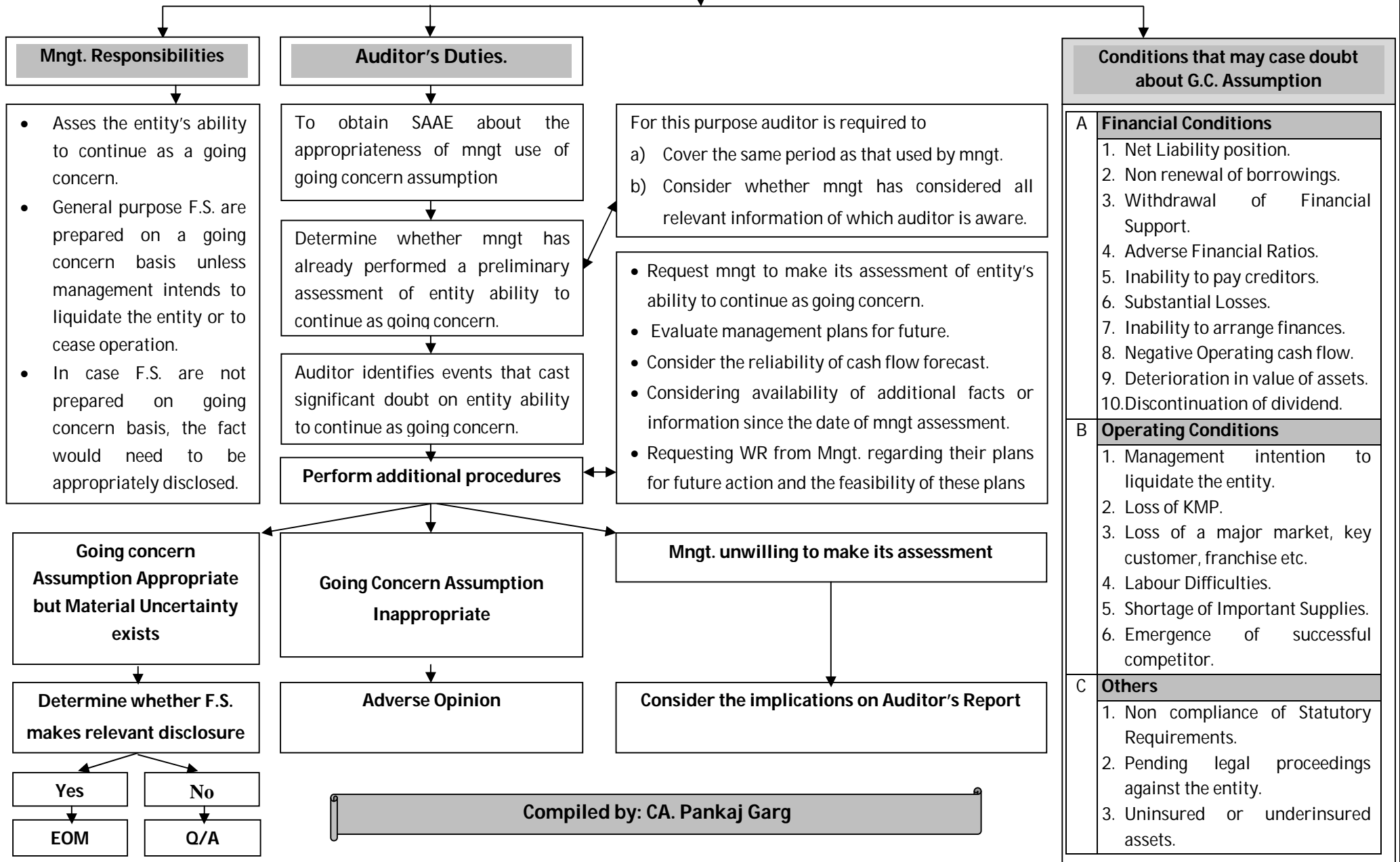
### After issue of F.S.

1. In general Auditor has no obligation.
2. However, in case of significant matter
  - Discuss with Management
  - Determine need to amend F.S.
  - Inquire how mngt intends to address the matter in F.S.
3. If Mngt. amend the F.S. auditor shall
  - Carry out procedures on amended F.S.
  - Review the steps taken by mngt to ensure that recipient of F.S. are informed of the situation.
  - provide a new auditor report on amended F.S.

or

  - Amend the audit report to include an additional date restricted to that amendment and include an EOM/OMP.
4. If mngt refuses to amend the F.S.
  - Notify to mngt and TCWG, that the auditor will seek to prevent reliance on Auditor's Report.
  - If mngt/TCWG does not take necessary steps, take appropriate action to prevent reliance on auditor's report.

# SA – 570 (Revised) "Going Concern"



Compiled by: CA. Pankaj Garg

# SA 580 "Written Representation"

## Meaning and Nature of WR

A written statement by  
Management  
↓  
provided to auditor  
↓  
to confirm certain matters  
or  
to support other audit evidence.

---

- WR recognized as audit evidence as a response to inquiries.
- WR do not provide SAAE

---

- WR should be in the form of a representation letter addressed to Auditor.
- WR shall be obtained for all financial statements and period(s) referred in Auditor's Report.
- Date of WR shall be as near as practicable to the date of the Auditor's report.

## Requirements of SA 580

### Matters for which WR may be obtained

1	<b>Management responsibilities</b>	<p>(a) <b>Preparation and presentation of Financial Statements:</b> In accordance with applicable FRF.</p> <p>(b) <b>Information provided to Auditor:</b> as agreed in terms of engagement</p> <p>(c) <b>Description of management Responsibilities:</b> In the manner as described in terms of engagement</p>
2	<b>Others</b>	<p>As required by other SA Or Where auditor determines that it is necessary to obtain one or more WR.</p>

### Auditor Responses in different Situations

#### Management refuses to provide WR

- Discuss the matter with management
- Re-evaluate the reliability and integrity of management.
- Determine possible effect on the opinion.
- Issue disclaimer of opinion.

#### Reliability of WR is doubtful

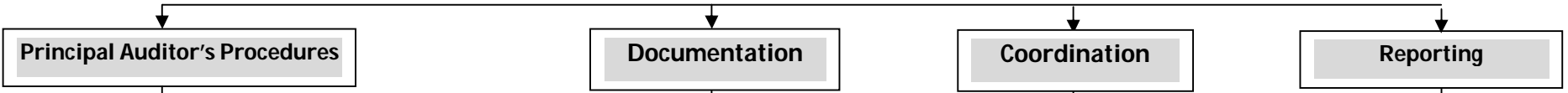
- In case of having concerns about competence and integrity of mngt, determine their effect in reliability of WR and other audit evidence in general.
- IF WR inconsistent with other evidences, perform additional procedures.
- If conclude that WR is not reliable, determine possible effect on audit opinion.
- In case of sufficient doubt over integrity of management, issue a disclaimer of opinion.

**Compiled by:**  
**CA. Pankaj Garg**

# SA – 600 “Using the Work of Another Auditor”

**Applicability:** In situation where an auditor (principal auditor - PA), reporting on the financial information of an entity, uses the work of another auditor (other auditor - OA) w.r.t. to the financial information of one/more components (Division, Branch subsidiary, J. V. etc.), included in the financial information of the entity.

**Non applicability:** (a) Joint auditors      (b) Auditor’s relationship with a predecessor auditor.



### Principal Auditor's Procedures

1. Consider the professional competence of Other Auditor, if Other Auditor is not a member of ICAI.
2. Visit component and examine books of account, if essential.
3. Obtain sufficient appropriate evidence, that work of Other Auditor is adequate for Principal Auditor's purposes.
4. Discuss audit procedures applied by Other Auditor.
5. Review a written summary of Other Auditor's procedures and findings through questionnaires/checklist.
6. Consider significant findings of Other Auditor:
  - Discuss audit findings with OA and Mgt. of component.
  - Perform supplemental tests if necessary.
7. In case Other Auditor is not a professionally qualified auditor - for instance, where a component is situated in foreign country:
  - Procedures mentioned above assume added importance.

### Documentation

1. Components whose FS are audited by Other Auditor and their significance to the financial information of the entity as a whole.
2. Names of the other auditors.
3. Any conclusions reached that individual components are not material.
4. Procedures performed regarding components.
5. Conclusions reached.
6. Manner of dealing with Modified Report of Other Auditor while finalising Principal Auditor's Report.

### Coordination

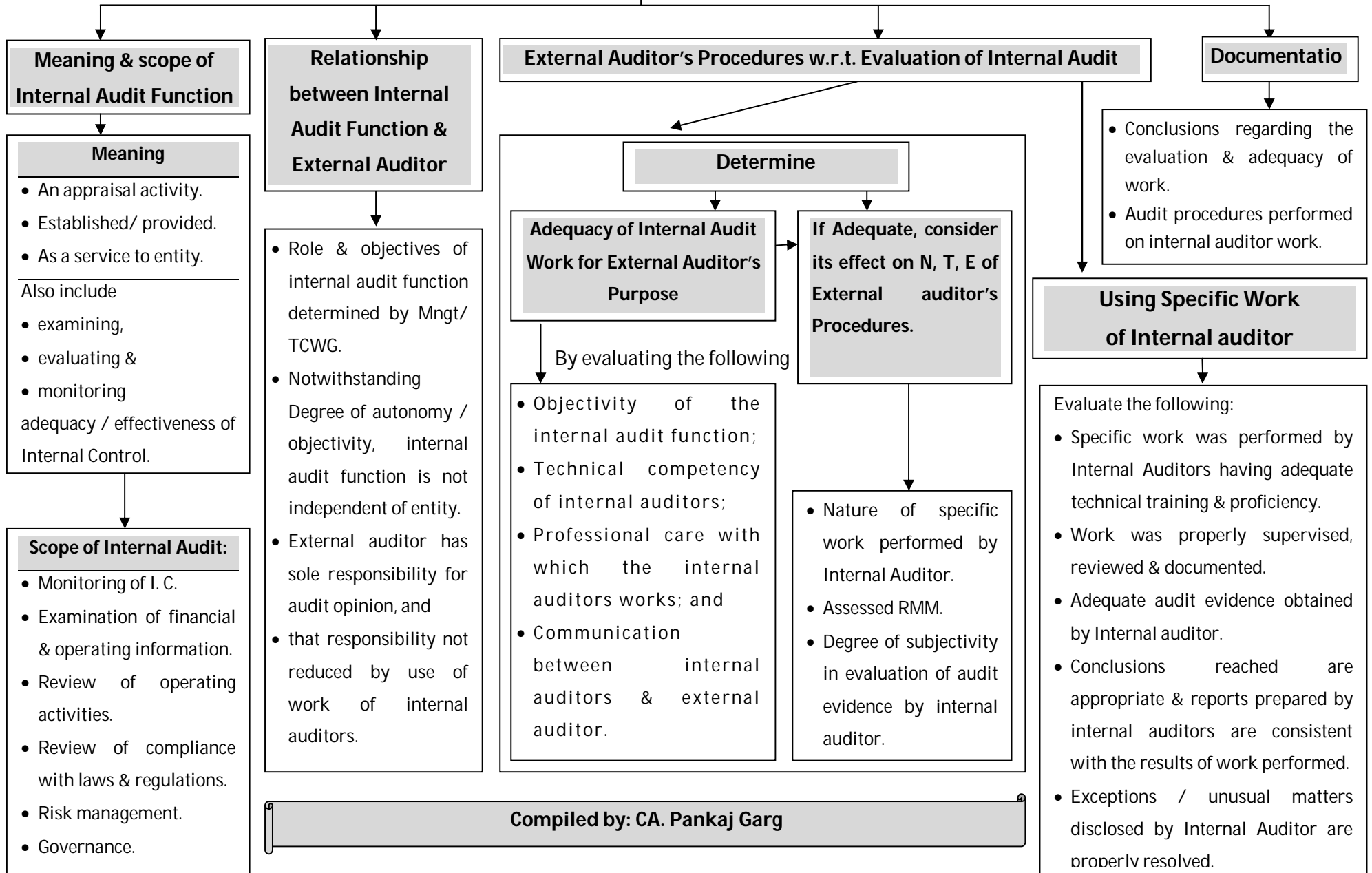
1. Sufficient liaison/co-ordination between Principal and Other auditor.
2. Principal auditor may require Other Auditor to answer a detailed questionnaire.
3. Other Auditor should coordinate with Principal Auditor:
  - Adhering to time-table.
  - Bringing to the attention of PA any significant finding.
  - Compliance with relevant statutory requirements.
  - Respond to detailed questionnaire.

### Reporting

1. Express a **qualified / disclaimer of opinion** because of scope limitation:
  - If Principal Auditor concludes that he cannot use the work of Other Auditor;
  - PA unable to perform sufficient additional procedures regarding FI of the component audited by OA.
2. Report should state clearly **division of responsibility** between PA and OA.

**Compiled by: CA. Pankaj Garg**

# SA 610 (Revised) "Using the Work of Internal Auditors"



**Compiled by: CA. Pankaj Garg**

## SA 620 "Using the Work of Auditor's Expert"

### Meaning of Auditor's Expert

- An individual or organisation
- possessing expertise in field other than accounting/auditing,
- whose work is used by the auditor
- to assist the auditor in obtaining SAAE.

### Areas where work of AE can be used

- Valuation of complex financial instruments, L & B, P & M, jewelry, works of art, antiques, intangible assets, assets acquired and liabilities assumed in business combinations and assets that may have been impaired.
- Actuarial calculation of liabilities associated with insurance contracts or employee benefit plans.
- Estimation of oil and gas reserves.
- Valuation of environmental liabilities, and site clean-up costs.
- Interpretation of contracts, laws and regulations.
- Analysis of complex or unusual tax compliance issues.

### Procedures to be followed while using the work of auditor's expert

<p><b>1 Determining need for an Auditor's Expert</b></p> <p>An auditor's expert may be needed to assist the auditor for the followings:</p> <ul style="list-style-type: none"> <li>• Obtaining an understanding of entity &amp; its environment, including IC.</li> <li>• Identifying and assessing the risks of material misstatement.</li> <li>• Determining &amp; implementing overall responses to assessed risks.</li> <li>• Designing and performing further audit procedures to respond to assessed risks.</li> <li>• Evaluating the sufficiency and appropriateness of audit evidence obtained.</li> </ul>	<p><b>4 Agreement with Auditor's Expert</b></p> <p>Need to be in writing and cover the followings:</p> <ul style="list-style-type: none"> <li>• Nature, scope and Objectives of Auditor's Expert work.</li> <li>• Respective Role and Responsibilities of Auditor and auditor's Expert.</li> <li>• NTE of Communication including form of report.</li> <li>• Confidentiality requirements to be observed by Auditor's Expert.</li> </ul>
<p><b>2 Evaluate Competence, Capability and Objectivity of the Expert</b></p> <p><b>Source of Information for evaluation:</b></p> <ul style="list-style-type: none"> <li>• Personal Experience with previous work.</li> <li>• Discussion with that expert.</li> <li>• Discussion with other Auditors.</li> <li>• Knowledge of expert's qualification, memberships, other forms of recognitions.</li> <li>• Published books or papers.</li> <li>• Auditor's firm Q. C. Policies and Procedures.</li> </ul>	<p><b>5 Evaluate appropriateness of Expert work</b></p> <ul style="list-style-type: none"> <li>• <b>Finding &amp; Conclusion</b> – Relevance, Reasonableness &amp; Consistency with other A.E.</li> <li>• <b>Assumptions and Methods</b> – Relevance and Reasonableness.</li> <li>• <b>Source Data</b> – Relevance, Completeness and accuracy.</li> </ul>
<p><b>3 Obtain an understating of expert work</b></p> <ul style="list-style-type: none"> <li>• To enable the auditor to determine the nature, scope and objectives of that expert's work for auditor's purposes.</li> <li>• Evaluate the adequacy of that work for the auditor's purposes.</li> </ul>	<p><b>6 Expert work not adequate for audit purposes</b></p> <ul style="list-style-type: none"> <li>• If Auditor concludes that work of auditor's expert is not adequate for the auditor's purposes and</li> <li>• auditor cannot resolve the matter through the additional audit procedures,</li> <li>• it may be necessary to express a modified opinion.</li> </ul>

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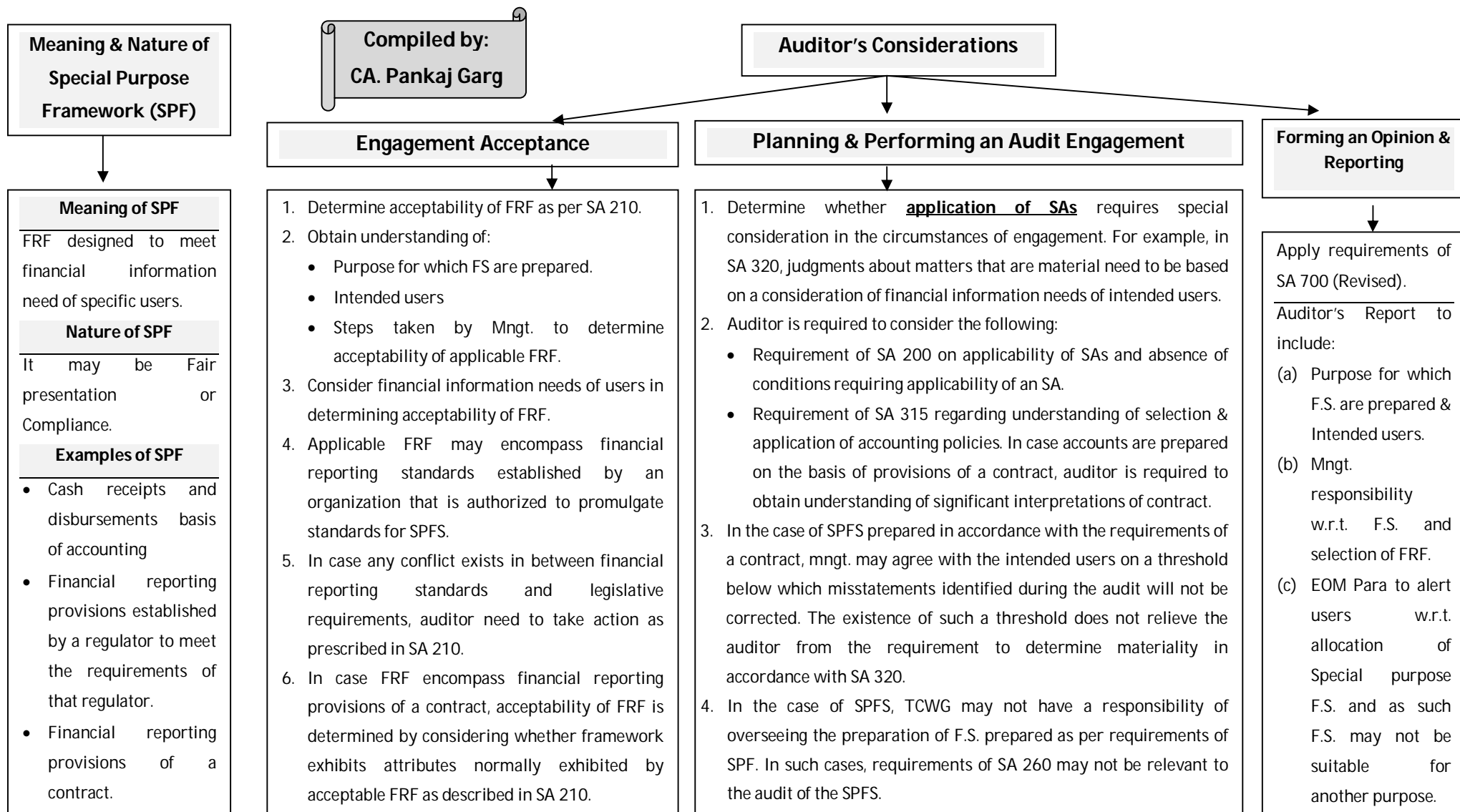
### Reference to the Auditor's Expert in the Auditor's Report

- No reference required in case of unmodified Audit Report unless required by L & R.
- In case of modified reports, it may be appropriate to refer to the auditor's expert, to explain the nature of the modification. In such case, auditor may need the permission of the auditor's expert before making such a reference..

# SA 800 – “Special Considerations – Audit of F.S. prepared in accordance with SPF”

**Scope of SA 800:** SA 800 deals with Special considerations in application of SAs in audit of F.S. (Complete set) prepared in accordance with SPF.

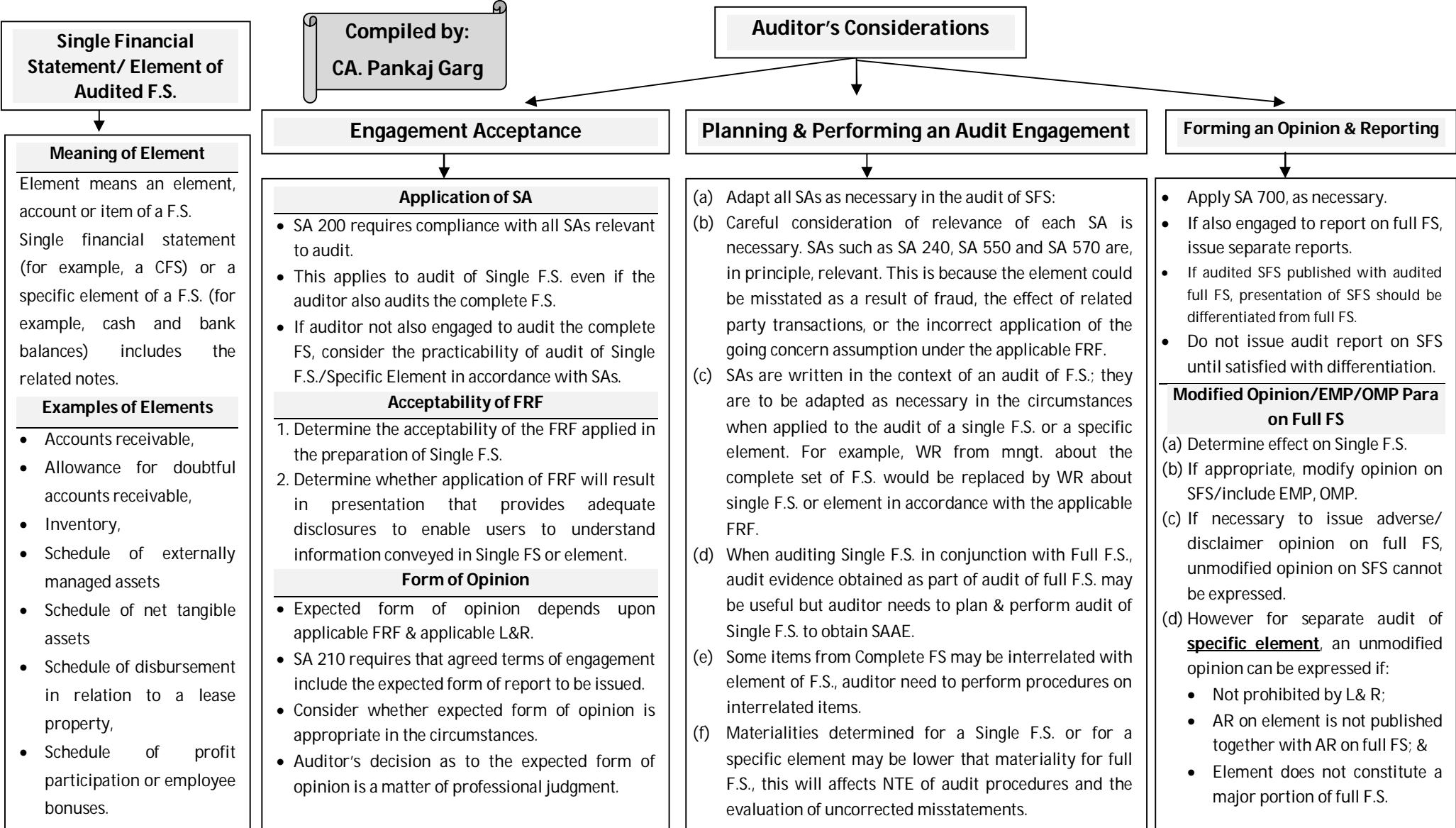
**Objective of Auditor:** to address appropriately special considerations w.r.t. (a) Engagement Acceptance (b) Planning & performance (c) Opinion & Reporting.





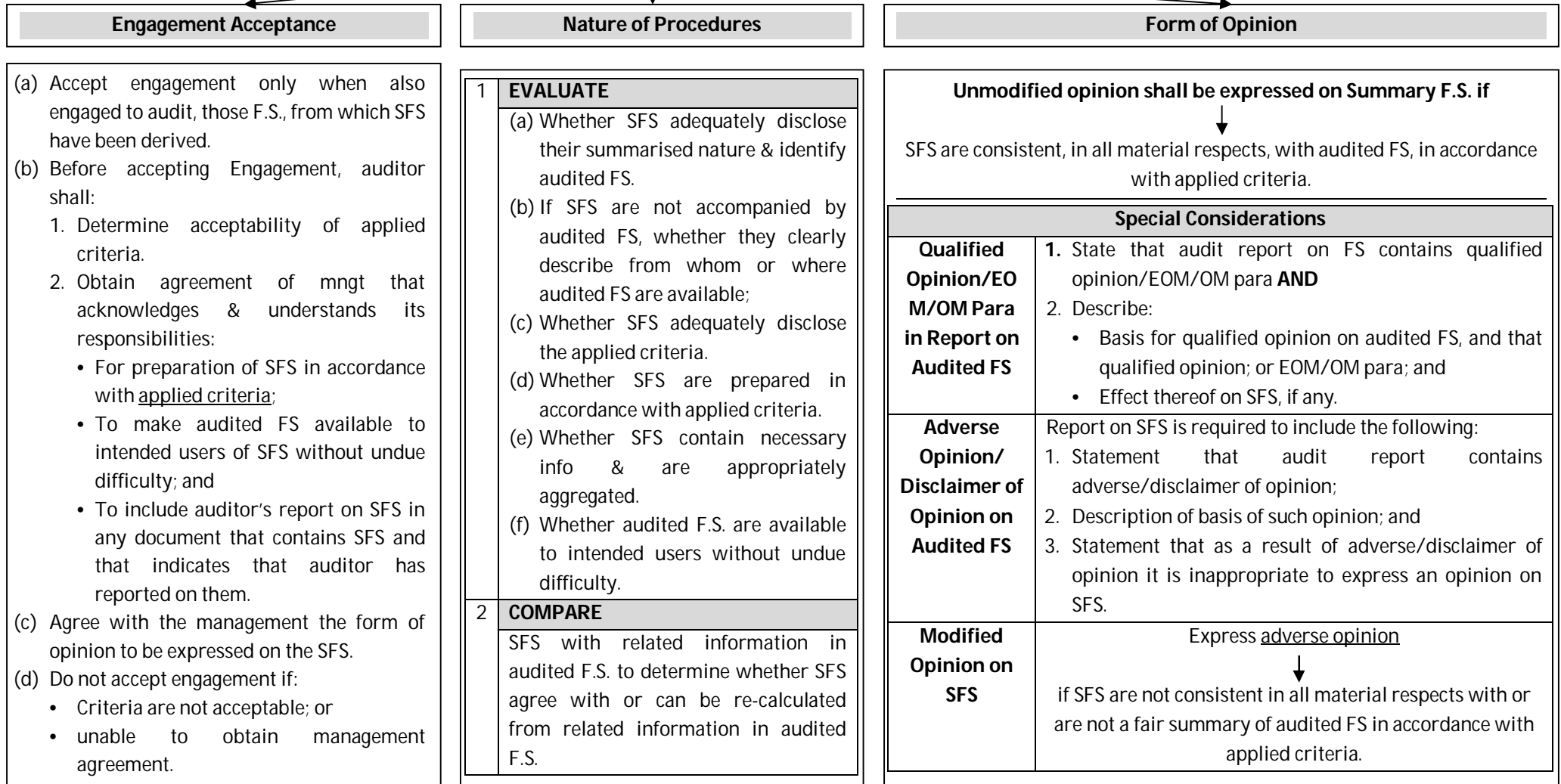
# SA 805 "Special Considerations – Audits of Single F.S. and Specific Elements, Accounts or Items of a F.S."

**Scope of SA 805:** SA 805 deals with Special considerations in application of SAs in audit of Single F.S. or Single Element/Account or Item of F.S.  
**Objective of Auditor:** to address appropriately special considerations w.r.t. (a) Engagement Acceptance (b) Planning & performance (c) Opinion & Reporting.



# SA 810 "Engagements to Report on Summary Financial Statements (SFS)"

- **Scope of SA 810:** deals with auditor's responsibilities, when engaged to report, on SFS, derived from FS audited in accordance with SA, by that same auditor.
- **Objective of Auditor:** to determine appropriateness of accepting the engagement & form opinion based on evaluation of Conclusions drawn from evidence obtained.
- **Meaning of Summary Financial Statements (SFS):** Historical financial info that is derived from FS, but contains less detail than FS, while still providing a structured representation consistent with that provided by entity's F.S.



## Chapter 2 - Audit Strategy, Planning and Programming

Audit Strategy		Audit Planning		Audit Programming											
<b>Meaning:</b> Designing Audit Approaches to achieve necessary audit assurance at the lowest cost.		<b>Meaning</b>	→ Developing an overall plan for the expected scope and conduct of the audit and → Developing an audit programme showing NTE of Audit procedures	<b>Meaning</b>	<ul style="list-style-type: none"> <li>• Detailed plan of work</li> <li>• comprises of techniques and procedures,</li> <li>• may also contain objectives for each audit step.</li> </ul>										
<b>Steps involved in Audit Strategy</b> 1. <b>Obtaining knowledge of business:</b> It provides a frame of reference within which the auditor exercises his professional judgement to assess risk, to plan audit, to evaluate audit evidence and providing quality services. 2. <b>Performing Analytical Procedures at Initial Stages:</b> To assess the potential for material misstatement in the F.S. as a whole. 3. <b>Evaluating Inherent Risk:</b> On the basis of prior audit experience, controls exercised by management, significant changes since last assessment.			<b>Aspects to be covered</b>		<ul style="list-style-type: none"> <li>• Acquiring knowledge of client accounting system, policies and internal control procedures.</li> <li>• Establishing the expected degree of reliance on internal control.</li> <li>• Determining the NTE of audit procedures.</li> <li>• Coordinating the work to be performed.</li> </ul>	<b>Matters to be considered</b>	<ul style="list-style-type: none"> <li>• Nature of business.</li> <li>• Overall Plan</li> <li>• System of internal control and accounting procedures.</li> <li>• Size and structure of organization.</li> <li>• Information regarding the organization.</li> <li>• Accounting policies followed.</li> </ul>								
<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th colspan="2" style="text-align: center;">Factors to be evaluated to assess inherent risk</th> </tr> <tr> <th style="text-align: center;">At the level of F.S.</th> <th style="text-align: center;">At the level of A/c Balance</th> </tr> </thead> <tbody> <tr> <td style="vertical-align: top;"> <ul style="list-style-type: none"> <li>• Integrity of Management.</li> <li>• Management experience</li> <li>• Changes in management</li> <li>• Pressures on Management</li> <li>• Nature of entity business.</li> <li>• Factors affecting industry.</li> </ul> </td> <td style="vertical-align: top;"> <ul style="list-style-type: none"> <li>• Quality of Accounting System.</li> <li>• Susceptibility to Misstatement / Misappropriation of assets.</li> <li>• Complexity of transactions.</li> <li>• Degree of judgement involved.</li> <li>• Unusual transactions</li> </ul> </td> </tr> </tbody> </table>		Factors to be evaluated to assess inherent risk		At the level of F.S.	At the level of A/c Balance		<ul style="list-style-type: none"> <li>• Integrity of Management.</li> <li>• Management experience</li> <li>• Changes in management</li> <li>• Pressures on Management</li> <li>• Nature of entity business.</li> <li>• Factors affecting industry.</li> </ul>	<ul style="list-style-type: none"> <li>• Quality of Accounting System.</li> <li>• Susceptibility to Misstatement / Misappropriation of assets.</li> <li>• Complexity of transactions.</li> <li>• Degree of judgement involved.</li> <li>• Unusual transactions</li> </ul>	<b>Importance of planning</b>	<ul style="list-style-type: none"> <li>• To devote attention to important areas</li> <li>• Identify &amp; resolve potential problems.</li> <li>• Organized and managed audit.</li> <li>• Selection of suitable ET.</li> <li>• Coordination of work done</li> <li>• Direction and supervision of engagement team.</li> </ul>	<b>Development of Audit programme</b>	<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: center;">First Time Audit</th> <th style="text-align: center;">Subsequent Engagement</th> </tr> </thead> <tbody> <tr> <td style="vertical-align: top;"> <ul style="list-style-type: none"> <li>→ Draw a broad outline</li> <li>→ Filled up the details on a consideration of deficiencies in internal control.</li> <li>→ Determine the special procedures needs to be applied.</li> </ul> </td> <td style="vertical-align: top;"> <ul style="list-style-type: none"> <li>Review earlier programme and modified on account of:                             <ul style="list-style-type: none"> <li>• Experience gained during the previous audit.</li> <li>• Important changes in internal control system, accounting procedures etc.</li> <li>• Evaluation of internal control for current year.</li> </ul> </li> </ul> </td> </tr> </tbody> </table>	First Time Audit	Subsequent Engagement	<ul style="list-style-type: none"> <li>→ Draw a broad outline</li> <li>→ Filled up the details on a consideration of deficiencies in internal control.</li> <li>→ Determine the special procedures needs to be applied.</li> </ul>
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4. <b>Evaluating Internal Control System:</b> By documenting the extent of computerization, preparing/updating flowcharts to record the transactions. 5. <b>Formulating Audit Strategy:</b> Requires consideration of:		<b>Factors to be considered</b>	<ul style="list-style-type: none"> <li>• Terms of engagement</li> <li>• Nature &amp; timing of reports</li> <li>• Legal or statutory requirements.</li> <li>• Accounting policies &amp; changes therein.</li> <li>• Effects of new accounting/auditing pronouncements.</li> <li>• Identification of significant audit areas.</li> <li>• Setting of materiality levels.</li> <li>• Degree of reliance on internal control.</li> </ul>	<b>Circumstances requiring changes</b>	<ul style="list-style-type: none"> <li>1. Substantial increase in Volume of turnover.</li> <li>2. Significant changes in accounting procedures.</li> <li>3. Observation w.r.t. ineffective internal control.</li> <li>4. Substantial increase in book debts or inventory.</li> <li>5. Suspicion as to misappropriation of assets.</li> </ul>										
• Engagement objective • Knowledge of clients business • Preliminary judgements as to materiality • Identified inherent risks • Extent of compliance testing • NTE of Substantive testing • Points relating to planning and controlling the audit.			<b>Relationship - Audit Strategy &amp; Audit Planning</b> <ul style="list-style-type: none"> <li>• Inter-related to each other because change in one would result change in other.</li> <li>• Audit strategy is prepared before the audit plan and provides the guidelines for developing the audit plan.</li> </ul>												
<b>Benefits</b> 1. Employment of Qualitative Resources. 2. Allocation of appropriate quantity of resources. 3. Determining the timing of deployment of resources. 4. Better management of resources in terms of direction, supervision, timing of team meetings etc.															

## CHAPTER 3 – RISK ASSESSMENT & INTERNAL CONTROL

1. AUDIT RISK			2. INTERNAL CONTROL												
<b>Meaning</b>	Risk that the auditor gives an inappropriate audit opinion when the financial statements are materially misstated.		<b>Definition</b>	The process designed, implemented and maintained, by TCWG and Management, to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, safeguarding of assets, and compliance with applicable laws and regulations.											
<b>Consideration</b>	Audit Risk need to be considered at Overall Level as well as at the level of Individual account balance or classes of transactions														
<b>Components</b>	<b>Inherent</b>	<b>Meaning</b>	<b>Factors to be considered</b>	<b>Control Objectives of Accounting Control System</b>	1. Whether all transactions are recorded; 2. Whether recorded transactions are real; 3. Whether all recorded transactions are properly valued; 4. Whether all transactions are recorded timely; properly posted; 5. Whether all transactions are properly classified & disclosed; properly summarized.										
		Susceptibility of an account balance or class of transaction to a material misstatement, assuming that there are no internal controls.				<ul style="list-style-type: none"> <li>• Experience on prior audits.</li> <li>• Controls established by Mngt.</li> <li>• Significant changes from last assessment.</li> </ul>									
	<b>Control</b>	<b>Meaning</b>	<b>Steps in Assessment of Control Risk</b>		<b>Methods of Collecting info to review I.C.</b>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 15%; text-align: center;"><b>Narrative Records</b></td> <td>Complete and exhaustive description of system as found in the operation by the auditor</td> <td style="text-align: center;"><b>Flow Chart</b></td> </tr> <tr> <td style="text-align: center;"><b>Check List</b></td> <td>Series of instructions and/or questions which a member of auditing staff must follow.</td> <td> <ul style="list-style-type: none"> <li>• Graphic presentation of I.C. of various sections in form of a diagram full with lines &amp; Symbols.</li> <li>• Provide most concise and comprehensive way to review I.C.</li> <li>• Provide a neat visual picture of various activities involving flow of documents through various stages, authorizations required, filing of documents, final disposal .</li> </ul> </td> </tr> <tr> <td style="text-align: center;"><b>IC Questionnaire</b></td> <td>Set of Questions designed to provide a thorough view of state of I.C.</td> <td></td> </tr> </table>	<b>Narrative Records</b>	Complete and exhaustive description of system as found in the operation by the auditor	<b>Flow Chart</b>	<b>Check List</b>	Series of instructions and/or questions which a member of auditing staff must follow.	<ul style="list-style-type: none"> <li>• Graphic presentation of I.C. of various sections in form of a diagram full with lines &amp; Symbols.</li> <li>• Provide most concise and comprehensive way to review I.C.</li> <li>• Provide a neat visual picture of various activities involving flow of documents through various stages, authorizations required, filing of documents, final disposal .</li> </ul>	<b>IC Questionnaire</b>	Set of Questions designed to provide a thorough view of state of I.C.	
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<b>IC Questionnaire</b>	Set of Questions designed to provide a thorough view of state of I.C.														
Risk that material misstatements will not be prevented or detected and corrected on a timely basis by the internal control system.		1. Preliminary assessment of control risk. 2. Documentation of understanding & assessment of control risk. 3. Performing Tests of Controls 4. Final Assessment of Control Risk.													
<b>Detection</b>	<ul style="list-style-type: none"> <li>• Risk that the substantive procedures performed by auditor fails to detect material misstatements.</li> <li>• Some detection risk would always be present even if an auditor was to examine 100% of the account balance or class of transactions.</li> </ul>		<b>Surprise check in Internal Control</b>	<ul style="list-style-type: none"> <li>• Useful method to determine whether errors exist and where they exist</li> <li>• ICAI Recommendation – Surprise checks should form part of normal audit.</li> <li>• Surprise check should be made at least once in the course of an audit.</li> </ul>	<b>Letter of weakness</b>	<ul style="list-style-type: none"> <li>• SA 260 - Weaknesses in I.C. identified during the audit should be communicated to mngt &amp; TCWG.</li> <li>• Helps TCWG to improve the systems.</li> <li>• Must indicate that evaluation of I.C. is done to determine NTE of further audit procedures.</li> </ul>									
<b>Relationships</b>	<b>IR &amp; CR</b>	<ul style="list-style-type: none"> <li>• IR and CR are highly interrelated as in many cases IR management reacts to IR by designing accounting and internal control systems to prevent or detect and correct misstatements.</li> <li>• As a result, auditor needs to make a combined assessment of IR &amp; CR as RMM.</li> </ul>		<b>3. INTERNAL CHECK</b>											
	<b>RMM &amp; R</b>	<ul style="list-style-type: none"> <li>• Inverse relationship between RMM and DR.</li> <li>• When RMM is high, DR needs to be low to reduce audit risk to an acceptable low level.</li> <li>• When RMM is low, auditor can accept a higher DR.</li> <li>• Mathematically <math>AR = IR \times CR \times DR</math></li> </ul>		<b>Meaning</b>	Checks on day to day transactions, which operate continuously as a part of routine system, whereby work of one person is proved independently to work of another, the object being prevention and earlier detection of error or fraud.										
<b>Risk Based Audit</b>	<b>Meaning</b>		<b>Stages</b>		<b>Objectives</b>	<ul style="list-style-type: none"> <li>• To detect fraud and error with ease.</li> <li>• Avoid &amp; minimize possibility of occurrence of fraud &amp; error.</li> <li>• Increase efficiency of staff.</li> <li>• Protect integrity of business.</li> <li>• Prevent misappropriation of cash &amp; falsification of accounts.</li> </ul>									
	An audit Approach that 1. Analyses Audit Risks, 2. Set materiality thresholds based on audit risk analysis and 3. develop audit programmes that allocates a larger portion of resources to high risk areas.		1. Understanding the auditee operations. 2. Determination of residual Risk 3. Manage residual Risk. 4. Reporting to Auditee.				<b>Considerations</b>	<ul style="list-style-type: none"> <li>• No single person should have an Independent Control.</li> <li>• Duties of staff members should be changed from time to time.</li> <li>• Every member should be encouraged to go on leave atleast once.</li> <li>• Persons having physical custody of assets must not be allowed access to books of accounts.</li> <li>• Implement Budgetary control procedures.</li> <li>• Judicious distribution of financial and administrative powers.</li> <li>• Procedures should be laid down for physical verification.</li> <li>• Accounting procedures should be reviewed periodically.</li> </ul>							

## AUDIT IN CIS ENVIRONMENT - BASICS

Types of Processing System		Impact of Changes from Manual Processing to Computerised Processing	Characteristics of CIS Environment
Batch Processing System	Online Real Time Processing System		
<p><b>Meaning:</b> Transactions are accumulated &amp; processed in group.</p> <p><b>Steps:</b> 4 steps</p> <ul style="list-style-type: none"> <li>• Occurrence of transaction.</li> <li>• Recorded in transaction file</li> <li>• Updation of master file.</li> <li>• Generation of output.</li> </ul> <p><b>Advantages:</b> Simple, existence of Audit Trail, processing volume of transactions.</p> <p><b>Limitations:</b> Time gap in between occurrence &amp; processing.</p>	<p><b>Meaning:</b> Transactions are processed as they occurred.</p> <p><b>Features:</b></p> <ul style="list-style-type: none"> <li>• Validation Check.</li> <li>• Online access of system to users.</li> <li>• Non-existence of audit Trail.</li> <li>• Unrestricted access to programmers.</li> </ul> <p><b>Advantages:</b> Immediate processing &amp; continuous updation.</p> <p><b>Limitations:</b> Non-existence of Audit Trail.</p>	<ol style="list-style-type: none"> <li>1. <b>Process of recorded Transactions:</b> as observed in manual system may not be followed strictly.</li> <li>2. <b>Form of Accounting Records:</b> Primary records may be abandoned.</li> <li>3. <b>Use of Loose-leaf stationeries:</b> as against bound hand written books in manual.</li> <li>4. Use of Accounting Code.</li> <li>5. Absence of link between transactions - Loss of Audit Trail.</li> </ol>	<ol style="list-style-type: none"> <li>1. Lack of Transaction Trail</li> <li>2. Uniform Processing of Transaction</li> <li>3. Lack of Segregation of Functions.</li> <li>4. Potential for Errors and Irregularities</li> <li>5. Automatic execution of transactions.</li> <li>6. Dependence of other Controls.</li> <li>7. Potential for increased management supervision.</li> <li>8. Potential for use of CAAT.</li> </ol>

## AUDIT IN CIS ENVIRONMENT – INTERNAL CONTROLS – MANAGEMENT PERSPECTIVE (DESIGN AND EXERCISE)

Controls to be designed and exercised			Problems in implementation of Internal Control in CIS
General CIS Controls	CIS application Controls	Other Safeguards	
<p><b>Purpose:</b> To establish framework of overall control over CIS Activities &amp; provide reasonable assurance that overall objectives of I.C. are achieved.</p> <p><b>Types:</b> 5 Types</p> <ol style="list-style-type: none"> <li>1. Organisation Structure &amp; Management Controls.</li> <li>2. Application System Development and Maintenance Controls.</li> <li>3. Computer Operations Controls.</li> <li>4. System Software Controls</li> <li>5. Data Entry and Program Controls</li> </ol>	<p><b>Purpose:</b> To establish specific control procedures over the accounting applications and provide reasonable assurance that all transactions are authorized, recorded and processed on a timely basis.</p> <p><b>Types:</b> 3 Types</p> <ol style="list-style-type: none"> <li>1. Controls over Input</li> <li>2. Controls over processing</li> <li>3. Controls over Output.</li> </ol>	<ol style="list-style-type: none"> <li>1. Offsite back up of data and computer programmes</li> <li>2. Recovery procedures in the event of loss of data.</li> <li>3. Provision for offsite processing</li> </ol>	<ol style="list-style-type: none"> <li>1. Separation of Duties.</li> <li>2. Delegation of authority and Responsibility.</li> <li>3. Availability of competent and Trustworthy person.</li> <li>4. System of Authorisation due to inbuilt controls.</li> <li>5. Non-Existence of adequate Documents &amp; Records.</li> <li>6. Physical Control over assets and records due to risk of loss and unauthorised access.</li> <li>7. Management Supervision over employees as work may have to be carried out remotely.</li> <li>8. Difficult in detection of unauthorised modifications to programs or data files.</li> </ol>

## AUDIT IN CIS ENVIRONMENT – INTERNAL CONTROLS – AUDITOR PERSPECTIVE (EVALUATION)

Controls to be Evaluated over Data	Clauses of Controls to be evaluated	Audit Plan to determine Reliability of Controls	Factors to be considered to evaluate Reliability of Accounting & Internal Control System
<ol style="list-style-type: none"> <li>1. <b>Organisation structure Control</b> – Authority and Responsibility</li> <li>2. <b>Documentation Control</b> – Existence, Adequacy, Authorisation for Changes</li> <li>3. <b>Access Control</b> – Unauthorised access</li> <li>4. <b>Input Control</b> – Authorised and Validation Check</li> <li>5. <b>Processing Control</b> – Integrity of data, validation check</li> <li>6. <b>Recording Control</b> – records to be kept free of errors</li> <li>7. <b>Storage Control</b> – Back up and recover facilities</li> <li>8. <b>Output Control</b> – access to authorized person, audit trail</li> </ol>	<ol style="list-style-type: none"> <li>1. <b>Authenticity:</b> to verify the identity of individuals involved.</li> <li>2. <b>Accuracy:</b> to ensure correctness of data</li> <li>3. <b>Completeness:</b> to ensure that no data is missing.</li> <li>4. <b>Privacy:</b> to ensure protection of data.</li> <li>5. <b>Audit Trail:</b> to ensure traceability of all events.</li> <li>6. <b>Redundancy:</b> to avoid data duplication.</li> <li>7. <b>Existence:</b> to ensure ongoing availability of system resources.</li> <li>8. <b>Asset Safeguarding:</b> protection of resources from destruction.</li> <li>9. <b>Effectiveness:</b> to ensure that system achieves its goals.</li> <li>10. <b>Efficiency:</b> use of minimum resources to achieve goals.</li> </ol>	<ol style="list-style-type: none"> <li>1. Existence and Effectiveness on Controls desired.</li> <li>2. Generality versus specialty of control.</li> <li>3. Focus on:                             <ul style="list-style-type: none"> <li>• Preventive Controls</li> <li>• Detective Controls</li> <li>• Corrective Controls</li> </ul> </li> <li>4. Number of components used to execute the control.</li> </ol>	<ol style="list-style-type: none"> <li>(i) Availability of authorized, correct &amp; complete data.</li> <li>(ii) Timely detection and correction of errors</li> <li>(iii) Existence of data recovery arrangement &amp; back up system.</li> <li>(iv) Adequate data security against fire &amp; other calamities, etc.</li> <li>(v) Prevention of unauthorized amendments to the program.</li> <li>(vi) Provision for Offsite processing in the event of disaster.</li> <li>(vii) Safe custody of source code of application software.</li> <li>(viii) Accuracy and completeness of output.</li> <li>(ix) Prevention of loss of data due to processing failure.</li> </ol>

## AUDIT IN CIS ENVIRONMENT – AUDIT TECHNIQUES

Audit Trail	CAAT – Computer Assisted Audit Techniques		
	Meaning, Need and Uses	Commonly Used CAAT	Considerations in Use of CAAT
<p><b>Meaning:</b> Facility to trace individual transactions from source to completion or vice versa. In CIS Environment, audit trail is often missing or sketchy.</p> <p><b>Reason for non-existence of Audit Trail in CIS:</b></p> <ol style="list-style-type: none"> <li>1. Non-availability of source documents.</li> <li>2. Replacement of ledger summaries by Master Files.</li> <li>3. Generation of reports on exception only.</li> </ol> <p><b>Remedies for audit trail:</b></p> <ul style="list-style-type: none"> <li>• Use of Computer Programs.</li> <li>• Use of Test Packs (Test Data)</li> </ul>	<p><b>Meaning:</b> Those auditing Techniques that take assistance of computer for being applied to audit.</p> <p><b>Need for CAAT:</b> arises due to</p> <ol style="list-style-type: none"> <li>1. Absence of Input Documents.</li> <li>2. System generated Transactions;</li> <li>3. the lack of a visible audit trail; and</li> <li>4. the lack of visible output.</li> </ol> <p><b>Uses of CAAT:</b> in performing various auditing procedures:</p> <ol style="list-style-type: none"> <li>1. <i>Compliance Test of General CIS Controls:</i> through Test Data</li> <li>2. <i>Compliance Test of CIS Application Controls:</i> through Test Data</li> <li>3. <i>Test of details of transactions and balances:</i> by use of Audit Software</li> <li>4. <i>Analytical Review:</i> by use of Audit Software</li> </ol>	<ol style="list-style-type: none"> <li>1. <b>Audit Software:</b> Computer programs used by auditor to process data of audit significance. 3 types                             <ul style="list-style-type: none"> <li>• <b>Package Programs:</b> Generalized programs designed to perform data processing.</li> <li>• <b>Purpose Written Programs:</b> Programs designed to perform audit task in specific circumstances.</li> <li>• <b>Utility Programs:</b> Programs to perform common data processing functions. Not designed for audit purpose.</li> </ul> </li> <li>2. <b>Test Data:</b> A set of Hypothetical data entered into computer system of organisation and result obtained is compared with pre-determined results. It is used in an “<b>Integrated Test Facility (ITF)</b>” where a dummy unit is established and to which test transactions are posted during normal processing. Under these circumstances, auditor is required to ensure that test transactions are subsequently eliminated.</li> <li>3. <b>Tagging and Tracing:</b> It involves tagging the client’s input data in such a way that relevant information is displayed at key points. It uses the actual data and hence no need of reversal.</li> </ol>	<ol style="list-style-type: none"> <li>1. Availability of Sufficient IT knowledge and Expertise.</li> <li>2. Incompatibility between CAAT and Computer Facilities.</li> <li>3. Impracticability of manual test.</li> <li>4. Impact of effectiveness and efficiency in extracting a data</li> <li>5. Time Constraints.</li> </ol>

Control Procedures while using CAAT	Essential features of Computer Audit Program	Collection & Evaluation of Audit Evidence–Reasons for Changes
<p><b>Audit Software Application:</b></p> <ol style="list-style-type: none"> <li>1. Participating in design and testing.</li> <li>2. Checking the coding of the programme.</li> <li>3. Ensure Compatibility of software with entity’s operating system.</li> <li>4. Running the audit software on small test files before running on main data files.</li> <li>5. Ensuring that the correct files were used.</li> <li>6. Obtaining evidence that the audit software functioned as planned.</li> <li>7. Establishing security measures to safeguard against manipulations of the entity’s data files.</li> </ol> <p><b>Test Data Application:</b></p> <ol style="list-style-type: none"> <li>1. Controlling the sequence of submissions of test data.</li> <li>2. Performing test runs containing small amounts of test data before submitting the main audit test data.</li> <li>3. Comparing results of the test data with pre-determined results.</li> <li>4. Ensure Test data is processed over the answered version of programmes.</li> <li>5. Ensure that the programmes used to process the test data were applied throughout the applicable audit period.</li> </ol>	<ol style="list-style-type: none"> <li>1. Simplicity</li> <li>2. Understandability</li> <li>3. Adaptability</li> <li>4. <b>Vendor Technical Support</b> – Installation, documentation, training, updations.</li> <li>5. <b>Capability of statistical Sampling</b> – at different confidence levels.</li> <li>6. <b>Acceptability</b> – to both auditor and computer centre in terms of compatibility, interference etc.</li> <li>7. <b>Processing Capabilities</b> - Multiple applications, extended data selection, stratification etc.</li> <li>8. Ability to prepare multiple reports.</li> </ol>	<p><b>Reasons for Changes in Collection of Evidences:</b></p> <ol style="list-style-type: none"> <li>1. Existence of diverse and complex range of I.C. technology.</li> <li>2. Rapid development in Hardware and Software technology.</li> <li>3. Cryptographic Controls to protect the privacy of data.</li> <li>4. Non-possibility of collection of audit evidence by manual means.</li> </ol> <p><b>Reasons for Changes in Evaluation of Evidences:</b></p> <ol style="list-style-type: none"> <li>1. Increasing complexity of computer system and control technology.</li> <li>2. Updation of Multiple data by a single input transaction.</li> <li>3. Deterministic nature of errors.</li> <li>4. Speed at which errors are generated and the high cost and effort to correct and rerun the program.</li> </ol>

### IMPORTANT SECTIONS OF CHARTERED ACCOUNTANT ACT, 1949

<b>Sec. 2(2)(iv)</b>	<p>A member of the Institute shall be deemed "to be in practice" when <b>individually or in partnership</b> with <b>Chartered Accountants in practice</b>, he, in <b>consideration of remuneration</b> received or to be received renders such other services as, in the opinion of the Council, are or may be rendered by a Chartered Accountant in practice.</p> <p>Pursuant to Section 2(2)(iv), the Council has passed a resolution permitting a CA in practice to render entire range of "Management Consultancy and other Services".</p> <p>Accordingly "Management Consultancy and other Services" shall include the following:</p> <ul style="list-style-type: none"> <li>• Personnel recruitment and selection.</li> <li>• Acting as advisor or consultant to an issue, including such matters as Drafting of prospectus and listing agreement and completing formalities with Stock Exchanges, ROC and SEBI, Preparation of publicity budget, Advice regarding selection of various agencies connected with issue etc.</li> </ul> <p><b>Explanation - For removal of doubts, it is hereby clarified that the activities of broking, underwriting and portfolio management are not permitted.</b></p>	
<b>Sec. 6</b>	<p>→ No member of the Institute shall be entitled to practice unless he has obtained from the Council a COP.</p> <p>→ Once a person becomes a member of ICAI, he is bound by the provisions of CA Act and its regulations.</p> <p>→ If he appears before the Income Tax Tribunal as an Income tax representative after becoming a member he could appear so only in his capacity as a CA and a member of ICAI.</p> <p>→ A member of ICAI can have no other capacity in which he can take up such practice, separable from his capacity to practice as a member of the Institute.</p> <p>→ A member not in practice cannot accept any engagement for services prescribed for a practicing CA. Therefore if a CA has surrendered his certificate of practice due to misconduct he cannot in any other capacity take up any practice separable from his capacity to practice as a member of the institute.</p>	
<b>Sec. 7</b>	<p>→ Every <b>member of the Institute in practice shall</b> use the designation of a chartered accountant.</p> <p>→ No member using such designation shall use any other description, whether in addition thereto or in substitution.</p> <p>→ In case a member have more than one Certificate of practice, (subject to permission), for matters involving practice as Chartered Accountant, they should use designation C.A.</p>	
<b>Sec. 21</b>	<p>"Professional or Other misconduct" shall be deemed to include any act or omission provided in any of the Schedules, but nothing in this section shall be construed to limit or abridge in any way the power conferred or duty cast on the Director (Discipline) u/s 21(1) to inquire into the conduct of any member of the Institute under any other circumstances.</p>	
<b>Sec. 25</b>	<p>No company, whether incorporated in India or elsewhere, shall practise as chartered accountants.</p>	
<b>Sec. 26</b>	<p>No person other than a member of the Institute shall sign any document on behalf of a chartered accountant in practice or a firm of such chartered accountants in his or its professional capacity.</p>	
<b>Sec. 27</b>	<b>Office</b>	A Place where a name board is fixed or where such place is mentioned in the letterhead or any other documents as a place of business.
	<b>Use of Name Board at residence</b>	Name board can be put in place of residence of member provided it is a name board of individual member and not of firm.
	<b>Requirement of Separate In-charge</b>	<p>→ If a CA in practice or a firm of CA has more than one office in India, each one of such offices should be in the separate charge of a member of the institute, who may be either partner / employee.</p> <p>→ The requirement of Section 27 in regard as to a member being in-charge of an office of a CA or a firm of such CAs shall be satisfied only if the member is actively associated with such office.</p> <p>→ Such association shall be deemed to exist if the member resides in the place where the office is situated for a period of not less than 182 days in a year or if he attends the said office for a period of not less than 182 days in a year.</p>
	<b>Exemption from Separate In-charge</b>	
	<b>Members practicing in Hilly area</b>	<p>subject to following conditions:</p> <ul style="list-style-type: none"> <li>• Temporary office in plains may be opened for a period not exceeding 3 Months in winter season.</li> <li>• Name board of firm to be displayed at temporary office only during these 3 months.</li> <li>• Temporary office should not be mentioned as place of Business on office documents,</li> <li>• Regular office need not be closed and all correspondence may continue at permanent office,</li> </ul> <p>Before commencement of every winter and at the close of such temporary office, it shall be obligatory on member to inform ICAI</p>
	<b>Second office</b>	<p>If it is situated in</p> <ul style="list-style-type: none"> <li>• same premises in which first office is situated, or</li> <li>• in the same city, or</li> <li>• within 50 kms. from the municipal limits of city in which first office is situated</li> </ul>

## First Schedule to CA Act, 1949

Part – I (Professional Misconduct - CA in Practice)		A CA in Practice is deemed to be guilty of professional Misconduct if he							
<b>Clause 1</b>		Allows any person to practice in his name as a Chartered Accountant, unless such person is also a Chartered Accountant in practice, and is in partnership with, or employed by himself.							
<b>Clause 2</b>		<p>→ Pays or allows or agrees to pay or allow, directly or indirectly,  → any share, commission or brokerage in fees or profits  → of his professional business to any person other than</p> <ul style="list-style-type: none"> <li>• a member of the Institute, or</li> <li>• partner / retired partner, or</li> <li>• legal representative of deceased partner (If partnership deed provides), or</li> <li>• member of any other professional bodies (ICSI, ICWAI, Bar Council of India, Indian Institute of Architects, Institute of Actuaries of India) or</li> <li>• with such other persons having prescribed qualifications (CS, CWA, Actuary, B.E. Bachelor in Technology, Bachelor in Architecture, Bachelor in Law; MBA).</li> </ul> <p><b>Sale of Goodwill:</b> In case of <b>sole proprietorship</b>, the Council of ICAI has resolved that the sale / transfer of goodwill shall be permitted in case of death of the proprietor provided:</p> <ul style="list-style-type: none"> <li>• ICAI's permission to practice in the deceased's firm name is sought within a year of death. (In such a case, name of the firm is kept in abeyance till one year from the date of death).</li> <li>• In case there exist a dispute as to the legal heir, information as to the existence of the dispute is received by the Institute within a year of the death. (In such a case, name of the firm is kept in abeyance till one year from the date of settlement of dispute).</li> </ul> <p><b>Note: In case of a partnership firm when all the partners die at the same time, the above council decision would also be applicable.</b></p>							
<b>Clause 3</b>		<p>Accepts or agrees to accept any part of the profits of the professional work of a person who is not a member of Institute. However, such restriction does not apply in respect of following persons:</p> <p>→ member of any other professional bodies (as specified in Clause 2), or  → with such other persons having prescribed qualifications (as specified in Clause 2).</p>							
<b>Clause 4</b>		<p>Enters into partnership in or outside India, with any person other than the following:</p> <ol style="list-style-type: none"> <li>1. C.A. in practice, or</li> <li>2. Member of any other professional body having prescribed qualifications, or</li> <li>3. a person who but for his residence abroad would be entitled to be registered as member, or</li> <li>4. a person whose qualifications are recognized by CG or Council for the purpose of permitting such partnerships.</li> </ol> <p><b>Persons Qualified in India for purpose of Membership (Regulation 53A):</b> CS, CWA, Actuary, B.E., B. Tech, B. Arch, LLB or MBA (from recognised Universities or Institutes) .</p> <p><b>Permitted memberships for Partnership (Regulation 53B):</b> Members of ICSI, ICWAI, Bar Council of India, Institution of Engineers, Indian Institute of Architects, Institute of Actuaries of India and professional Bodies outside India whose qualifications are recognised by the Council.</p>							
<b>Clause 5</b>		Secures any professional business through the services of a person who is not an employee or not his partner or by means which are not open to a CA.							
<b>Clause 6</b>		<p>→ Solicits clients or professional work, either directly or indirectly,  → by circular, advertisement, personal communication or by any other means.  However, solicitation is relaxed in following cases:</p> <p>→ Securing professional work from another CA in practice.  → <b>Responding to tenders issued by various users of professional services exclusively reserved for CAs provided minimum fee is prescribed in the tender document or Those tenders which are open to other professionals along with the Chartered Accountants.</b></p> <p><b>Council Guidelines w.r.t. Permitted and Prohibited forms of Solicitation</b></p> <table border="1"> <tbody> <tr> <td><b>Empanelment for allotment of audit / professional work</b></td> <td> <p>→ In respect of organisations, where a panel of CA's exists, a member is free to request to place his name on the panel.</p> <p>→ Roving enquiries for existence of such panel is not permitted.</p> <p>→ It is permissible to quote fees on enquiries being received from such organisations, which maintains such panel.</p> </td> </tr> <tr> <td><b>Scope of representation u/s 140(4) of Companies Act 2013</b></td> <td> <p>→ Representation should not be used to secure needless publicity and soliciting for his continuance as an auditor.</p> <p>→ I may set out in a dignified manner how he has been acting independently through his term of office and his willingness to continue as an auditor.</p> </td> </tr> <tr> <td><b>Public Interviews</b></td> <td>→ permitted subject to condition that it should not result in publicity.</td> </tr> </tbody> </table>		<b>Empanelment for allotment of audit / professional work</b>	<p>→ In respect of organisations, where a panel of CA's exists, a member is free to request to place his name on the panel.</p> <p>→ Roving enquiries for existence of such panel is not permitted.</p> <p>→ It is permissible to quote fees on enquiries being received from such organisations, which maintains such panel.</p>	<b>Scope of representation u/s 140(4) of Companies Act 2013</b>	<p>→ Representation should not be used to secure needless publicity and soliciting for his continuance as an auditor.</p> <p>→ I may set out in a dignified manner how he has been acting independently through his term of office and his willingness to continue as an auditor.</p>	<b>Public Interviews</b>	→ permitted subject to condition that it should not result in publicity.
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Guidelines for Posting the particulars on Website			
	<ul style="list-style-type: none"> <li>• No standard format is prescribed and no restriction on use of colours.</li> <li>• Website should run on 'pull' model not on 'push' model of technology.</li> <li>• Mention of Website Address on professional stationery is permitted.</li> <li>• Members are not allowed to use logo (other than prescribed by ICAI) on website.</li> <li>• Photographs of any sort (other than passport size photo of member) is not permitted.</li> <li>• Details should be so designed that it does not amount to soliciting client or advertisement of professional attainments or services.</li> <li>• Website may provide a link to the website of ICAI, its regional councils and branches and also to the websites of Government/Government departments/Regulatory Authorities only.</li> <li>• Address of the website may be different from the name of the firm.</li> <li>• Name of clients and fees charged is not permitted to be given on website, <b>except when required by any regulator.</b></li> </ul>		
<b>Clause 7</b>	<p>→ Advertises his professional attainments or services, or</p> <p>→ uses any designation or expressions other than CA</p> <p>→ on professional documents, visiting cards, letter heads or sign boards.</p> <p>However, recognized degree of university or membership recognized institution may be used.</p> <p>(a) Words like income-tax consultant, cost consultant or management consultant - not allowed.</p> <p>(b) Persons eligible otherwise, subject to permission may practice as advocates but can't use designation "Chartered Accountant" and "Advocate" simultaneously.</p> <p>(c) A member may appear on T.V. and films and etc. and describe themselves as CA, but no reference, as to name/address/services of firm should be made.</p> <p>(d) Name of CA acting as director in the company is permissible to appear in the prospectus of the company, however descriptions regarding his expertise and knowledge is not permitted.</p>		
<b>Clause 8</b>	<p>→ accept a position as Auditor, previously held by another chartered accountant,</p> <p>→ without first communicating with him, in writing.</p> <p>(a) <b>Professional reasons for not accepting Audit:</b></p> <p>(i) Non-compliance of provisions of Sec. 139 &amp; 140 of Companies Act 2013.</p> <p>(ii) Non-payment of undisputed audit fee (except sick unit).</p> <p>(iii) Issuance of a qualified Report.</p> <p>In first two, acceptance of audit amounts to professional misconduct. In (iii), member may accept audit if he thinks that attitude of retiring auditor wasn't proper and justified.</p> <p>(b) <b>Mode of communication:</b> Registered post acknowledgement due or by hand against an acknowledgement in writing. Mere posting of a letter under certificate of posting is not sufficient to establish communication.</p> <p>(c) The requirement for communicating would apply to all types of audit i.e. statutory audit, tax audit, internal audit, concurrent audit or any other kind of audit.</p>		
<b>Clause 9</b>	<p>→ accepts an appointment as auditor of a company, without ascertaining</p> <p>→ whether requirements of Sec. 224 &amp; 225 of Companies Act, 1956 (Sec. 139 &amp; 140 of Companies Act 2013), in respect of such appointment have been duly complied with.</p>		
<b>Clause 10</b>	<p>→ Charges or offers to charge, accepts or offers to accept,</p> <p>→ in respect of any professional employment,</p> <p>→ fee which is based on a %age of profits or which are contingent upon findings, or results of such employment, except as permitted under regulations.</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 20%;"><b>Regulation 192 (Restriction on Fees)</b></td> <td> <p>In respect of below mentioned cases fees may be fixed as specified below:</p> <ul style="list-style-type: none"> <li>• <b>In the case of receiver or liquidator:</b> on the basis of %age of realisation or disbursement of assets.</li> <li>• <b>In the case of co-operative society:</b> on the basis of %age of paid up capital or working capital or gross/net income or profits.</li> <li>• <b>In the case of valuer for purposes of direct taxes and duties:</b> on the basis of %age of value of property valued.</li> <li>• <b>In the case of management consultancy services:</b> on percentage basis which may be contingent upon the findings, or results of such work.</li> <li>• <b>In case of fund raising services:</b> on a percentage of the fund raised;</li> <li>• <b>In case of debt recovery services:</b> on basis of percentage of the debt recovered.</li> <li>• <b>In case of services related to cost optimization:</b> on a percentage of the benefit derived.</li> </ul> </td> </tr> </table>	<b>Regulation 192 (Restriction on Fees)</b>	<p>In respect of below mentioned cases fees may be fixed as specified below:</p> <ul style="list-style-type: none"> <li>• <b>In the case of receiver or liquidator:</b> on the basis of %age of realisation or disbursement of assets.</li> <li>• <b>In the case of co-operative society:</b> on the basis of %age of paid up capital or working capital or gross/net income or profits.</li> <li>• <b>In the case of valuer for purposes of direct taxes and duties:</b> on the basis of %age of value of property valued.</li> <li>• <b>In the case of management consultancy services:</b> on percentage basis which may be contingent upon the findings, or results of such work.</li> <li>• <b>In case of fund raising services:</b> on a percentage of the fund raised;</li> <li>• <b>In case of debt recovery services:</b> on basis of percentage of the debt recovered.</li> <li>• <b>In case of services related to cost optimization:</b> on a percentage of the benefit derived.</li> </ul>
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<b>Clause 11</b>	<p>→ Engages in any Business or occupation, other than profession of C.A</p> <p>→ unless permitted by council so to engage.</p> <p>Note: However, a member may become director (not being M.D. or Whole time director) in a company provided he or any of his partner is not interested in such company as an auditor.</p>		
<b>Clause 12</b>	<p>→ Allows a person not being a member of Institute in practice or a member not being his partner, to sign on his behalf or on behalf of his firm,</p> <p>→ any Balance Sheet, P&amp;L A/c, Report or Financial Statements</p>		

<b>Part – II</b> <b>(Professional Misconduct - CA in Service)</b>	A CA in Service shall be deemed to be guilty of professional misconduct if he:	
	<b>Clause 1</b>	Pays or allows or agrees to pay directly or indirectly to any person any share in the emoluments of the employment undertaken by him.
	<b>Clause 2</b>	Accepts or agrees to accept any part of fees, profits or gains from a lawyer, a chartered accountant or broker engaged by such company, firm or person or agent or customer of such company, firm or person by way of commission or gratification.
<b>Part – III</b> <b>(Professional Misconduct - CA Generally)</b>	A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he	
	<b>Clause 1</b>	Not being a fellow of the Institute, but acts as a fellow of the Institute.
	<b>Clause 2</b>	Does not supply the information called for, or does not comply with the requirements asked for by the Institute, Council or any of its committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the appellate authority.
<b>Part – IV</b> <b>(Other Misconduct – CA Generally)</b>	A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he	
	<b>Clause 1</b>	is held guilty of any civil or criminal court for an offence which is punishable with imprisonment for a term not exceeding six months.
	<b>Clause 2</b>	In the opinion of the Council brings disrepute to the profession or the Institute as a result of his action whether or not related to his professional work.
Illustrative Cases of Other Misconduct:		
<ol style="list-style-type: none"> <li>1. Retaining of books of account and documents of the client without a reasonable cause.</li> <li>2. Misappropriation by office-bearer of a Regional Council, of funds for his personal use.</li> <li>3. Keeping assessment records of income tax department belonging to the client at home.</li> <li>4. Adopting coercive methods on a bank for having a loan sanctioned to him.</li> </ol>		

### Second Schedule to CA Act, 1949

<b>Part – I</b> <b>(Professional Misconduct - CA in Practice)</b>	A CA in Practice is deemed to be guilty of professional Misconduct if he	
	<b>Clause 1</b>	<ul style="list-style-type: none"> <li>→ discloses the information, acquired in the course of his professional engagement</li> <li>→ to any person other than his client so engaging him</li> <li>→ without the consent of his client or otherwise than as required by any law.</li> </ul>
	<b>Clause 2</b>	<ul style="list-style-type: none"> <li>→ Certifies or submits in his name or in the name of his firm</li> <li>→ a report of an examination of financial statements</li> <li>→ unless the examination of such statements and the related records has been made by him or by a partner or an employee in his firm or by another CA in practice.</li> </ul>
	<b>Clause 3</b>	<ul style="list-style-type: none"> <li>→ Permits his name or the name of his firm,</li> <li>→ to be used in connection with an estimate of earnings</li> <li>→ contingent upon future transactions</li> </ul> <p>in manner which may lead to the belief that he vouches for the accuracy of the forecast.</p> <p><b>Participation in preparation of forecasts &amp; their review:</b> SAE 3400 "The Examination of Prospective Financial Information" allows to a member to participate in the preparation of profit or financial forecasts and can review them subject to following conditions:</p> <ol style="list-style-type: none"> <li>(a) He indicates the source of information.</li> <li>(b) He indicates the basis of forecasts.</li> <li>(c) He gives in his report the major assumptions made in arriving at the forecasts.</li> <li>(d) He does not vouch for the accuracy of the forecasts.</li> </ol>
	<b>Clause 4</b>	<ul style="list-style-type: none"> <li>→ expresses his opinion, on financial statements of any business or enterprise</li> <li>→ in which he, his firm or a partner in his firm has a substantial interest</li> </ul> <ol style="list-style-type: none"> <li>(1) Sec. 141 of Companies Act 2013 also prohibits a member from auditing the accounts of a company in various situations.</li> <li>(2) A member of the Institute can not express the opinion in the following cases: <ul style="list-style-type: none"> <li>(a) Where the member himself is owner/partner of concerned business.</li> <li>(b) Where the partner/relative (within the meaning of AS 18) of CA has substantial interest in concerned business.</li> <li>(c) Where the member himself or his partner or relative is a director.</li> </ul> </li> <li>(3) Members are not permitted to write books of accounts of their auditee clients.</li> </ol>
<b>Clause 5</b>	<ul style="list-style-type: none"> <li>→ fails to disclose a material fact, known to him, which is not disclosed in a financial statement,</li> <li>→ but disclosure of which is necessary, in making such financial statement not misleading</li> <li>→ where he is concerned with that financial statement in a professional capacity.</li> </ul>	

	<b>Clause 6</b>	→ fails to report a material misstatement. known to him, to appear in a financial statement → with which he is concerned in a professional capacity.
	<b>Clause 7</b>	→ Does not exercise due diligence, or is grossly negligent → in the conduct of his professional duties.
	<b>Clause 8</b>	→ Fails to obtain sufficient information, which is necessary for expression of an opinion or → its exceptions are sufficiently material to negate the expression of an opinion.
	<b>Clause 9</b>	→ Fails to invite attention to any material departure → from the generally accepted procedure of audit applicable to the circumstances.
	<b>Clause 10</b>	→ Fails to keep moneys of his client, → other than fees or remuneration or money meant to be expended, → in a separate banking account or → to use such moneys for purposes for which they are intended within a reasonable time.
<b>Part – II (Professional Misconduct - CA Generally)</b>	A member of the Institute will be held guilty of professional misconduct if he	
	<b>Clause 1</b>	→ Contravenes any of the <b>provisions</b> of this act or → the <b>regulations</b> made there under or <b>any guidelines issued by the council.</b>
	<b>Clause 2</b>	→ Being an employee of any company, firm or person, → discloses confidential information acquired in the course of his employment → except as and when required by any law or except as permitted by the employer.
	<b>Clause 3</b>	→ Includes in any information, statement, return or form to be submitted to → the Institute, Council or any of its committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority, → any particulars knowing them to be false.
	<b>Clause 4</b>	Defalcates or embezzles money received in his professional capacity.
<b>Part – III (Other Misconduct – CA Generally)</b>	<b>Clause 1</b>	→ A member of the Institute, whether in practice or not, → shall be deemed to be guilty of other misconduct, → if he is guilty by any civil or criminal court for an offence which is punishable for a term exceeding 6 months.

**COUNCIL GENERAL GUIDELINES, 2008**

Heading	Provision
<b>Opinion on financial statements when there is substantial interest</b>	<ul style="list-style-type: none"> <li>A member of the Institute shall not express his opinion on financial statements of any business or enterprise in which one or more persons who are his "relatives" within the meaning of AS 18 has/have, either by themselves or in conjunction with such member, a substantial interest in the said business or enterprise.</li> <li>Explanation: For this purpose and for the purpose of compliance of Clause (4) of Part I of the Second Schedule to the Chartered Accountants Act, 1949, the expression "substantial interest" shall have the same meaning as is assigned thereto under Appendix (9) to the CA Regulations, 1988.</li> </ul> <p style="text-align: center;"><b>Points to remember</b></p> <p><b>Relative as per AS 18, in relation to an individual, means the spouse, son, daughter, brother, sister, father and mother who may be expected to influence, or be influenced by, that individual in his/her dealings with the reporting enterprise.</b></p>
<b>Maintenance of books of accounts</b>	A member of the Institute in practice or the firm of CAs of which he is a partner, shall maintain and keep in respect of his / its professional practice, proper books of account including the following:- (i) a Cash Book; (ii) a Ledger.
<b>Tax Audit assignments u/s Section 44 AB of the Income-tax Act, 1961</b>	<ul style="list-style-type: none"> <li>A member of the Institute in practice shall not accept, in a financial year, more than the "specified number of tax audit assignments" u/s 44AB of the Income-tax Act, 1961.</li> <li>"The specified number of tax audit assignments" means - (a) in the case of a CA in practice or a proprietary firm of CA, 60 tax audit assignments.. (b) in the case of firm of CAs in practice, 60 tax audit assignments per partner in the firm.</li> <li><b>It is clarified by the ICAI that any partner in the firm can sign tax audit report on behalf of firm.</b></li> </ul>
<b>Appointment of an Auditor in case of non-payment of undisputed fees</b>	<ul style="list-style-type: none"> <li>A member of the Institute in practice shall not accept the appointment as auditor of an entity in case the undisputed audit fee of another Chartered Accountant for carrying out the statutory audit under the Companies Act, 1956 or various other statutes has not been paid:</li> <li><b>In the case of sick unit (Negative net worth), the above prohibition of acceptance shall not apply.</b></li> </ul>

<b>Specified number of audit assignments</b>	<ul style="list-style-type: none"> <li>A member of the Institute in practice shall not hold at any time appointment of more than the "specified number of audit assignments" of Companies u/s 139 of the Companies Act, 2013.</li> <li>A CA in practice as well as firm of Chartered Accountants in practice shall maintain a record of the audit assignments accepted by him or by the firm of Chartered Accountants, or by any of the partners of the firm in his individual name or as a partner of any other firm, as far as possible, in the following format:</li> </ul> <table border="1" style="margin-left: 20px;"> <thead> <tr> <th>S.No</th> <th>Name of the Co</th> <th>Registration No.</th> <th>Date of Appointment</th> <th>Date of Acceptance</th> <th>Date on which Form ADT-1 Filed with ROC</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>2</td> <td>3</td> <td>4</td> <td>5</td> <td>6</td> </tr> <tr> <td> </td> <td> </td> <td> </td> <td> </td> <td> </td> <td> </td> </tr> </tbody> </table>	S.No	Name of the Co	Registration No.	Date of Appointment	Date of Acceptance	Date on which Form ADT-1 Filed with ROC	1	2	3	4	5	6						
S.No	Name of the Co	Registration No.	Date of Appointment	Date of Acceptance	Date on which Form ADT-1 Filed with ROC														
1	2	3	4	5	6														
<b>Appointment as Statutory auditor</b>	<p>→ A member of the Institute in practice shall not accept the appointment as statutory auditor of PSU/ Govt. Co/Listed Co &amp; other Public Co having turnover of Rs. 50 Cr. or more in a year where he accepts any other work or assignment or service in regard to the same Undertaking/Co on a remuneration which in total exceeds the fee payable for carrying out the statutory audit of the same Undertaking/company.</p> <p>→ For the above purpose, the term "other work" or "service" or "assignment" shall include Management Consultancy &amp; other professional services permitted by Council pursuant to Sec. 2(2)(iv) of the CA Act.</p>																		
<b>Appointment of an auditor when he is indebted to a concern</b>	→ A member of the Institute in practice or a partner of a firm in practice or a firm shall not accept appointment as auditor of a concern while indebted to the concern or given any guarantee or provided any security in connection with the indebtedness of any third person to the concern, for limits fixed in the statute and in other cases for amount exceeding Rs. 10,000/-																		

**KYC (KNOW YOUR CLIENT) NORMS FOR A CA**

Norms to be observed by Member Practice	Individual Client		Corporate Entity		Non Corporate Entity	
	General Information	<ul style="list-style-type: none"> <li>Name of Individual</li> <li>PAN No. or Aadhar No.</li> <li>Business Description</li> <li>Copy of Last Audited F.S.</li> </ul>		<ul style="list-style-type: none"> <li>Name and Address</li> <li>Business description</li> <li>Name of Parent Company</li> <li>Copy of Last Audited F.S.</li> </ul>		<ul style="list-style-type: none"> <li>Name and address</li> <li>PAN No.</li> <li>Business Description</li> <li>Partner's Name &amp; address</li> <li>Copy of Last Audited F.S.</li> </ul>
Engagement Information	Type of Engagement		Type of Engagement		Type of Engagement	
Regulatory Information			<ul style="list-style-type: none"> <li>Company PAN No.</li> <li>Company Identification No.</li> <li>Director's Name and address</li> <li>Director's identification No.</li> </ul>			
<b>Importance of KYC Norms</b>	<ul style="list-style-type: none"> <li>The financial services industry globally is required to obtain information of their clients and comply with KYC norms.</li> <li>Keeping in mind the highest standards of Chartered Accountancy profession in India, the Council of ICAI recommended such norms to be observed by the members of the profession who are in practice.</li> <li>Considering the spirit underlying these measures, it is expected that every CA carrying out attest function is encouraged to follow them and implementation of these measures would go a long way in ensuring equitable flow of work among the members and would enhance prestige of the profession in the society.</li> <li>These Know Your Client (KYC) Norms are also important in order to ensure a healthy growth of the profession and an equitable flow of professional work among the members.</li> </ul>					

**FUNDAMENTAL PRINCIPLES as per CODE OF ETHICS**

<b>Fundamental Principles</b>	<b>Integrity</b>	A professional accountant should be straightforward and honest in all professional and business relationships.
	<b>Objectivity</b>	A professional accountant should not allow bias, conflict of interest or undue influence of others to override professional judgments.
	<b>Professional Competence</b>	A professional accountant should act diligently and in accordance with applicable technical and professional standards.
	<b>Confidentiality</b>	A professional accountant should respect the confidentiality of information acquired as a result of professional and employment relationships.
	<b>Professional Behavior</b>	A professional accountant should comply with relevant laws and regulations and should avoid any action that discredits the profession.
<b>Threats involves in compliance</b>	<b>Self-interest threats</b>	It may occur as a result of the financial or other interests of a professional accountant or of a relative
	<b>Self Review Threats</b>	It may occur when a previous judgment needs to be re- evaluated by the professional accountant responsible for that judgment.
	<b>Advocacy Threats</b>	It may occur when a professional accountant promotes a position or opinion to the point that subsequent objectivity may be compromised.
	<b>Familiarity Threats</b>	It may occur when, because of a relationship, a professional accountant becomes too sympathetic to the interests of others.
	<b>Intimidation Threats</b>	It may occur when a professional accountant may be deterred from acting objectively by threats, actual or perceived.

(\* For details - Refer Main Book)

## Chapter – 8 “COMPANY AUDITOR”

### SECTION – WISE INDEX of Chapter X of Companies Act, 2013 along with Corresponding rules

Chapter X of Companies Act, 2013 – AUDIT and AUDITORS (Sec. 139 – 148)		Companies (Audit and Auditors) Rules, 2014	
<b>Sec. 139(1)</b>	Appointment of Subsequent Auditor of Non Government Company at AGM	<b>Rule 3</b>	Manner and Procedure of Selection and Appointment of Auditors
		<b>Rule 4</b>	Conditions for appointment and Notice to Registrar
<b>Sec. 139(2)</b>	Rotation of Auditors	<b>Rule 5</b>	Class of Companies
<b>Sec. 139(3)</b>	Rotation of Auditing Partner and his team		
<b>Sec. 139(4)</b>	Power of C.G. to prescribe the manner of rotation.	<b>Rule 6</b>	Manner of Rotation of Auditors by the companies on expiry of their term.
<b>Sec. 139(5)</b>	Appointment of Subsequent Auditor of Government Company		
<b>Sec. 139(6)</b>	Appointment of First Auditor of Non Government Company		
<b>Sec. 139(7)</b>	Appointment of First Auditor of Government Company		
<b>Sec. 139(8)</b>	Filling of Casual Vacancies		
<b>Sec. 139(9)</b>	Re-appointment of Retiring Auditor		
<b>Sec. 139 (10)</b>	No Auditor is appointed or reappointed at AGM		
<b>Sec. 139 (11)</b>	Considerations of recommendations of Audit Committee		
<b>Sec. 140(1)</b>	Removal of Auditor before expiry of his term	<b>Rule 7</b>	Removal of Auditor before expiry of his term
<b>Sec. 140(2)</b>	Filing of statement in case of Resignation	<b>Rule 8</b>	Resignation of Auditor
<b>Sec. 140(3)</b>	Penalty for non-compliance of Sec. 140(2)		
<b>Sec. 140(4)</b>	Removal of Auditor on expiry of tenure / Giving of Special Notice		
<b>Sec. 140(5)</b>	Directions for Change of Auditors	<b>Rule 9</b>	Liability to devolve on concerned partners only.
<b>Sec. 141(1)</b>	Eligibility for appointment as Auditor		
<b>Sec. 141(2)</b>	Authorised Partner to act and sign in case of audit firm and LLP		
<b>Sec. 141(3)</b>	Disqualifications to be appointed as auditor	<b>Rule 10</b>	Disqualifications of Auditor
<b>Sec. 141(4)</b>	Vacation of Office in case of Subsequent disqualifications		

<b>Sec. 142</b>	Remuneration of Auditors		
<b>Sec. 143(1)</b>	Right of Access/Right to obtain Information/Inquiry into propriety matters		
<b>Sec. 143(2)</b>	Reporting on Books and Accounts and Financial Statements		
<b>Sec. 143(3)</b>	Reporting on other Matters	<b>Rule 11</b>	Other Matters to be included in Auditor's Report
<b>Sec. 143(4)</b>	Reasons for Adverse Remarks or Qualifications		
<b>Sec. 143(5)</b>	Directions by CAG to auditor of Government Company		
<b>Sec. 143(6)</b>	Order by CAG of Supplementary Audit of F.S. of Govt. Company.		
<b>Sec. 143(7)</b>	Order by CAG of Test audit of Accounts of Government Company		
<b>Sec. 143(8)</b>	Audit of accounts of Branch Office	<b>Rule 12</b>	Duties and Powers of the company auditor's with reference to audit of the branch and the branch auditor
<b>Sec. 143(9)</b>	Compliance with Standards of Auditing		
<b>Sec. 143(10)</b>	Powers of C.G., to prescribe the Standards of Auditing		
<b>Sec. 143(11)</b>	Powers of C.G. to issue order for specified companies to report on certain matters. (CARO, 2015)		
<b>Sec. 143(12)</b>	Reporting on Fraud	<b>Rule 13</b>	Reporting of Frauds by auditor
<b>Sec. 143(13)</b>	No Breach of duty if reporting u/s 143(12) is done in good faith.		
<b>Sec. 143(14)</b>	Application of Sec. 143 over Cost Accountant and Company Secretary.		
<b>Sec. 143(15)</b>	Penalty for non-compliance of Sec. 143(12)		
<b>Sec. 144</b>	Auditor not to render certain services		
<b>Sec. 145</b>	Auditor to sign audit reports, etc.		
<b>Sec. 146</b>	Auditor to attend General Meetings		
<b>Sec. 147</b>	Punishment for contravention		
<b>Sec. 148</b>	Central Government to specify audit of certain items of cost in respect of certain companies	<b>Rule 14</b>	Remuneration of Cost Auditor.

# APPOINTMENT OF AUDITOR

## Appointment of Subsequent Auditor

## Appointment of First Auditor

<b>Non Government Company – Sec. 139(1)</b>			
<ul style="list-style-type: none"> <li>→ Appointment will be at First AGM</li> <li>→ Till conclusion of 6<sup>th</sup> AGM; and</li> <li>→ Thereafter till conclusion of every 6<sup>th</sup> AGM</li> <li>→ In prescribed manner (Rule 3)</li> </ul>			
<b>1<sup>st</sup> Proviso</b>	<ul style="list-style-type: none"> <li>→ Company shall place the matter</li> <li>→ For ratification at every AGM.</li> </ul>		
	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 10%;"><b>Rule 3</b></td> <td> <ul style="list-style-type: none"> <li>→ Ratification will be through Ordinary Resolution.</li> <li>→ If not ratified, Board of Directors will appoint auditor.</li> </ul> </td> </tr> </table>	<b>Rule 3</b>	<ul style="list-style-type: none"> <li>→ Ratification will be through Ordinary Resolution.</li> <li>→ If not ratified, Board of Directors will appoint auditor.</li> </ul>
<b>Rule 3</b>	<ul style="list-style-type: none"> <li>→ Ratification will be through Ordinary Resolution.</li> <li>→ If not ratified, Board of Directors will appoint auditor.</li> </ul>		
<b>2<sup>nd</sup> Proviso</b>	Before appointment company shall obtain (a) Written consent from auditor (b) Certificate from auditor (Rule 4)		
<b>3<sup>rd</sup> Proviso</b>	<ul style="list-style-type: none"> <li>→ Certificate shall indicate</li> <li>→ Whether auditor has satisfied the criteria as provided u/s 141.</li> </ul>		
<b>4<sup>th</sup> Proviso</b>	<ul style="list-style-type: none"> <li>→ Company shall inform the auditor and ROC about the appointment of auditor within 15 days of appointment.</li> <li>→ Rule 4 – Intimation to ROC will be in Form ADT-1</li> </ul>		

**Government, Govt. owned / controlled Companies – Sec. 139(5)**

Appointment of Auditor

↓

In respect of a Financial year

↓

will be made by

↓

CAG

↓

Within a period of 180 Days

↓

From the commencement of financial year

↓

Who shall hold the office till the conclusion of next AGM

**Compiled by:**  
**CA. Pankaj Garg**

**Non Government Company – Sec. 139(6)**

First auditor shall be appointed by

↓

Board of Directors

↓

Within 30 days

↓

Of registration of company

↓

If Board Fails, Board shall inform the members

↓

Members shall within 90 Days

↓

At an EGM

↓

appoint the first auditor

↓

Who hold office till conclusion of first AGM

**Government, Govt. owned / controlled Companies – Sec. 139(7)**

First Auditor shall be appointed

↓

by CAG

↓

Within 60 days

↓

Of registration of company

↓

If CAG does not appoint the auditor

↓

BOD will appoint within next 30 days

↓

If Board fails Board shall inform the members

↓

Members shall within 60 days

↓

At an EGM

↓

appoint the first auditor

↓

who hold office till conclusion of first AGM

## ROTATION OF AUDITOR

**Sec. 139(2)**

**Sec. 139(3)**

**Sec. 139(4)**

Listed companies and Other prescribed companies Shall not appoint ↓ An individual as an auditor for more than one term of five consecutive years. ↓ An audit Firm as an auditor for more than two terms of five consecutive years.	<b>Rule 5</b>	Unlisted Public Companies having paid up capital ≥ 10Cr. Private Companies having paid up capital ≥ 20 Cr. Companies not covered above if public borrowings from banks and FI/ public deposits ≥ 50Cr.
<b>1<sup>st</sup> Proviso</b>	<b>Individual Auditor</b>	Not eligible for reappointment for 5 years after completing of as auditor in same company → tenure
	<b>Audit Firm</b>	Not eligible for reappointment for 5 years after completing of as auditor in same company → tenure
<b>2<sup>nd</sup> Proviso</b>	<b>Audit Firm</b>	→ Having a common partner with audit firm → Whose tenure has just expired → As on date of appointment → Shall not be appointed as auditor of same company → for a period of five years
<b>3<sup>rd</sup> Proviso</b>	<b>Every Company</b>	→ Existing before commencement of this Act → Shall comply with requirement of Sec. 139(2) → Within a period which shall not be later than the date of First AGM after 3 years from the date of commencement of this Act.
<b>4<sup>th</sup> Proviso</b>	<b>Sec. 139(2) shall not prejudice the</b>	→ Right of company to remove auditor → Right of auditor to resign.

Members may resolve the following:

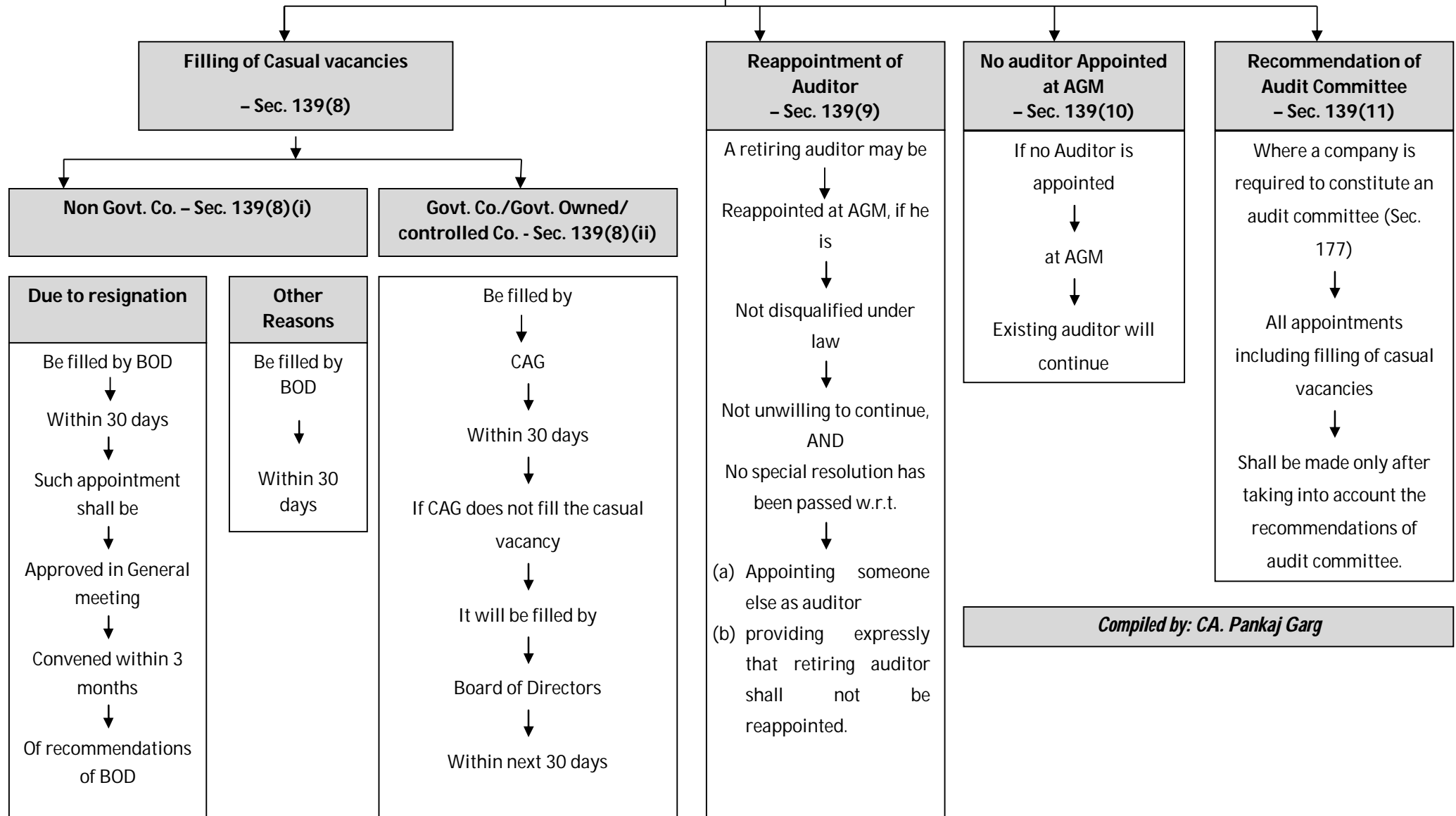
- (a) Rotation of auditing partner & his team at such interval as may be prescribed.
- (b) That audit shall be conducted by more than one auditor

Central Government  
 ↓  
 May by Rules  
 ↓  
 Prescribe the manner of rotation for Sec. 139(2)  
 ↓  
**(Rule 6 prescribes the manner of rotation)**

**Compiled by: CA. Pankaj Garg**



## OTHER PROVISIONS OF SEC. 139



**Compiled by: CA. Pankaj Garg**

## Sec. 140 – Removal, Resignation of Auditor and giving of Special Notice

**Sec. 140(1) – Removal before expiry**

Requires  
↓  
Special resolution of Company  
&  
Previous approval of CG in prescribed manner  
(Rule 7).  
↓  
Before taking any action, auditor concerned  
should be provided an opportunity of being  
heard.

---

**Rule 7**

Application to CG  
↓  
should be made within 30 days  
↓  
of passing of Board Resolution  
↓  
in Form ADT-2.

---

Within 60 days of approval by CG,  
↓  
convene a general meeting  
↓  
to Pass Special Resolution.

Opportunity	→	Board Resolution	→	Application to CG	→	General Meeting
-------------	---	---------------------	---	----------------------	---	--------------------

**Sec. 140(2) & (3) – Filing of Statement in case of Resignation**

Auditor who has resigned  
↓  
Shall file  
↓  
Within 30 days of  
resignation  
↓  
Statement in prescribed  
form  
(Rule 8 : ADT-3)  
↓  
To Company & ROC  
(Also to CAG – in case of  
Govt. Companies)  
↓  
Indicating the reasons and  
other facts relating to

---

**Sec. 140(3): Fine for non-compliance, Ranging from Rs. 50,000 – Rs. 5,00,000**

---

*Compiled by: CA. Pankaj Garg*

**Sec. 140(4) – Special Notice**

Special notice shall be required  
↓  
to pass the **Special resolution** at  
AGM providing that  
↓  
(a) Retiring Auditor shall not be re-appointed.  
or  
(b) To appoint as auditor any person other than retiring auditor.  
↓  
Copy of notice to be sent immediately to concerned auditor.  
↓  
Auditor has a right of representation (reasonable length)  
↓  
Copy of notice and representation needs to be sent to every person to whom notice of AGM was given.  
↓  
Auditor may demand for reading the representation in meeting.

---

**Representation need not be sent or read out at meeting, if on application of company or other person, Tribunal pass such order.**

**Sec. 140(5) – Directions for change of Auditor**

Tribunal may, by order, direct the company to change its auditors  
↓  
either *suo motu* or on an application made to it by the C.G. or by any person concerned,  
↓  
if it is satisfied that the auditor has acted in a fraudulent manner or abetted or colluded in any fraud.

---

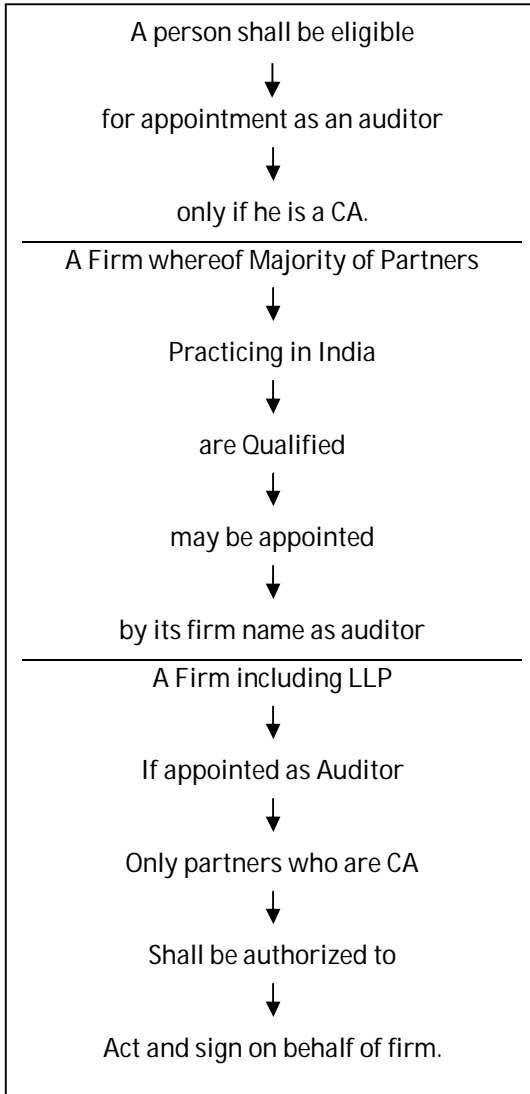
If the application is made by the C.G.  
and  
Tribunal is satisfied that any change of the auditor is required  
↓  
Tribunal shall within 15 days of receipt of such application, make an order  
↓  
that he shall not function as an auditor  
and  
C.G. may appoint another auditor in his place.

---

An auditor against whom final order has been passed by the Tribunal u/s 140(5)  
↓  
shall not be eligible to be appointed as an auditor of any company for a period of 5 years from the date of passing of the order  
and  
the auditor shall also be liable for action u/s 447.

## Sec. 141 – Eligibility, Qualifications and Disqualifications of Auditor

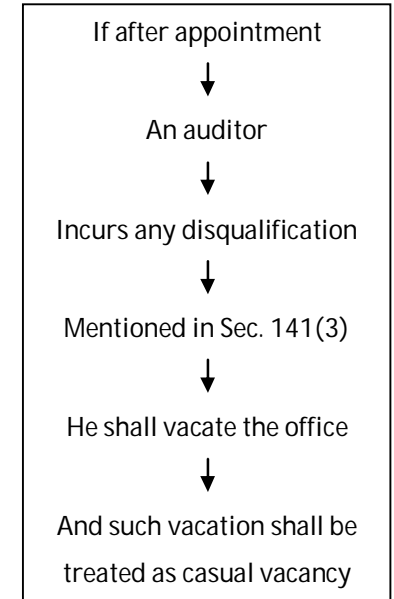
### Sec. 141 (1) & 141 (2) – Eligibility to be appointed as Auditor



### Sec. 141(3) - Persons not eligible for appointment

(a)	Body Corporate other than LLP			
(b)	Officer or Employee of the company			
(c)	Partner/Employee of Officer/Employee of the company			
(d)	(i)	person/ relative/	is holding any security * or interest in the	Company / subsidiary / holding / associate, or subsidiary of same holding.
	(ii)	partner	is indebted > 5 Lacs in the	
	(iii)		has given a guarantee in connection with indebtedness of 3 <sup>rd</sup> person > 1 Lac in the	
* no disqualification if relative holds any security in the company of face value upto 1 Lac.				
(e)	Person or firm having business relationship with Company / Subsidiary / Holding / Associate / Subsidiary of Such Holding or Associate Company			
(f)	A Person whose relative is a director or is in employment of the company as a Director or KMP.			
(g)	A person who is in full time employment elsewhere			
	Or			
A person holding appointment as auditor or more than 20 companies <b>other than OPC, dormant companies, Small Companies and private companies having paid up capital &lt; 100Cr.</b>				
(h)	A person who has been convicted of an offence involving fraud and a period of 10 years has not elapsed.			
(i)	Any person whose Subsidiary or Associate or any other form of entity is rendering services specified u/s 144 to the same company.			

### Sec. 141(4) – Vacation of office



**Compiled by:**  
**CA. Pankaj Garg**

# POWERS / RIGHTS & DUTIES OF COMPANY AUDITOR (Sec. 143)

## RIGHTS OF AUDITOR – Sec. 143(1)

**Right of Access**

- at all times
- to books of Account & Vouchers
- whether kept at Regd. Office or at any other place.

**Right to Obtain Info.**

- From the officers of the company
- As considers necessary
- For performance of his duties.

Duties of Auditor of Govt. Cos. – Sec. 143(5)	Supplementary Audit – Sec. 143(6)	Test Audit – Sec. 143(7)
CAG – direct the auditor the manners in which accounts are to be audited.	Within 60 days of days of receipt of Audit Report	CAG may If considers necessary
Auditor report shall include:	CAG have a Right	↓
• Directions issued by CAG.	↓	by an order
• Action taken thereon	To order for supplementary audit of F.S.	↓
• Its impact on Accounts and F.S.	↓	cause test audit
	Bu such persons as authorized by him	↓
		of accounts of Govt. companies

Sec. 143(8)	Audit of Branch Accounts (will be discussed separately)
Sec. 143(9)	Every Auditor shall comply with Auditing Standards
Sec. 143(10)	CG may prescribe the SA in consultation with NFRA
Sec. 143(11)	CG may direct that auditor's report shall include a statement on such matters as specified in order issued by it. (CARO, 2016)

## DUTIES of AUDITOR

### Inquire into Propriety Matters – Sec. 143(1)

1. Loans and advances are properly secured and terms are prejudicial .
2. Book entries are prejudicial.
3. Shares, debentures and other securities are sold at a price less than acquisition cost in case of non banking and non investment company.
4. Loans and advances made are shown as deposits.
5. Personal expenses charged to revenue account.
6. Cash has actually been received on shares allotted for cash, if not received, correct position shown in books and balance sheet.

### Reporting over Accounts & Financial Statements – Sec. 143(2)

That to the best of auditor information & knowledge, the accounts & financial statements give a true and fair view of the state of the company affairs as at the end of its financial year & profit & loss and cash flow for the .....

### Reporting u/s 143(3)

1. Obtained all necessary information for the audit.
2. Proper books of accounts have been maintained.
3. Branch audit report has been received and manner of dealing with it.
4. Balance Sheet and P & L Account agree with the books of accounts.
5. Financial statements comply with AS.
6. Comments on financial transactions having any adverse effect on functioning of c
7. Directors disqualified u/s 164(2).
8. Qualifications w.r.t. maintenance of accounts.
9. Adequacy and operative effectiveness of internal financial controls.
10. Other matters as prescribed. (Rule 11)

#### Rule 11

1. Disclosure of impact of pending litigations on financial position.
2. Provisions for Material Forseeable losses on long term contracts made.
3. Any delay in transferring amounts to IEPF.
4. Disclosures w.r.t. holdings and dealings in SBNs.

### Reasons for reservations – Sec. 143(4)

For every matter reported with a qualification  
↓  
Auditor shall state the reasons thereof

**Compiled by:**  
**CA. Pankaj Garg**

### Reporting u/s 143(12)

Fraud involving prescribed amount  
↓  
Committed by officers or employees  
↓  
Should be report to CG in prescribed manner (Rule 13)

Frauds below prescribed amount  
↓  
Should be reported to Audit Committee or BOD  
↓  
Details of Such Frauds need to be disclosed in Board's report.

**Rule 13**

Fraud ≥ 1Cr.  
↓  
Reported to Audit Committee / BOD within 2 days  
↓  
Seeking their reply within 45 days  
↓  
If reply receive, forward his report, reply and comments on reply to CG within 15 days  
↓  
If reply not recd., forward his report to CG along with a note that reply not recd.

Nature of Fraud with description	Approx. amount involved
Parties involves	remedial action taken

## OTHER PROVISIONS (Sec. 142, 144, 145, 146 & 147)

### Sec. 142 – Remuneration of Auditors

#### Authority to Fix remuneration

- Shall be General meeting or in such manner as may be determined therein.
- May be BOD in case of first auditor if appointed by BOD

#### Elements of remuneration

- Shall include all expenses incurred in connection with audit and any facility extended to auditor.
- Does not include remuneration paid for any other service.

### Sec. 144 – Auditor not to render certain services

#### Other Services that may be rendered

- As approved by the BOD or Audit Committee.

#### Services that cannot be rendered directly or indirectly to Co, Holding or Subsidiary

- Accounting & Book Keeping.
- Internal Audit
- Design & Implementation of Financial Information System.
- Actuarial Services.
- Investment advisory.
- Investment Banking
- Outsourced Financial
- Management Services
- Other Prescribed.

### Sec. 145 – Signing of Audit Reports

Shall be in accordance with Sec. 141(2)

### Sec. 146 – Attending of General meetings

- All Notice & other communication of general meetings shall be forwarded to Auditor.
- Unless exempted auditor shall attend either himself or through his authorized representative any general meeting,
- Auditor shall have right to be heard at such meeting on part of business which concerns him as auditor.

### Sec. 147 – Punishment for Contravention

#### Over the Company & Officer in default – 147(1)

- Violation of Sec. 139-146
- Company – Fine from Rs. 25,000 to Rs. 5 Lacs.
- Officer in default – Imprisonment upto 1 year or fine from Rs. 10,000 to Rs. 1 Lac or Both

#### Over the Auditor – 147(2)

- Violation of Sec. 139, 143, 144, 145.
- Fine from Rs. 25,000 to Rs. 5 Lacs.
- In case of Willful default – Imprisonment upto 1 year and fine from Rs. 1 Lac to Rs. 25 Lacs

If auditor convicted u/s 147(2)

he shall be liable to

Refund the remuneration and Pay for damages

Compiled by: CA. Pankaj Garg

# CARO 2016

## Applicability of CARO 2016

CARO 2016 apply to all companies including foreign companies except the following

- (a) Banking Company  
 (b) Insurance Company  
 (c) Company licensed to operate u/s 8  
 (d) One Person Company  
 (e) Small Company  
 (f) Private limited Company (not being a subsidiary or holding of public co)
- Paid up capital + Reserves & Surplus  $\leq$  1Cr. (as on Balance Sheet Date)
  - +
  - Total borrowings from Bank & F.I.  $\leq$  1Cr. (at any point of time during the FY)
  - +
  - Total revenue as disclosed in Schedule III  $\leq$  10 Cr. (for the FY)

### Important Notes

1. CARO not apply over audit report on Consolidated F.S.
2. Provisions of CARO are equally applicable in case of branches.
3. Paid up capital includes equity as well as Preference.
4. Reserves include all types of reserves & P & L Balance.
5. All Loans (secured/unsecured, long term/short term, etc.) are to be considered and in aggregate.
6. F.I. includes NBFC.
7. Total Revenue comprises of Revenue from Operations and Other Income.

**Compiled by: CA. Pankaj Garg**

## Matters to be reported under CARO 2016 (Para 3)

Para No.	Reporting Area	Reporting Requirements
3(i)	<b>Fixed Assets</b>	<ul style="list-style-type: none"> <li>• Whether proper records maintained.</li> <li>• Whether physical verification has been conducted at reasonable intervals by mngt.</li> <li>• Whether material discrepancies noticed and if so, whether dealt properly in books.</li> <li>• Title deeds of immovable properties are held in name of Co., if not provide details.</li> </ul>
3(ii)	<b>Inventories</b>	<ul style="list-style-type: none"> <li>• Whether physical verification has been conducted at reasonable intervals by mngt.</li> <li>• Whether material discrepancies noticed and if so, whether dealt properly in books.</li> </ul>
3(iii)	<b>Loans and Advances</b>	Whether loans have been granted to companies, firms, LLP covered u/s 189. If so, <ol style="list-style-type: none"> <li>(a) T &amp; C are not prejudicial to the company's interest;</li> <li>(b) Schedule of repayment of principal &amp; payment of interest has been stipulated;</li> <li>(c) State the total amount overdue for &gt; 90 days.</li> </ol>
3(iv)	<b>Compliance of Provisions of Sec. 185 &amp; 186</b>	<ul style="list-style-type: none"> <li>• In respect of loans, investments, guarantees, and security</li> <li>• If not, provide the details thereof.</li> </ul>
3(v)	<b>Public Deposits</b>	<ul style="list-style-type: none"> <li>• Directives by RBI and Sec. 73 to 76 complied with. If not - nature of contravention.</li> <li>• Order passed by CLB/RBI/Court/Tribunal-Whether complied with or not.</li> </ul>
3(vi)	<b>Cost Records</b>	<ul style="list-style-type: none"> <li>• Whether Specified u/s 148(1); whether accounts and records made and maintained.</li> </ul>
3(vii)	<b>Statutory Dues</b>	<ul style="list-style-type: none"> <li>• Whether undisputed PF, ESI, IT, ST, ST, Custom, Excise, VAT, cess &amp; Other – paid regularly. If Not outstanding &gt;6 months as on Balance Sheet Date.</li> <li>• W.r.t. disputed IT, ST, ST, Custom, Excise, VAT – State Amount involved &amp; forum</li> </ul>
3(viii)	<b>Repayment of Dues</b>	<ul style="list-style-type: none"> <li>• Whether co. default in repayment of dues – F.I., Bank, Govt., Debenture holders.</li> <li>• If Yes – Nature and Amount of Default.</li> </ul>
3(ix)	<b>Money raised by public issue &amp; term loans</b>	<ul style="list-style-type: none"> <li>• Whether money Raised by IPO/FPO/term Loans – applied for stated purpose.</li> <li>• If Not – details along with delay and subsequent ratification be reported.</li> </ul>
3(x)	<b>Fraud</b>	<ul style="list-style-type: none"> <li>• Whether any fraud by company or on company by its officers/employees-noticed or reported.</li> <li>• If Yes – Nature and amount to be stated.</li> </ul>
3(xi)	<b>Managerial remuneration</b>	<ul style="list-style-type: none"> <li>• Whether managerial remuneration has been paid with requisite approvals u/s 197.</li> <li>• If Not, amount involved and steps taken for securing refund to be reported.</li> </ul>
3(xii)	<b>Nidhi Companies</b>	<ul style="list-style-type: none"> <li>• Whether the net owned funds to deposits ratio 1:20.</li> <li>• Whether 10% unencumbered term deposits maintained..</li> </ul>
3(xiii)	<b>Transaction with Related Parties</b>	<ul style="list-style-type: none"> <li>• Whether transactions with related parties are in compliance with Sec. 177 &amp; 188.</li> <li>• Whether details disclosed in F.S. as required by applicable AS.</li> </ul>
3(xiv)	<b>Preferential Allotment</b>	<ul style="list-style-type: none"> <li>• Whether any preferential allotment of shares/FCD/PCD has been made.</li> <li>• If so, whether Sec. 42 complied with and amount raised used for stated purpose.</li> <li>• If Not – provide details of amount involved and nature of non compliance.</li> </ul>
3(xv)	<b>Non cash transactions with Directors</b>	<ul style="list-style-type: none"> <li>• Whether co. has entered into non cash transactions with directors.</li> <li>• If so. Whether Sec. 192 has been complied with.</li> </ul>
3(xvi)	<b>Registration with RBI</b>	Whether regn. required u/s 451A of RBI Act, 1934. If So- whether regn. obtained.

# Chapter 12 – Audit of Dividend

## SEC. 123 – DECLARATION OF DIVIDEND

<b>Sec. 123(1)</b>	<p><b>Sources of Dividend:</b></p> <ul style="list-style-type: none"> <li>• CY Profits after providing dep.</li> <li>• Profits of previous FYs after providing dep.</li> <li>• Money provided by CG/SG.</li> </ul> <p><b>Transfer to Reserves:</b> Company may transfer appropriate %age of profits to reserves. (Optional)</p> <p><b>Set off of Previous Losses:</b> Dividend cannot be declared unless carried over losses &amp; dep. not provided in earlier years are set-off against profit of CY.</p>
123(2)	Dep. shall be provided in accordance with Sec. 123(2).
<b>123(3) – Interim Dividend</b>	<ul style="list-style-type: none"> <li>• BOD may declare Interim dividend during any FY out of Surplus in P &amp; L A/c or CY profits.</li> <li>• It cannot be higher than avg dividend of preceding 3FYs, if company has incurred losses in current FY upto the end of quarter immediately preceding the declaration of interim dividend.</li> </ul>
123(4)	Dividend including interim dividend shall be deposited within 5 days of declaration in a separate Bank Account.
123(5)	Dividend shall be paid in cash only and to the registered shareholder or his order or his banker.
123(6)	Company which fails to comply with Sec. 73 & 74 shall not so long as failure continues declare any dividend on its equity shares.

### Declaration of dividend out of

<b>Proviso to Sec. 123(1):</b>
<ul style="list-style-type: none"> <li>• Dividend out of reserves shall be made in accordance with Rules.</li> <li>• Dividend can be declared only out of free reserves.</li> </ul>
<b>Rules 3 of Companies Declaration and Payment of Dividend Rules, 2014</b>

Dividend out of reserves is subject to following conditions:

1. Rate of Dividend  $\leq$  Average rate of preceding 3 years.
2. Amount withdrawn from reserves  $\leq$  10% of PUC & free reserves.
3. Balance of Reserves after withdrawal  $\geq$  15% of PUC.
4. Amount withdrawn from reserves shall be first utilised to set off the losses of Current FY.

## SEC. 124 – UNPAID DIVIDEND ACCOUNT

124(1)	Dividend declared but not paid or claimed within 30 days from date of declaration, shall be transferred to unpaid dividend account within 7 days from the expiry of 30 days.
124(2)	With 90 days from transfer of unpaid dividend to unpaid dividend account, company shall prepare a statement containing name, address and unpaid dividend and place it on website of the company and on other website as approved by CG in prescribed manner.
124(2)	Any default in transferring the amount to unpaid dividend account will attract interest @12% p.a. to be paid to members in proportion to amount remaining unpaid.
124(4)	Any person entitled for money transferred to unpaid dividend account may apply to company for payment of money claimed.
124(5)	Money transferred to unpaid dividend account remaining unclaimed for 7 years shall be transferred to IEPF.
124(6)	<ul style="list-style-type: none"> <li>• All shares in respect of which dividend has not been paid for 7 consecutive years or more shall be transferred to IEPF.</li> <li>• Claimant of shares shall be entitled to claim the transfer of shares from IEPF.</li> </ul>
124(6)	For non-compliance, company is punishable with fine ranging from Rs. 5 Lacs to Rs. 25 Lacs. Officer in default – Rs. 1 Lac to Rs. 5 Lac.

## SEC. 125 – IEPF

<b>Amount to be credited to IEPF</b>
<ul style="list-style-type: none"> <li>(a) Amount given by C.G. by way of grants;</li> <li>(b) Donations given by C.G., S.G., companies or any other institution;</li> <li>(c) Amount in the Unpaid Dividend Account;</li> <li>(d) Amount in the general revenue account of the C.G.;</li> <li>(e) Amount lying in the IEPF u/s 205C of the Companies Act, 1956;</li> <li>(f) the interest or other income received out of investments made from the Fund;</li> <li>(g) the amount received u/s 38(4);</li> <li><b>(h) the application money received by companies and due for refund;</b></li> <li><b>(i) matured deposits with companies ;</b></li> <li><b>(j) matured debentures with companies;</b></li> <li>(k) interest accrued on amounts referred to in clauses (h) to (j);</li> <li>(l) sale proceeds of fractional shares arising out of issue of bonus shares, merger &amp; amalgamation;</li> <li>(m) redemption amount of preference shares remaining unpaid for 7 or more years; &amp;</li> <li>(n) such other amount as prescribed.</li> </ul>
<b>Utilisation of IEPF</b>
<ul style="list-style-type: none"> <li>(a) Refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money due for refund and interest thereon;</li> <li>(b) promotion of investors' education, awareness and protection;</li> <li>(c) distribution of any disgorged amount among eligible applicants;</li> <li>(d) reimbursement of legal expenses incurred in class suits u/s 37 and 245;</li> <li>(e) any other purpose incidental thereto.</li> </ul>

# Chapter 12 – Audit of Dividend

## Steps for Verification

1. Examine MOA & AOA to ascertain dividend rights of different classes of shares.
2. Confirm that the dividend is made out of distributable profits having regard to the provisions of Sec. 123.
3. If the dividend is made out of reserves, examine the compliance of conditions as set out in the rules.
4. Inspect the shareholders' Minute Book to verify the amount of dividend declared.
5. Examine whether the amount of dividend payable has been deposited in a separate bank account within five days of declaration of dividend.
6. Check the particulars of members as are entered in the Dividend List by reference to the Register of Members.
7. Check the amount of dividend paid with the dividend warrants surrendered.
8. Verify whether dividend which is unclaimed or unpaid within 30 days of date of declaration has been transferred to "Unpaid Dividend Account" within 7 days from the date of expiry of 30 days.
9. Verify whether unpaid dividend amount which remain unpaid or unclaimed for a period of 7 years from the date of such transfer transferred to IEPF.

## Miscellaneous Provisions

Sec. 127	<p><b>Penalty for failure to pay dividend within 30 days:</b></p> <ul style="list-style-type: none"> <li>• Company – Simple Interest @18% p.a.</li> <li>• Directors – Imprisonment upto 2 years and fine which shall not be less than Rs. 1,000 per day of default.</li> </ul>
Sec. 126	<p><b>Right of dividend to be kept in Abeyance</b></p> <p>Where any instrument of transfer has been delivered to the company, but transfer not yet registered, the company shall transfer the dividend in unpaid dividend account unless the registered holder authorises the company to pay such dividend to transferee</p>
Revocation of Dividend	<ul style="list-style-type: none"> <li>• Regulation 80 of Table F of Schedule I - Company in general meeting may declare dividends, but it shall not exceed amount recommended by Board.</li> <li>• Sec. 127 - dividend has to be paid within 30 days from date of declaration.</li> <li>• Dividend once declared, becomes a debt against the company and cannot be revoked except in certain situations.</li> </ul> <p><b>Note: Final Dividend once declared in the AGM cannot be revoked by BOD. However before declaration of dividend in the AGM, dividend recommended by BOD may be revoked for just and proper reasons.</b></p>
Disclosure requirements for proposed dividend	<ul style="list-style-type: none"> <li>• Schedule III - Amount of dividend proposed to be distributed to equity and preference shareholders for the period and the related amount per share to be disclosed separately. It also requires separate disclosure of the arrears of fixed cumulative dividends on preference shares.</li> <li>• AS-4, "Contingencies and Events Occurring after the Balance Sheet Date" - if an enterprise declares dividends to shareholders after the balance sheet date, the enterprise should not recognise those dividends as a liability at the balance sheet date unless a statute requires otherwise. Such dividends should be disclosed in notes.</li> </ul>

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**PANKAJ GARG (CA, CS, CMA(I) – All India Topper & Gold Medalist)**



# Chapter 13 – CORPORATE GOVERNANCE

System by which companies are directed and governed by the management in the best interests of the stakeholders and others ensuring better management, greater transparency and timely financial reporting.

## Audit Committee (A.C.) u/s 177 of Companies Act, 2013

Section	Details		
<b>177(1)</b>	Companies required to constitute A.C.: Listed Companies & other prescribed (Public) companies: (i) companies with a paid up capital of ≥ 10 Cr.; (ii) companies having turnover ≥ Rs. 100 Cr.; (iii) companies, having in aggregate, outstanding loans or borrowings or debentures or deposits > 50 Cr.		
<b>177(2)</b>	<ul style="list-style-type: none"> <li>• Composition-Minimum 3 directors; majority independent directors.</li> <li>• Majority Members with Chairperson-ability to read &amp; understand, F.S.</li> </ul>		
<b>177(4)</b>	<p>Functions of Audit Committee include:</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 50%; vertical-align: top;"> <ol style="list-style-type: none"> <li>1. Recommendation-Appointment, Remuneration &amp; terms of auditors;</li> <li>2. Review &amp; monitor auditor’s independence &amp; audit effectiveness;</li> <li>3. Examination of F.S. &amp; auditors’ report thereon;</li> <li>4. Approval/Modification of transactions with related parties;</li> </ol> </td> <td style="width: 50%; vertical-align: top;"> <ol style="list-style-type: none"> <li>5. Scrutiny of inter-corporate loans and investments;</li> <li>6. Valuation of undertakings/assets, wherever it is necessary;</li> <li>7. Evaluation of IFC and risk management systems;</li> <li>8. Monitoring end use of funds raised through public offers.</li> </ol> </td> </tr> </table>	<ol style="list-style-type: none"> <li>1. Recommendation-Appointment, Remuneration &amp; terms of auditors;</li> <li>2. Review &amp; monitor auditor’s independence &amp; audit effectiveness;</li> <li>3. Examination of F.S. &amp; auditors’ report thereon;</li> <li>4. Approval/Modification of transactions with related parties;</li> </ol>	<ol style="list-style-type: none"> <li>5. Scrutiny of inter-corporate loans and investments;</li> <li>6. Valuation of undertakings/assets, wherever it is necessary;</li> <li>7. Evaluation of IFC and risk management systems;</li> <li>8. Monitoring end use of funds raised through public offers.</li> </ol>
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<b>177(5)</b>	<p>The Audit Committee may:</p> <ul style="list-style-type: none"> <li>• call for the comments of the auditors about IC systems, the scope of audit, including the observations, and</li> <li>• review of F.S. before their submission to the Board and</li> <li>• may discuss any related issues-internal &amp; statutory auditors.</li> </ul>		
<b>177(6)</b>	<ul style="list-style-type: none"> <li>• Investigate any matter specified u/s. 177(4) or referred to it by Board.</li> <li>• Power-to obtain professional advice from external sources &amp; full access to info contained in the records of the company.</li> </ul>		
<b>177(7)</b>	Auditors and KMP - right to be heard in meetings of A.C. when it considers auditor’s report but shall not have the right to vote.		
<b>177(8)</b>	<ul style="list-style-type: none"> <li>• Board’s report shall disclose the composition of A.C. and</li> <li>• Where the Board had not accepted recommendation of A.C., it shall be disclosed in report along with the reasons therefor.</li> </ul>		
<b>177(9)</b>	Vigil Mechanism		
<b>177(10)</b>			

## SEBI (LODR) Regulations, 2015

- (a) Board of Director including its composition, independent director, non executive director etc.;
- (b) Provisions regarding composition and functioning of Audit Committee (Regulation 18).
- (c) Provisions regarding setting up and role of Nomination and Remuneration Committee.
- (d) Provisions regarding setting up and role of Stakeholder Relationship Committee
- (e) Provisions regarding setting up and role of Risk Management Committee
- (f) Vigil mechanism
- (g) Related party Transaction
- (h) Management of Subsidiaries
- (i) Obligations w.r.t. Independent Directors
- (j) Obligations w.r.t. directors and senior management
- (k) Others as specified in Part E of schedule II (Discretionary).

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## AUDIT COMMITTEE (A.C.)

### Requirements of Audit Committee

1. A.C. - Minimum 3 directors. 2/3 shall be independent directors.
2. All members shall be financially literate & at least one member shall have accounting/related financial management expertise.
3. Chairman of the A.C. shall be an independent director.
4. Chairman of A.C. shall be present at AGM to answer shareholder queries.
5. A.C. at its discretion shall invite finance director or head of finance function, head of internal audit & representative of statutory auditor & such other executives, to be present at meetings of A.C.
6. Company Secretary shall act as the secretary to the committee.

### Meetings of Audit Committee:

- At least 4 & gap between 2 meetings - not more than 4 months.
- Quorum-Greater of 2 or 1/3 - minimum 2 independent members.

### Powers of audit Committee:

- To investigate any activity within its terms of reference.
- To seek information from any employee.
- To obtain outside legal or other professional advice.
- To secure attendance of outsiders with relevant expertise.

### Mandatory review Area:

- Management discussion & analysis of financial conditions and results of operations.
- Statement of significant related party transactions.
- Letters of IC weaknesses issued by the statutory auditors.
- Internal audit reports to internal control weaknesses; and
- Appointment, removal & remuneration of the Chief Internal Auditor.
- Statement of deviations on (a) quarterly statement of deviation including report of monitoring agencies submitted to stock exchange (b) annual statement of funds utilized for purposed other than those stated in offer document.

### Role of Audit Committee w.r.t. review of financial statements

Audit committee is required to review with management the annual financial statements before submission to the Board, focusing primarily on:

- (a) Matters required to be included in the Director's Responsibility Statement to be included in the Board's report in terms of Sec. 134(3)(c) of the Companies Act, 2013.
- (b) Changes, if any, in accounting policies and practices and reasons for the same
- (c) Major accounting entries involving estimates based on the exercise of judgment by management
- (d) Significant adjustments made in the financial statements arising out of audit findings
- (e) Compliance with listing and other legal requirements relating to financial statements
- (f) Disclosure of any related party transactions
- (g) Qualifications in draft audit report

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CA. PANKAJ GARG**

## MISCELLANEOUS

### 1 Content of Management Discussion and Analysis

1. Industry structure and developments.
2. Opportunities and Threats.
3. Segment-wise or product-wise performance.
4. Outlook
5. Risks and concerns.
6. Internal control systems and their adequacy.
7. Discussion on financial performance.
8. Material developments in Human Resources/Industrial Relations front, including number of people employed.

### 2 CEO/CFO Certification to Board

- (a) They have reviewed F.S. & CFS and that to the best of their knowledge & belief:
  - These statements do not contain any materially untrue statement or omit any material fact or contain statements that might be misleading.
  - These statements together present a true and fair view of the company's affairs & are in compliance with existing AS, applicable laws and regulations.
- (b) There are no transactions entered that are fraudulent, illegal and violative of the company's code of conduct.
- (c) They accept responsibility for establishing & maintaining IC w.r.t. financial reporting.
- (d) They have indicated to the auditors & A.C.:
  - Significant changes in i.C.
  - Significant changes in accounting policies during the year.
  - Instances of significant fraud.

### 3 Circumstances in which adverse or qualified statement can be issued on Corporate Governance

1. Number of non-executive directors is < 50% of the strength of BOD.
2. A qualified and independent audit committee is not set up.
3. The chairman of the audit committee is not an independent director.
4. The audit committee does not meet four times a year.
5. Necessary powers not been vested by Board in the audit committee.
6. Time gap between two Board meetings is more than four months.
7. Director is a member of more than 10 committees.
8. Information of quarterly results is neither put on the company's website nor sent in a form so as to enable the Stock Exchange to put it on its own website.
9. The power of share transfer is not delegated to an officer or a committee or to the registrar and share transfer agents.

# Chapter 14 – LIABILITIES OF AUDITOR

## LIABILITIES UNDER COMPANIES ACT, 2013

## LIABILITIES UNDER INCOME TAX ACT, 1961

### CRIMINAL LIABILITIES

### CIVIL LIABILITIES

<b>Sec. 34</b>	<b>Criminal liability for mis-statements in prospectus</b>
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Where any prospectus is issued or circulated or distributed, which includes any statement which is untrue or misleading or where any inclusion or omission of any matter is likely to mislead, then every person who authorises the issue of such prospectus shall be liable u/s 447 (fraud).

<b>Sec. 448</b>	<b>Criminal Liability for making false statement</b>
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If in any return, report, certificate, F.S., prospectus, statement or other document under this law, any person makes a statement,

(a) which is false in any material particulars, knowing it to be false; or

(b) which omits any material fact, knowing it to be material,

he shall be liable under section 447.

<b>Sec. 447</b>	<b>Punishment for Fraud u/s 447</b>
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- any person who is found to be guilty of fraud, shall be punishable with imprisonment for a term 6 months to 10 years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to 3 times the amount involved in fraud.
- Provided that where the fraud in question involves public interest, the term of imprisonment shall not be less than 3 years.

<b>Sec. 35</b>	<b>Civil liability for mis-statements in prospectus</b>
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Where a person has subscribed for securities of a company acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the company and every person who—

- (a) is a director of the company at the time of the issue of the prospectus;
  - (b) has authorised himself to be named and is named in the prospectus as a director of the company, or has agreed to become such director, either immediately or after an interval of time;
  - (c) is a promoter of the company;
  - (d) has authorised the issue of the prospectus; and
  - (e) is an expert,
- shall, be liable to pay compensation to every person who has sustained such loss or damage.

**COMPILED BY:  
CA. PANKAJ GARG**

<b>Sec. 288</b>	<b>Disability as to represent the assessee</b>
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- A person who has been convicted of any offence connected with any Income Tax proceeding or on whom a penalty has been imposed under the said Act is disqualified from representing an assessee.
- CA found guilty of professional misconduct by the Council of the ICAI, can not act as a representative for such time that the order of Council disqualifies him from practising.

<b>Sec. 278</b>	<b>Any person who acts or induces, in any manner another person to make &amp; deliver to IT Authorities a false account, statement, or declaration, relating to any taxable income which he knows to be false or does not believe to be true is punishable with imprisonment from 3 months to 7 years &amp; fine</b>
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Any person who acts or induces, in any manner another person to make & deliver to IT Authorities a false account, statement, or declaration, relating to any taxable income which he knows to be false or does not believe to be true is punishable with imprisonment from 3 months to 7 years & fine

<b>Rule 12A</b>	<b>A CA who as an authorised representative has prepared the return filed by the assessee, has to furnish to the A.O., the particulars of accounts, statements and other documents supplied to him by the assessee for the preparation of the return.</b>
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- A CA who as an authorised representative has prepared the return filed by the assessee, has to furnish to the A.O., the particulars of accounts, statements and other documents supplied to him by the assessee for the preparation of the return.
- Where the CA has conducted an examination of such records, he has also to submit a report on the scope and results of such examination.
- If this report contains any information which is false and which the CA either knows or believes to be false, he would be liable to rigorous imprisonment which may extend to seven years and to a fine.

# Chapter 15 - COST AUDIT

## Meaning, Functions & Types

Meaning of Cost Audit	
Application of auditing principles and procedure in the field of cost accounting.	
Functions of Cost Audit	
1	<b>Verification of Cost accounting Records</b> - to ensure accuracy of cost accounts, cost reports, cost statements, cost data.
2	<b>Examination of Cost Accounting Records</b> - to ensure that they adhere to cost accounting principles, procedures and objectives.
Types of Cost Audit	
1	<b>Cost Audit on behalf of management</b> - <ul style="list-style-type: none"> <li>establish accuracy of cost data,</li> <li>ascertaining abnormal wastages,</li> <li>fixation of contract prices,</li> <li>Determination of p.u. cost of production.</li> <li>Determining overhead absorption rates</li> </ul>
2	<b>Cost Audit on behalf of customers</b> - insisted in case of cost plus contract
3	<b>Cost Audit on behalf of Government</b> - to consider the grant or assessment of production based taxes.
4	<b>Cost Audit on behalf of trade associations</b> - so as to control the prices.
5	<b>Statutory Cost audit</b> - Sec. 148
Circumstances under which a cost audit is ordered	
1	Price Fixation
2	Cost Variations within the industry
3	Inefficient management
4	Tax Assessment
5	Trade Disputes.

## Advantages

Advantages of Cost Audit	
<b>Management</b>	<ol style="list-style-type: none"> <li>1. Get reliable data for day to day operations.</li> <li>2. Close and continuous check on wastes.</li> <li>3. Identification of inefficiencies.</li> <li>4. Management by Exception.</li> <li>5. Reliable check in valuation of inventory.</li> <li>6. Detection of errors and frauds.</li> </ol>
<b>Society</b>	<ol style="list-style-type: none"> <li>1. Price fixation on basis of correct data.</li> <li>2. No price increase without justified increase in cost.</li> <li>3. Helpful in cost reduction.</li> <li>4. Proper utilisation of scarce resources.</li> </ol>
<b>Shareholder</b>	<ol style="list-style-type: none"> <li>1. Ensures proper maintenance of records.</li> <li>2. Economic and efficient operations.</li> <li>3. Fair valuation of Inventories.</li> </ol>
<b>Govt.</b>	<ol style="list-style-type: none"> <li>1. Fixation of Prices of essential commodities.</li> <li>2. Identifying inefficient units.</li> <li>3. Protection to sick industries.</li> <li>4. Settlement of trade disputes.</li> <li>5. Generation of healthy competition.</li> <li>6. Decision for sanctioning grants.</li> <li>7. Assessments of taxes based on production.</li> </ol>

## Cost Audit Programme/Matters to be covered

<b>Review of Records</b>	<p>This will include:</p> <ul style="list-style-type: none"> <li>Method of costing in use</li> <li>Method of accounting for raw material, stores, spares, wastage</li> <li>System of recording wages, etc.</li> <li>Basic of allocation of overheads</li> <li>Treatment of expenses on finance, R&amp;D, royalty, etc.</li> <li>Method for dep. accounting</li> <li>Method of stocktaking &amp; valuation</li> <li>System of budgetary control</li> </ul>
<b>Verification of Cost statement</b>	<p>This will mainly cover:</p> <ul style="list-style-type: none"> <li>Licensed, installed and utilized capacity</li> <li>Operating and financial ratio</li> <li>Production data</li> <li>Consumption of material and actual expenses</li> <li>Sales realization</li> <li>Abnormal non-recurring and special cost</li> <li>Reconciliation with financial books</li> </ul>
<b>Reference to financial records</b>	<ul style="list-style-type: none"> <li>Cost auditor, while framing his opinion is required to examine various information like cost of raw materials consumed, cost of fuel, employee costs, dep, etc., which is turn is available in financial records.</li> <li>Annexure to the cost audit reports (Form CRA-3) require reporting on followings:                             <ol style="list-style-type: none"> <li>1. Reconciliation of profit,</li> <li>2. Value addition &amp; Distribution of Earnings</li> <li>3. Financial Position and Ratio analysis.</li> <li>4. Related Party Transactions.</li> <li>5. Reconciliation of Indirect Taxes.</li> </ol> </li> <li>Such information is available only from financial records.</li> <li>Information covered in Part II of Schedule III to the Companies Act, 2013, w.r.t. consumption of raw materials, purchases of stock-in-trade, sales of products, changes in inventories, work-in-progress, stock-in-trade etc. are also to be covered in cost statements.</li> </ul>

## Miscellaneous

<b>True &amp; Fair Cost of Production</b>	<p>Considerations in determining true and fair cost of production are:</p> <ul style="list-style-type: none"> <li>Determination of cost as per generally accepted cost accounting principles</li> <li>Application of costing system appropriate to product</li> <li>Materiality</li> <li>Consistency in the application of costing system and cost accounting principles</li> <li>Maintenance of cost records &amp; preparation of cost statements in the prescribed form</li> <li>Abnormal wastage's and losses and other unusual transactions being ignored in determination of cost.</li> </ul>																					
<b>Reconciliation of Cost and Financial accounts</b>	<p>Part D of Annexure to CRA-3 requires cost auditor to incorporate a profit reconciliation.</p> <table border="1" style="width: 100%; border-collapse: collapse; margin: 5px 0;"> <thead> <tr> <th></th> <th style="text-align: center;">CY</th> <th style="text-align: center;">PY</th> </tr> </thead> <tbody> <tr> <td>1 Profit as per Cost Records</td> <td></td> <td></td> </tr> <tr> <td>2 Add: income not considered</td> <td></td> <td></td> </tr> <tr> <td>3 Less: Expenses not considered</td> <td></td> <td></td> </tr> <tr> <td>4 Difference in valuation of stock</td> <td></td> <td></td> </tr> <tr> <td>5 Other Adjustments</td> <td></td> <td></td> </tr> <tr> <td>6 Profit as per financial accounts</td> <td></td> <td></td> </tr> </tbody> </table> <p>It helps the auditor to identify instances of any misstatement by comparing the information.</p>		CY	PY	1 Profit as per Cost Records			2 Add: income not considered			3 Less: Expenses not considered			4 Difference in valuation of stock			5 Other Adjustments			6 Profit as per financial accounts		
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<b>Composite audit</b>	<ul style="list-style-type: none"> <li>Composite audit means combining cost audit and financial audit.</li> <li>Possible only if objectives of both audits are common.</li> <li>Objective of financial audit is to express an opinion on true and fair view of F.s. while objective of cost audit is to ascertain true and fair view of cost of production.</li> <li>Cost audit is a tool in hands of management while financial audit is conducted on behalf of shareholders.</li> </ul> <p><b>Conclusion:</b> difficult to combine due to different objectives.</p>																					
<b>Cost statement</b>	<p>Cost statement as per CRA-1 shall include the following:</p> <ol style="list-style-type: none"> <li>1. <b>Quantitative information</b> in respect of each good or service showing details of available capacity, actual production, production as per excise records, capacity utilization, quantity available for sale, wastage and actual sale.</li> <li>2. Details of cost of production, cost of sale of goods and margin in total as well as p.u.</li> <li>3. Reconciliation of Indirect Taxes.</li> </ol> <p>These statements are to be prepared for each plant, factory or service centre.</p>																					

# Cost Records and Cost Audit (Section 148 of Companies Act, 2013 & Companies (Cost Records and Audit), Rules, 2014)

## Cost Records

**Sec. 148(1)**  
C.G. may by order  
↓  
In respect of such companies  
↓  
Engaged in  
↓  
production of prescribed goods  
Or  
providing prescribed services  
↓  
direct that  
↓  
particulars relating to  
↓  
Material  
Labour  
or  
Other items of cost  
↓  
Shall be included in  
↓  
the books of accounts

**Rule 3 of Companies (Cost Records & Audit) Rules, 2014**  
Companies including foreign companies  
↓  
Engaged in  
↓  
production of goods  
Or  
providing services as specified  
↓

Regulated Sector	Non Regulated Sector
<ul style="list-style-type: none"> <li>• Telecommunication</li> <li>• Electricity</li> <li>• Petroleum</li> <li>• Sugar</li> <li>• Drugs and Pharma</li> <li>• Fertilisers</li> </ul>	<ul style="list-style-type: none"> <li>• Iron</li> <li>• Steel</li> <li>• Rubber</li> <li>• Cement</li> <li>• etc.</li> </ul>

↓  
Having turnover  $\geq 35$  Cr.  
↓  
During immediate preceding financial year  
↓  
shall include cost records in their books of accounts

**Rule 5** Every Company under these Rules shall In respect of each of its Financial year  
↓  
Maintain Cost records in Form CRA - 1

## Cost Audit

**Requirement**  
↓

**Sec. 148(2)**  
C.G. may be order  
↓  
direct for the  
↓  
audit of cost records of  
↓  
companies covered u/s 148(1)  
↓  
having prescribed net worth or turnover  
↓  
in a manner  
↓  
specified in that order

**Rule 4 of Companies (Cost Records & Audit) Rules, 2014**  
Cost Records are required to be audited  
↓  
If overall annual turnover  
↓  
From all products and services  
↓  
In immediate preceding Financial Year  
↓  
In case of

Regulated Sector	Non Regulated Sector
$\geq 50$ Cr.	$\geq 100$ Cr.

↓  
**AND**  
↓

Aggregate Turnover of Individual product or service	
$\geq 25$ Cr.	$\geq 35$ Cr.

**Exemption - Rule 4(3)**  
Requirement of Cost Audit shall not apply to a company  
↓  
Whose revenue from exports in foreign exchange exceeds 75% of its total revenue  
or  
which is operating from SEZ.  
or  
Engaged in generation of electricity for captive consumption

## Cost Auditor

**Sec. 148(3)**  
Cost Audit shall be conducted  
↓  
by Cost Accountant  
↓  
Appointed by BOD  
↓  
No person appointed u/s 139 As an auditor  
↓  
Shall be appointed as cost auditor

**Rule 6 of Companies (Cost Records & Audit) Rules, 2014**  
Cost Auditor shall be appointed within 180 days of commencement of every financial year.  
Before appointment written consent & certificate be obtained.  
Company Shall inform the cost auditor of his appointment.  
Company Shall file a notice with CG in Form CRA-2 within 30 days of Board meeting or within 180 days of commencement of FY whichever is earlier.  
Cost Auditor appointed as such shall continue till expiry of 180 days of closure of FY or till submission of cost audit report.  
Cost statements shall be approved by BOD before being signed by any director on behalf of Board for submission to cost auditor.

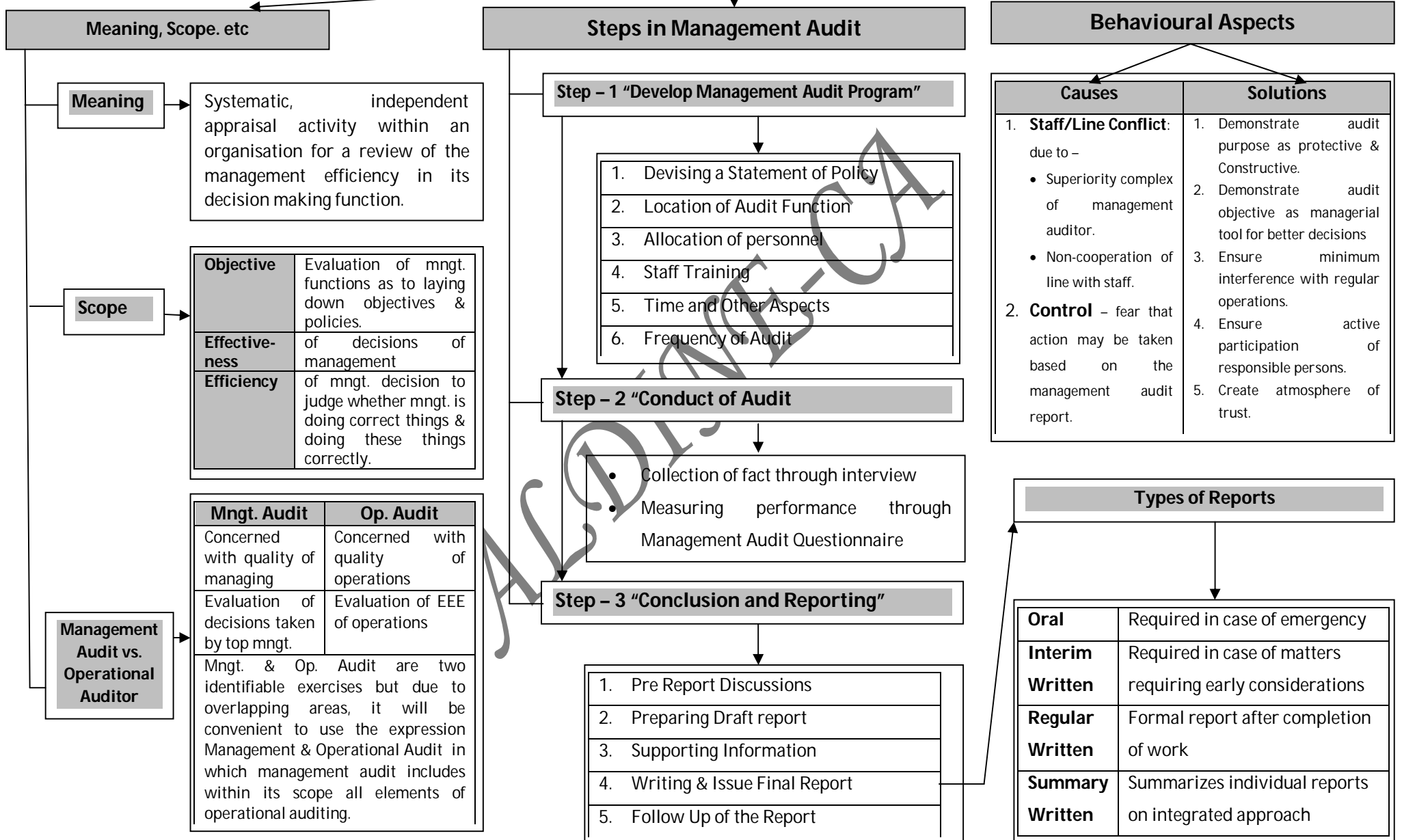
## Cost Audit report

**Sec. 148(5) & 148(6)**  
Cost Auditor shall submit his report to  
↓  
BOD  
↓  
Company shall  
↓  
within 30 days of date of receipt of report  
↓  
furnish such report to CG  
↓  
along with full information & explanation.

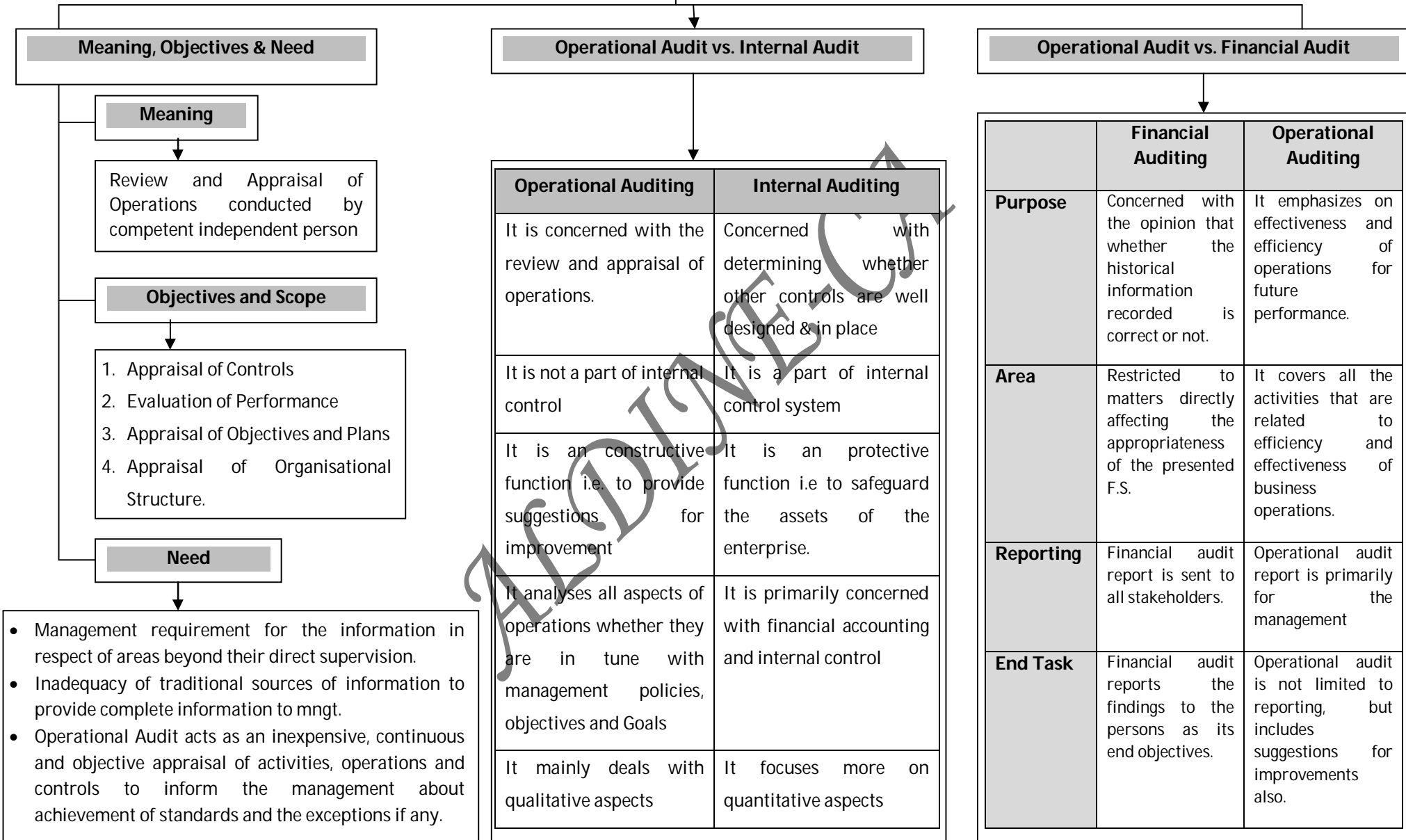
**Rule 6 of Companies (Cost Records & Audit) Rules, 2014**  
Cost Auditor shall submit Cost Audit Report  
↓  
in Form CRA-3.  
Cost Auditor shall forward Duly Signed Report to BOD  
↓  
Within 180 days from closure of FY.  
Report along with information & explanation to  
↓  
Shall be furnished to CG in Form CRA-4 in XBRL Format

*Compiled by: CA. Pankaj Garg*

# Management Audit



# OPERATIONAL AUDIT



## INVESTIGATION UNDER COMPANIES ACT 2013

### Investigation into affairs of company – Sec. 210

CG	may →	Order an investigation into affairs of the company ↓ On receipt of a report of Registrar/Inspector u/s 208 Or On intimation of a Special resolution passed by company in this regard Or In public interest.
CG	shall →	Order an investigation into affairs of a company ↓ Where an order is passed by a Court or Tribunal in this regard
CG	may →	Appoint one or more persons ↓ as inspectors ↓ who report to CG ↓ in manner as directed by CG.

### Investigation into affairs of company by SFIO – Sec. 212

CG may, by order assign investigation into affairs of a company to ↓ SFIO (Serious Fraud Investigation Office) ↓ On receipt of a report of Registrar/Inspector u/s 208 Or On intimation of a Special resolution passed by company in this regard Or In public interest Or On request from any Department of CG/SG	
Director, SFIO	may designate such number of inspectors ↓ as he considers necessary for investigation.
SFIO	Shall conduct the investigation ↓ In prescribed manner ↓ And submit its report to CG within period specified in order

### Investigation into affairs in other cases – Sec. 213 (Not notified yet)

Tribunal may on application of ↓	
Specified number of Members	Any Other person
Company having Share Capital	≥100 Members or Members holding ≥ 1/10 <sup>th</sup> of Total Voting Power If satisfied that: Business of company is being conducted with intent to defraud Or Promoters / Mngt. being guilty of fraud or misconduct towards the company Or Members not being provided with required information
Company having no Share Capital	1/5 <sup>th</sup> of Total Members
↓	
After giving a reasonable opportunity of being heard to concerned parties ↓	
Order for the investigation into affairs of the company ↓	
By an inspector appointed by CG.	

### Investigation into Ownership of company – Sec. 216

CG may appoint one or more Inspectors ↓ To investigate and report ↓ For purpose of determining the true persons ↓ Who are or have been financially interested in the success or failure of the company Or Who are or have been able to control or materially influence the policy of the company.
CG may define the scope of investigation wr.t. matters / period / particular shares or debentures
Powers of Inspector extended to investigation of any circumstances suggesting the existence of any arrangement which is relevant for investigation
<b>Compiled by: CA. Pankaj Garg</b>



# POWERS OF INSPECTORS & REPORT OF INSPECTOR ON INVESTIGATION UNDER COMPANIES ACT 2013

## Procedures, Powers etc. of Inspectors - Sec. 217

<b>Production of documents</b>	<ul style="list-style-type: none"> <li>Officers, Employees and agents of the company should produce all book and papers and provide necessary assistance.</li> <li>With the previous approval of CG, inspector may require information of any other body corporate.</li> <li>Inspector may detain the books for 180 days.</li> </ul>
<b>Examine on Oath</b>	<ul style="list-style-type: none"> <li>Inspectors may examine Officers, employees and agents of company or related companies on oath.</li> <li>Previous approval is required to examine any other person.</li> </ul>
<b>Powers of Civil Court</b>	<ul style="list-style-type: none"> <li>Discovery &amp; production of books &amp; other documents at such place &amp; time as specified.</li> <li>Summoning and enforcing attendance of person and examine them on oath.</li> <li>Inspection of any books, registers &amp; other documents at any place.</li> </ul>

## Investigation into affairs of related companies - Sec. 219

With the prior approval of CG,  
↓  
inspector may also investigate the affairs of following:  
↓

- any body corporate which is/has at relevant time been the subsidiary or holding or another subsidiary of same holding of company under investigation.

or

- Any body corporate which is/has at relevant time been managed by any person as MD or Manager who is the MD or Manager of company under investigation.

or

- Any body corporate whose BOD comprises nominees of company under investigation.

or

- Managing Director, Manager or employee of company under investigation.

**Compiled by: CA. Pankaj Garg**

## Seizure of documents - Sec. 220

If Inspector has reasonable grounds  
↓  
That books & papers of company / other body corporate/MD/Manager  
↓  
are likely to destroyed  
↓  
the inspector may  
↓  
enter into places where these books are kept with required assistance  
And  
Seize the books and papers after allowing the company to take copies of such books.  
↓  
Such books and papers may be kept by inspector  
↓  
for such period not later than the conclusion of the investigation.

## Inspector's Report - Sec. 223

Inspector  
↓

May/shall	shall
Submit	Submit
Interim Report	Final Report
To CG	To CG
When required	On conclusion of investigation

↓  
Report shall be in writing or printed as CG may direct.  
↓  
Report may be obtained by making an application to CG  
↓  
The report shall be authenticated  
↓  
by seal of the company whose affairs have been investigated  
or  
by certificate of a public officer

# Chapter 21 – PEER REVIEW

## MEANING, OBJECTIVES & SCOPE OF PEER REVIEW

<b>Meaning</b>	<ul style="list-style-type: none"> <li>Examination &amp; Review of systems &amp; procedures to determine whether they have been put in place by PU</li> <li>for ensuring the quality of attestation services as envisaged and implied/ mandated by the <b>technical standards, Ethical Standards &amp; Professional Standards</b> and</li> <li>whether these were effective or not during the period under review.</li> </ul>
<b>Objectives</b>	<ol style="list-style-type: none"> <li>To ensure that members while carrying out assurance service assignments comply with <b>Technical, Professional and Ethical Standards</b> issued by the Institute;</li> <li>To ensure that member has in place proper system, including documentation thereof, for maintaining the quality of assurance services;</li> <li>To ensure adherence to various statutory &amp; regulatory requirements.</li> <li>To identify and address patterns of non-compliance with quality control standards.</li> </ol>
<b>Scope</b>	<p>Peer Review process shall apply to <b>all assurance services</b> provided by PU. While carrying out review, reviewer examines assurance engagement records of PU so as to cover the following:</p> <ol style="list-style-type: none"> <li>Compliance with <b>Technical, Professional &amp; Ethical Standards</b>;</li> <li>Quality of reporting.</li> <li>Systems and procedures for carrying out <b>assurance services</b>.</li> <li>Training programmes for staff concerned with assurance functions, including availability of appropriate infrastructure.</li> <li>Compliance with directions and/or guidelines issued by the Council including Fees to be charged, Number of audits undertaken, register for Assurance Engagements conducted during the year and such other related records.</li> <li>Compliance with directions and/or guidelines issued by the Council in relating to article assistants and/or audit assistants, including attendance register, work diaries, stipend payments, and such other related records.</li> </ol>

### Technical, Ethical & Professional Standards

- (1) AS issued by ICAI and/or prescribed and notified by the C.G. of India;
- (2) Standards issued by the ICAI including
  - (a) Engagement standards
  - (b) Statements
  - (c) Guidance notes
  - (d) Standards on Internal Audit
  - (e) Statements on Quality Control
  - (f) Notifications/Directions/Announcements/Guide lines/Pronouncements/Professional standards issued by the Council or any of its committees.
- (3) Framework for Preparation & presentation of F.S.;
- (4) Framework of statements and SA, SAE, SQC
- (5) Guidance Notes on related services issued by ICAI;
- (6) Provisions of the various relevant statutes and/or regulations which are applicable in the context of the specific engagements.

**'Assurance Services'** is used interchangeably with **Audit Services, Attestation Functions & Audit Functions**, but shall not include the following:

1. Management Consultancy Engagements;
2. Representation before various Authorities;
3. Engagements to prepare tax returns or advising clients in taxation matters;
4. Engagements for compilation of F.S.;
5. Engagements solely to assist the client in preparing, compiling or collating information other than F.S.;
6. Testifying as an expert witness;
7. Providing expert opinion on points of principle, such as AS or the applicability of certain laws, on the basis of facts provided by the client; and
8. Engagement for Due diligence

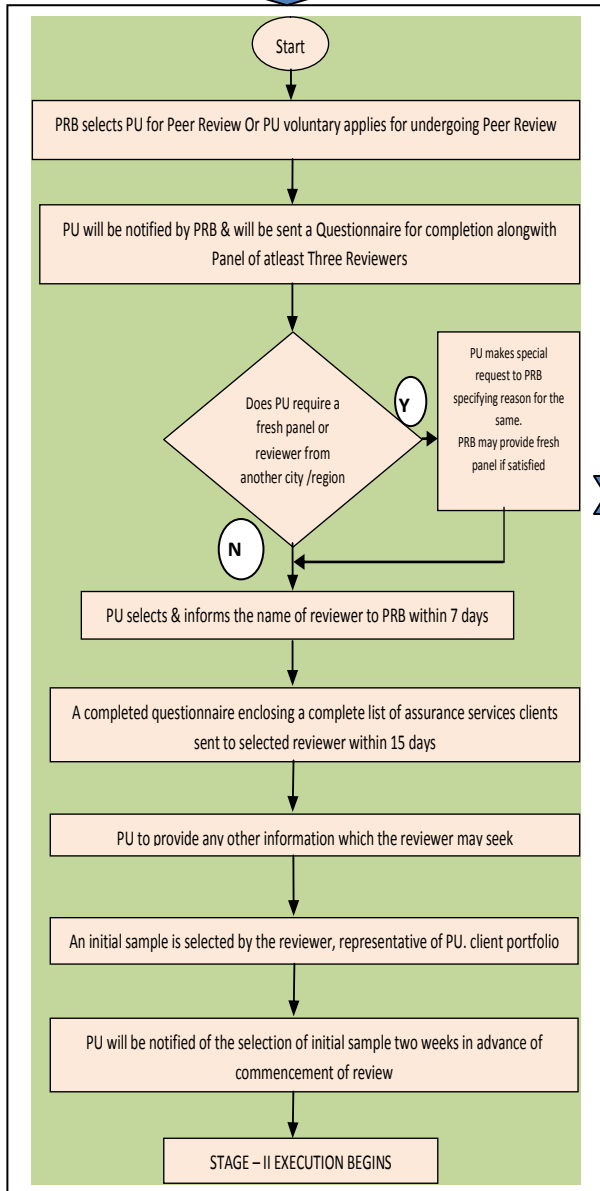
## Miscellaneous

<b>Assessment of Independence</b>	<ul style="list-style-type: none"> <li>Does the PU have a policy to ensure independence, objectivity and integrity, on the part of partners and staff? Who is responsible for this policy?</li> <li>Does the PU communicate these policies and the expected standards of professional behavior to all staff?</li> <li>Does the PU monitor compliance with policies and procedures relating to independence?</li> <li>Does the PU periodically review its association with clients to ensure objectivity and independence?</li> </ul>
<b>Collection of Evidences</b>	<p>A Peer Reviewer collects evidence by applying the following methods:</p> <ol style="list-style-type: none"> <li><b>Inspection:</b> It includes scrutiny of documentation &amp; other records of PU.</li> <li><b>Observation:</b> of procedures/processes followed in the PU.</li> <li><b>Inquiries:</b> from the responsible person of PU, even by the use of questionnaire.</li> </ol>
<b>Inherent Limitations of Peer Review</b>	<ul style="list-style-type: none"> <li>Review is conducted in accordance with Statement on Peer Review.</li> <li>Review would not necessarily disclose all weaknesses in compliance of technical standards and maintenance of quality of assurance services since it would be based on selective tests.</li> <li>As there are inherent limitations in the effectiveness of any system of quality control which happens to be subject-matter of review, departure from the system may occur &amp; may not be detected.</li> </ul>

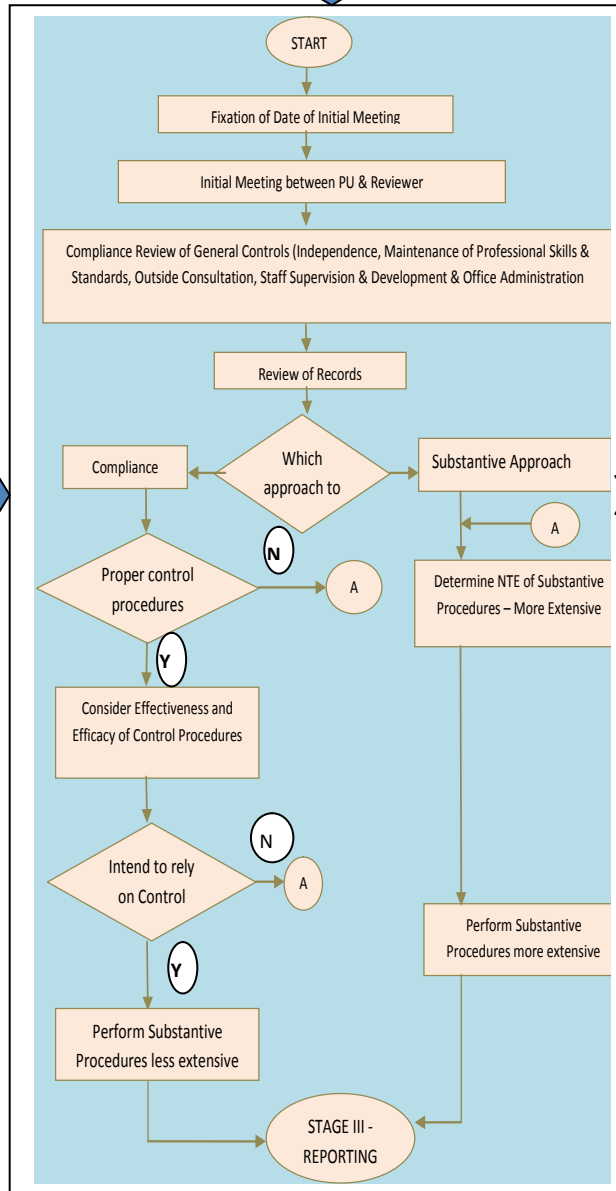
**Compiled by: CA. Pankaj Garg**

# PEER REVIEW PROCESS

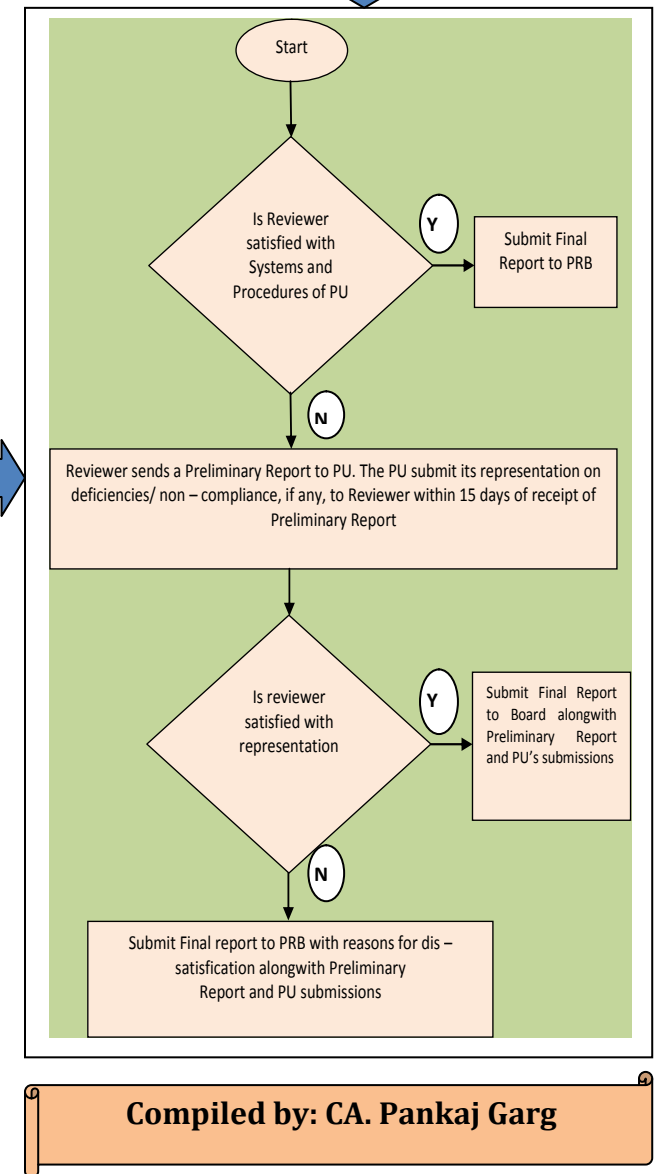
## Stage I - Planning



## Stage II - Execution



## Stage III - Reporting



**Compiled by: CA. Pankaj Garg**

# Audit of Banking Companies - BASICS

## Principal Enactments Governing Bank Audit

- Banking Regulation Act, 1949;
- RBI Act, 1934;
- Banking Companies (Acquisition & Transfer of Undertakings) Act, 1970;
- SBI Act, 1955;
- SBI (Subsidiary Banks) Act, 1959;
- Regional Rural Banks Act, 1976;
- Companies Act, 2013;
- Cooperative Societies Act, 1912;
- Information Technology Act, 2000;
- Prevention of Money Laundering Act, 2002;
- SRFAESI Act, 2002;
- Credit Information Companies Regulation Act, 2005; and
- Payment & Settlement systems Act, 2007

## REQUIREMENTS OF RISK MANAGEMENT SYSTEM

<b>1</b>	<b>Involvement of TCWG</b>	Risk Management policies should be approved by TCWG having regard to bank's business objectives & strategies, capital strength, mngt expertise, regulatory requirements & types of risks.
<b>2</b>	<b>Identification, Measurement &amp; Monitoring of Risks</b>	Risks that may significantly affect the achievement of bank's goals and objectives should be identified, measured and monitored.
<b>3</b>	<b>Control Activities</b>	Banks must have controls including the following: <ul style="list-style-type: none"> <li>effective segregation of duties,</li> <li>verification and approval of transactions,</li> <li>setting of limits,</li> <li>reporting and approval of exception.</li> </ul>
<b>4</b>	<b>Monitoring Activities</b>	Risk mng models, methodologies and assumptions used to measure and manage risk need to be evaluated by Independent risk management unit
<b>5</b>	<b>Reliable Information System</b>	must exist so as to provide adequate financial, operational and compliance information on a timely and consistent basis to management and TCWG.

## EVALUATION OF INTERNAL CONTROLS

1. Bills for Collection	2. Bills Purchased
<ol style="list-style-type: none"> <li>1. Documents accompanying bill should be received &amp; entered in the register by a proper officer.</li> <li>2. Account of principal should be credited only after realisation of the bill.</li> <li>3. Ensure that bills sent by one branch to another for collection are not included twice in balance sheet.</li> </ol>	<ol style="list-style-type: none"> <li>1. Verify that all documents of title are properly assigned to the bank.</li> <li>2. Sufficient margin should be kept while purchasing or discounting of a bill.</li> <li>3. Irregular outstanding accounts should be periodically reported to the head office.</li> <li>4. Proportionate income should be recognised between the periods.</li> </ol>
3. Loans and Advances	4. Credit Card Operation
<ul style="list-style-type: none"> <li>Evaluation of Customer creditworthiness.</li> <li>Sanctioning by proper authority.</li> <li>Execution of Necessary Documents.</li> <li>Keeping Sufficient Margin.</li> <li>Safe custody of securities held.</li> <li>Registration of charges in favour of bank.</li> <li>Inspection of securities on regular basis.</li> <li>Determination of market value of securities.</li> <li>Adjustment in drawing power with decrease in value of assets.</li> <li>Reporting of Irregular accounts to Head office</li> <li>Review of accounts on timely basis.</li> </ul>	<ol style="list-style-type: none"> <li>1. Effective screening of applications.</li> <li>2. Strict control over storage and issue of cards.</li> <li>3. Existence of a system to confirm status of unutilised limit before accepting the settlement .</li> <li>4. Existence of system of prompt reporting by the merchants of all settlements accepted.</li> <li>5. Reimbursement to merchants only after verification of valid acceptance of cards.</li> <li>6. Reimbursements should be immediately charged to the customer's account.</li> <li>7. Existence of system to ensure that statements are sent regularly and promptly to the customer.</li> <li>8. Existence of a system to monitor and follow-up of customers' payments.</li> <li>9. Identifying the items overdue beyond a reasonable period.</li> <li>10. Existence of a system for periodic review of credit card holders' accounts.</li> </ol>
5. Telegraphic Transfers and Demand Drafts	
<ol style="list-style-type: none"> <li>1. Codes for TT should be known only to responsible officers.</li> <li>2. Coding and Decoding should be done only by authorised officers.</li> <li>3. Signatures on documents used for TT and DD should be checked by an officer.</li> <li>4. All TT &amp; DD sold by a branch should be immediately confirmed by advices to the branches concerned.</li> <li>5. If the paying branch does not advice from the issuing branch or does not receive credit in its account with that branch, it should take immediate steps to ascertain the reasons.</li> </ol>	

*Compiled by:*  
**CA. Pankaj Garg**

# Audit of Banking Companies – VERIFICATION OF INVESTMENTS

## AUDIT PROCEDURE

1	<b>Internal control evaluation</b>	To ensure they are in accordance with RBI Guidelines. Investment policy must confirm to RBI Guidelines.
2	<b>Separation of Investment Functions</b>	Own investment account need to be separated from PMS client accounts.
3	<b>Examination of Reconciliation</b>	
4	<b>Examination of Documents</b>	To ensure that investments made are within authority and supported by documentation.
5	<b>Physical verification</b>	<ul style="list-style-type: none"> <li>Should be carried out on balance Sheet date,</li> <li>In exceptional case, carry out the physical verification as near to balance sheet date as possible.</li> <li>In case of scripless dealings, verify the yearend confirmations of depository.</li> </ul>
6	<b>Examination of Valuation</b>	Method of accounting including yearend valuation is appropriate. If inappropriate, consider the effect of adoption of such policy on F.S.
7	<b>Dealing in securities on behalf of Others</b>	Income from such activities to be recorded fairly.
8	<b>Examination of Classification and Shifting</b>	

*Compiled by: CA. Pankaj Garg*

## SPECIAL PURPOSE CERTIFICATES

Central Auditors are required to issue following certificates:

1. Certificate on reconciliation of securities by the bank (both on its own investment account as well as PMS Client's account).
2. Certificate on compliance by the bank in key areas of prudential and other guidelines relating to such transactions issued by RBI.

## CLASSIFICATION AS PER PRUDENTIAL NORMS

1	<b>Held to Maturity (HTM)</b>	Securities acquired by bank with the intention to hold till maturity.
2	<b>Held for Trading (HFT)</b>	Securities acquired by bank with the intention of trading, i.e. to be sold within 90 days.
3	<b>Available for Sale (AFS)</b>	Securities which do not qualify for being classified as HTM or HFT.
<b>Category of investment should be decided at the time of acquisition and recorded on investment proposal.</b>		

## NON PERFORMING INVESTMENTS

Those investments where interest/principal is due and remains unpaid for >90 days and includes:

1. Preference Shares where dividend is not paid.
2. Unquoted equity shares value @1.
3. Securities issued by a person who has been given credit facility which is a NPA.
4. Equity, debentures etc. received as a result of conversion of NPA.

## INCOME RECOGNITION NORMS

1	<b>Performing Investments</b>	Accrual basis provided interest rate is predetermined.
2	<b>NPI</b>	Realisation Basis
3	<b>Govt. Guarantee</b>	Accrual basis, provided interest is serviced regularly.
4	<b>Dividend</b>	Accrual basis, if right to receive dividend is established.
5	<b>Discount on discounted instruments</b>	Accrual basis over the remaining period of maturity.
6	<b>Units of Mutual Funds</b>	Cash Basis
7	<b>Sale of Investments</b>	Profit or loss to be shown in Profit & Loss Account.

## NPA CLASSIFICATION

An Advance will be classified as NPA if:

- (a) It ceases to generate income for a bank.
- (b) Interest and/or installment of principal remained overdue or out of order for a specified period of time.
  - Overdue: Amount not paid on the due date fixed by the Bank.
  - Out of Order: outstanding balance remains continuously in excess of the sanctioned limit/drawing power.

Or

No credits continuously for 90 days as on B/S date or credits are not enough to cover interest debited during same period.

### Classification in Special cases

<b>Account regularized near B/S date</b>	Classify as NPA if account has inherent weaknesses.
<b>Account classification borrower wise</b>	All facilities granted to same borrower will be treated as NPA
<b>Advances under Consortium</b>	Based on recovery of individual member bank.
<b>Moratorium Period</b>	A/c will not be treated as overdue with respect to date of debit of interest during moratorium period.
<b>Temporary Deficiencies</b>	Ensure - DP arrived on basis of stock statement (not older than 3 months)

### NPA Classification w.r.t. Specified Advances

<b>Term Loans</b>	Interest /Installment remain overdue >90 days
<b>CC/OD</b>	Account remained overdue >90 days.
<b>BP/BD</b>	Bills remained overdue >90 days
<b>Agricultural Advances</b>	Interest/Installment remain overdue >2 crop seasons (short duration crops) >1 crop season (long duration crops)
<b>Credit Card Accounts</b>	Min. amount due not paid within 90 days from next statement due.
<b>Other Accounts</b>	Amount overdue >90 days.

## Exception to NPA Classification Norms

<b>1</b>	<b>Temporary Deficiencies</b>	<ul style="list-style-type: none"> <li>• Like non submission of stock statement, non renewal of limits.</li> <li>• A/c will not be classified as NPA if A/c has inherent strength.</li> </ul>
<b>2</b>	<b>Natural Calamities</b>	Short term agricultural loan converted short term loans will be treated as current dues.
<b>3</b>	<b>Facilities backed by CG Guarantee</b>	Overdue A/c will be classified as NPA only when CG repudiates its guarantee.

## INCOME RECOGNITION

<b>1</b>	<b>General Rule</b>	Accrual basis if it is reasonable to expect its ultimate collection.
<b>2</b>	<b>NPAs</b>	Cash Basis
<b>3</b>	<b>Advanced against LIC/ KVP/NSC/FDs</b>	Accrual basis provided adequate margin is available.
<b>4</b>	<b>Fees/ commission on rescheduled advances</b>	Accrual basis over the period covered by rescheduled extension of credit period.
<b>5</b>	<b>Govt. guaranteed advances</b>	If overdue, income to be realized on cash basis.

## REVERSAL OF INCOME

<b>1</b>	<b>First Time NPAs</b>	Interest credited but not realized should be reversed.
<b>2</b>	<b>Commission/Other Income in respect of NPAs</b>	Recognized on accrual basis and not received yet, should be reversed
<b>3</b>	<b>Finance Charge of Leased Assets</b>	Recognised as income on accrual basis, but not yet realised should be reversed.

## VERIFICATION OF SECURITY AGAINST ADVANCES

<b>Examination Aspects</b>	<ol style="list-style-type: none"> <li>1. Execution of documents.</li> <li>2. Limitation period.</li> <li>3. Evidences as to Market Value.</li> <li>4. Evidences as to ownership of assets.</li> <li>5. Registration of charge with ROC.</li> <li>6. Regular submission of information by borrower.</li> </ol>	
<b>Special Considerations</b>	To examine whether advance is secured & extent to which it is secured, determine the following: <ol style="list-style-type: none"> <li>(a) whether the security is legally enforceable;</li> <li>(b) whether the security is in the effective control of the bank; &amp;</li> <li>(c) to what extent the value of the security, covers the loan.</li> </ol>	
<b>Examples</b>	ECGC/DICGC guarantee	Secured*
	Lower Margin	Secured*
	Cheques purchased	Unsecured
	Supply Bills	Unsecured
<b>Verification of advances made against LIC</b>	<ul style="list-style-type: none"> <li>• Inspect policies &amp; ensure policies assigned in favour of bank.</li> <li>• Examine whether premium has been paid and policy is in force.</li> <li>• Obtain Certificate regarding surrender value (SV).</li> <li>• If SV is subject to payment of premium, such premium need to be deducted from SV.</li> </ul>	
<b>Verification of Advances against Stock</b>	<ol style="list-style-type: none"> <li>1. Examine Sanction letter &amp; loan documents.</li> <li>2. Verify stock statement to ascertain quantity and value.</li> <li>3. Physically inspect the inventory.</li> <li>4. Review the stock audit report.</li> <li>5. Insurance policies assigned in favour of bank.</li> <li>6. Inspect document of title of goods.</li> </ol>	

## Verification of Provision for NPA

- Study the latest Master Circular of RBI to get familiarise with the norms prescribed by RBI in relation to provisioning requirements for NPA.
- Provisioning norms as laid down in the master circular should be construed as the minimum provisioning requirements and wherever a higher provision is warranted in the context of the threats to recovery, ensure that higher provision is made by the bank.
- Examine whether the classification made by the branch into Standard, Sub-standard, doubtful and loss assets is appropriate.
- Examine whether the secured and the unsecured portions of advances have been segregated correctly and provisions have been calculated properly.
- As per the RBI guidelines, if an account has been regularised before the balance sheet date by payment of overdue amount through genuine sources, the account need not be treated as NPA.
- Date of NPA is of significant importance to determine the classification and hence specific care be taken in this regard and ensure that the classification is made as per the position as on date and hence classification of all standard accounts be reviewed as on balance sheet date.

## Verification of Accounts falling under CDR

- (a) Review the present classification of the account under IRAC norms adopted by the bank and corresponding provision made in the books of accounts, if any.
- (b) If the account is already treated as NPA, the same cannot be upgraded only because of the CDR package.
- (c) Review the Debtor-Creditor Agreement (DCA) and Inter Creditor Agreement (ICA) with respect to availability of such agreements.
- (d) Ascertain the terms of rehabilitation along with the sacrifices, if any, to verify whether such sacrifices have been accounted in the books of accounts of the lender.
- (e) Ascertain whether any additional financing / conversion of loan into equity have been envisaged in the restructuring program.
- (f) Ascertain whether account has been referred to BIFR, as such cases are not eligible for restructuring under CDR system. Large value BIFR cases may be eligible for restructuring under CDR if specifically recommended by CDR core group.
- (g) Ensure that accounts wherein recovery suits have been filed, the initiative to resolve under CDR system is taken by at least by 75% of the creditors by value and 60% in number.

*Compiled by: CA. Pankaj Garg*

## Verification of Sale/Purchase of NPA

- A NPA in the books of a bank is eligible for sale to other banks only if it has remained a NPA for at least two years in the books of the selling bank.
- NPA can be sold only on 'without recourse' basis.
- Subsequent to sale of NPA, selling bank do not assume operational, legal or any other type of risks relating to the financial assets sold.
- NPAs can be sold to other banks only on cash basis.
- Entire sale consideration should be received upfront.
- The sale price should not be lower than NPV of estimated cash flows associated with realisable value of the available securities net of the cost of realisation.
- Purchasing bank can further sold NPA only after 15 months.

### Asset Classification Norms

- NPA purchased, may be classified as 'standard' in the books of purchasing bank for a period of 90 days from the date of purchase. Thereafter, the asset classification shall be determined on the basis of recovery.

### Provisioning Norms:

- When a bank sells its nonperforming financial assets to other banks, the same will be removed from its books on transfer.
- In the books of purchasing bank, the asset shall attract provisioning requirement appropriate to its asset classification status.

## DRAFTS PAID WITHOUT ADVICE

- (i) Examine the following:
- System of verifying genuineness of draft by reference to specimen signature of signing authority
  - System of co-relating drafts paid, with advices subsequently received;
  - System of sending reminders, if advices are not received within reasonable time and recording of reasons for their non receipt.
- (ii) Verify composition of balances appearing in this account with reference to any long outstanding items.
- (iii) Verify whether items appearing in this a/c have been subsequently cleared on receipt of relevant advices.
- (iv) Verify that the bank maintain a record of names and addresses of the payees of such drafts.

## Inter-office Adjustments (Branch Adj. Accounts)

- (a) Examine origin and validity of old outstanding unmatched entries, particularly debit entries.
- (b) Whether there are any reversal entries indicating the possibilities of irregular payments or frauds.
- (c) Examine whether the balances include any items in nature of cash-in-transit, which remain pending for more than a reasonable period.
- (d) Whether transactions, other than those relating to inter-branch have been included in inter-branch accounts.
- (e) The auditor may also seek explanations from the management for old outstanding unmatched entries and transactions other than inter branch transactions.

## CONTINGENT LIABILITIES

<b>Disclosure requirements as per 3<sup>rd</sup> Schedule</b>	(i) Claims against the bank not acknowledged as debts. (ii) Liability for partly paid investments. (iii) Liability on account of outstanding forward exchange contracts. (iv) Guarantees given on behalf of constituents- In India & Outside India. (v) Acceptances, endorsements and other obligations. (vi) Other items for which the bank is contingently liable.
<b>Verification Aspects</b>	(a) Ascertain existence of adequate internal controls to ensure that transactions giving rise to contingent liabilities are executed only by persons authorised to do so. (b) Ascertain whether the accounting system of the bank provides for maintenance of adequate records in respect of such obligations. (c) Perform substantive audit tests to establish the completeness of the recorded obligations. (d) 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. (e) Obtain representation from the management that all contingent liabilities have been disclosed. (f) Ensure Compliance of AS 29, "Provisions, contingent liabilities and contingent assets".

### Claims against the bank not acknowledged as debt

- Examine relevant evidence like correspondence with lawyers, claimants, workers/officers etc.
- Review the minutes of the meeting of the BOD, contracts, agreements, pending legal cases & correspondence relating to taxes etc., to identify claims against the bank.
- Ascertain from the management the status of claims outstanding as at the end of previous year.
- Review subsequent events to obtain evidence about completeness and valuation of claims.

### Acceptances, endorsements and other obligations

#### Letters of credit:

1. Evaluate adequacy of internal controls over LC Forms e.g. custody, records, reconciliation etc.
2. Verify the balance of LC from the Register maintained by the bank.
3. Examine the guarantees of the customers, copies of the LC issued & security obtained.

#### Other acceptances and endorsements:

- Examine arrangements made by bank with customers.
- Test check amounts of bills with the register.
- Verify whether bills are marked off in register on payment at maturity.

*Compiled by: CA. Pankaj Garg*



## STATUTORY LIQUIDITY RATIO

Central statutory auditors are required to verify the compliance of SLR on 12 odd dates in different months not having Fridays. To verify compliance with SLR requirements, the statutory auditor has to examine two aspects:

(a) Correctness of the figure of DTL at the close of business on the reporting Friday relevant to the dates selected by the auditor, and

(b) Maintenance of prescribed percentage of liquid assets on the selected date.

### STEPS OF VERIFICATION

1. Examine the composition of items of DTL as per circulars/instructions of RBI.
2. Verification of trial balance and cash balance for 12 selected dates by Branch auditors.
3. Inclusion of demand and time liabilities in Consolidated Statement based on the returns received from the unaudited branches.
4. Examine whether Net credit balance in Branch Adjustment Account has been included in liabilities.
5. In computation of liquid assets, deposits maintained with RBI, cash balance with itself or RBI, excess balance maintained with RBI, net balance in current account are all treated as cash.
6. Price of gold taken does not exceed market price.
7. Specify number of unaudited branches.

## CAPITAL ADEQUACY RATIO

**Meaning:** Measurement of adequacy of capital resources of bank in relation to risks associated with its operation.

**Requirement:** Public Sector: 9%; Private Sector: 10%

**Computation:** Capital Funds  
Risk Adjusted Assets & Off Balance Sheet Items

**Components of Capital Funds**

- Capital Funds are classified in two categories: Tier I and tier II.
- Tier I Fund includes Paid Up capital, Statutory Reserves, Free Reserves as reduced by equity investments in subsidiaries, intangible assets & current b/f losses.
- Tier II Fund includes undisclosed reserves, general provision and loss reserves, hybrid debt capital instruments and subordinated assets.
- Tier II Capital cannot exceed 100% of Tier I Capital.

## LONG FORM AUDIT REPORT (LFAR)

- LFAR has to be furnished by the auditor of a bank in addition to the audit report as per the statutory requirement.
- The matters which the banks require their auditor to deal with in the form of Long Form Audit Report have been specified by the RBI.

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## CONCURRENT AUDIT

<b>Meaning</b>	Examination which is contemporaneous with the occurrence of transactions. It attempts to shorten the interval between a transaction and its examination by an independent person not involved in its documentation. Emphasise substantive checking rather than test checking.
<b>Coverage</b>	Concurrent audit should cover the following: (a) Branches whose total credit aggregate to not less than 50% of the total credit of the bank; and (b) Branches whose aggregate deposits cover not less than 50% of the aggregate deposits of the Bank. In addition, bank should ensure the coverage of following: (a) Exceptionally large, very large and large branches; (b) Special branches handling foreign exchange business; (c) Branches rated as poor/very poor; (d) Head Office department dealing with treasury/funds management and handling investment portfolio.
<b>Scope</b>	<ol style="list-style-type: none"> <li>1. Daily cash transactions with reference to abnormal receipts and payments.</li> <li>2. Verification of procedure and documentation to open new current, savings, term deposit accounts, etc.</li> <li>3. Verification of advances, OD, CC, term loans, bills purchase, LC etc. Procedure for sanction and documentation to be verified.</li> <li>4. Verification of Foreign exchange transactions.</li> <li>5. Verification of ledgers, inter branch reconciliation &amp; verification of interest, discount, commission.</li> <li>6. Revenue leakage.</li> <li>7. Verification of high value transactions.</li> <li>8. Procedure for safe custody of security forms with the branch.</li> <li>9. Ensure adequacy of procedures for tax deduction at source.</li> <li>10. Verification of returns, statements, calculation of capital adequacy ratio and compliance with RBI Guidelines.</li> <li>11. Study of RBI and Internal Inspection reports, statutory auditor's report and compliance thereto.</li> </ol>

# Audit of General Insurance Companies

LEGAL FRAMEWORK	REGULATORY REQUIREMENTS OF INSURANCE ACT 1938 SOLVENCY MARGIN	RESERVE FOR UNEXPIRED RISKS
<ol style="list-style-type: none"> <li>1. Insurance Act, 1938</li> <li>2. IRDA Act, 1999</li> <li>3. IRDA Regulations</li> <li>4. Companies Act, 2013</li> <li>5. GIC (Nationalisation) Act, 1972</li> </ol>	<ul style="list-style-type: none"> <li>• <b>Requirement of solvency margin:</b> Every insurer and re-insurer shall at all times maintain an excess of value of assets over the amount of liabilities of, not less than 50% of the amount of minimum capital.</li> <li>• <b>Non-compliance of solvency margin:</b> Insurer or re-insurer, who does not comply with requirement of solvency margin shall be deemed to be insolvent &amp; may be wound-up by court on application made by IRDA.</li> <li>• <b>Power of authority to prescribe level of solvency:</b> The Authority shall by way of regulation made for the purpose, specify a level of solvency margin known as control level of solvency on the breach of which the Authority shall act.</li> <li>• <b>Submission of Financial Plan:</b> If, at any time, insurer or re-insurer does not maintain required control level of solvency margin, he shall, in accordance with directions issued by IRDA, submit a financial plan, indicating a plan of action to correct the deficiency within a specified period not exceeding 6 months.</li> <li>• <b>Modifications to Financial Plan:</b> If the authority considers the financial plan inadequate, it shall propose modifications to the plan and shall give directions, including direction in regard to transacting any new business, or, appointment of an administrator or both.</li> <li>• <b>Non submission of financial plan:</b> An insurer or re-insurer who does not submit financial plan shall be deemed to have made default in complying with the requirements of this section.</li> </ul>	<p>IRDA (General insurance-Claim Reserving) Regulations, 2013 requires creation of a minimum amount of unexpired risks reserve at a specified percentage of net premium as under:</p> <ul style="list-style-type: none"> <li>• For marine hull insurance – 100% of net premium</li> <li>• For fire, marine cargo and miscellaneous business – 50% of net premium.</li> </ul> <p><b>Note: Sec. 64V of Insurance Act, 1938 also specifies these percentages. Subsequent to Amendment Act of 2015, these percentages are no more specified in amended Section 64V.</b></p>

*Compiled by:*  
**CA. Pankaj Garg**

## Audit of GIC – Revenue Items

Premium Income	Claims Paid	Commission	Receipt & Payment A/c						
<ol style="list-style-type: none"> <li>1. <b>Review of Internal Control:</b> <ul style="list-style-type: none"> <li>• Issue of proper cover notes</li> <li>• Serial no. of cover notes</li> <li>• Internal check on stamps, stationary etc.</li> </ul> </li> <li>2. <b>Accounting:</b> <ul style="list-style-type: none"> <li>• Recognition of premium income for all risks incepted.</li> <li>• Proper recording for Fire, Marine, Motor &amp; Other Ins.</li> <li>• Accounting for premium received in advance &amp; premium outstanding.</li> <li>• Recording at gross figure without providing for reserve.</li> </ul> </li> <li>3. <b>Inception of Risk:</b> Sec. 64VA                             <ul style="list-style-type: none"> <li>• Issue of Policy Documents</li> <li>• No risk w.r.t. premiums received in advance and outstanding.</li> </ul> </li> <li>4. <b>Co-Insurance:</b> <ul style="list-style-type: none"> <li>• Proper booking of share of premium.</li> </ul> </li> </ol>	<ol style="list-style-type: none"> <li>1. <b>Review of Internal Control:</b> <ul style="list-style-type: none"> <li>• Payment of only bonafide claims.</li> <li>• Sanctioned by appropriate authority.</li> <li>• Collection of information from branches.</li> </ul> </li> <li>2. <b>Claims Paid:</b> <ul style="list-style-type: none"> <li>• <b>Coinsurance:</b> Proper booking</li> <li>• <b>Settlement Amount:</b> must include all incidental expenses</li> <li>• <b>Claims communicated after year end:</b> accounting for provisions</li> <li>• <b>Accounting for Salvage and letter of subrogation:</b> in accordance with procedure.</li> <li>• <b>Amount deposits with Court:</b> not treated as claim till final decision.</li> <li>• <b>Unqualified Discharge Note:</b> in case of final settlement.</li> </ul> </li> <li>3. <b>Claims Outstanding at year end:</b> <ul style="list-style-type: none"> <li>• Provision for all unsettled Claims.</li> <li>• Provision for legally enforceable claims.</li> <li>• Provisions should not be made in excess.</li> <li>• Application of Average Clause.</li> <li>• Consideration of salvage value.</li> </ul> </li> <li>4. <b>Claims Register:</b> <table border="1" style="width: 100%; border-collapse: collapse; margin-top: 5px;"> <tr> <td style="width: 33%;">Claims Intimation Register</td> <td style="width: 33%;">Claims Paid Register</td> <td style="width: 33%;">Salvage Register</td> </tr> <tr> <td>Claim Dockets</td> <td>Report of Quality Assurance Team</td> <td>Claims Disbursement Book</td> </tr> </table> </li> </ol>	Claims Intimation Register	Claims Paid Register	Salvage Register	Claim Dockets	Report of Quality Assurance Team	Claims Disbursement Book	<ol style="list-style-type: none"> <li>1. Vouching of disbursement entries.</li> <li>2. Proper Authorisation of disbursements.</li> <li>3. Calculation of commission.</li> <li>4. Examination of agent's ledger.</li> <li>5. Examine accounting of commission paid.</li> </ol>	<p>Sec. 11 of Insurance Act, 1938 – F.S. to include Receipt and Payment Account (R &amp; P ).</p> <p><b>Auditor Duties:</b></p> <ul style="list-style-type: none"> <li>• report whether the R &amp; P account of the insurer is in agreement with the books of account and returns;</li> <li>• express an opinion as to whether the R &amp; P account has been prepared in accordance with the provisions of the relevant statutes; and</li> <li>• express an opinion whether the R &amp; P account give a true and fair view of the receipts and payments of the insurer.</li> </ul>
Claims Intimation Register	Claims Paid Register	Salvage Register							
Claim Dockets	Report of Quality Assurance Team	Claims Disbursement Book							

## Audit of GIC – Balance Sheet Items

2

Investments	Outstanding Premium	Contingent Liabilities – Disclosure Requirements
<ol style="list-style-type: none"> <li>1. Physically verify the securities on the balance sheet date or a date as near as possible. Prepare a reconciliation statement where verification is carried out on date other than BS date.</li> <li>2. Obtain separate lists of securities held physically and those held in demat form.</li> <li>3. Examine the records for investments held at branches and request the respective branch auditors to issue a certificate to this effect.</li> <li>4. Examine in detail investments on which income has not been received for a long period and those which have not been redeemed even after redemption date.</li> <li>5. Where certificates are held by other persons such as nominees, share transfer agents etc. the auditor should obtain written certificates from such person.</li> <li>6. Examine that norms relating to valuation and disclosure in F.S. have been complied with.</li> <li>7. Examine whether income from investments is properly accounted for</li> <li>8. Ensure that certificates of TDS are properly maintained.</li> <li>9. Ensure compliance of Sections 27, 27A and 27B of the Insurance Act, 1938 as well as the guidelines issued from time to time by the Ministry of Finance through GIC.</li> </ol>	<ol style="list-style-type: none"> <li>1. Scrutinize and review control account debit balances and their nature should be enquired into.</li> <li>2. Examine in-operative balances and treatment given for old balances with reference to company rules.</li> <li>3. Enquire into the reasons for retaining the old balances.</li> <li>4. Verify old debit balances which may require provision or adjustment. Notes of explanation may be obtained from the management in this regard.</li> <li>5. Check age-wise, sector-wise analysis of outstanding premium.</li> <li>6. Verify whether outstanding premiums have since been collected.</li> <li>7. Check the availability of adequate bank guarantee or premium deposit for outstanding premium.</li> </ol>	<ol style="list-style-type: none"> <li>1. Partly paid up investments.</li> <li>2. Underwriting Commitments outstanding.</li> <li>3. Claims, other than those under policies, not acknowledged as debts.</li> <li>4. Guarantees given by or on behalf of the Company.</li> <li>5. Statutory demands / Liabilities in dispute, not provided for.</li> <li>6. Reinsurance obligations to the extent not provided for in the accounts.</li> <li>7. Others (to be specified).</li> </ol>

## Audit of GIC - Miscellaneous

Co-Insurance	Trade Credit Insurance
<p><b>Meaning &amp; Concept:</b> Sharing of Business between more than one insurer at agreed percentages is known as co-insurance. The Lead Insurer issues documents, collects premium and settles claims. Statement of accounts is rendered by the Lead insurer to the other co-insurers.</p> <p><b>Incoming Co-Insurance</b></p> <ol style="list-style-type: none"> <li>1. Ensure that the Premium Account is credited on the basis of statements received from the Lead insurer.</li> <li>2. In case, the statement is not received, the premium is accounted for on the basis of advices to ensure that all premium in respect of risks assumed in any year is booked in the same year.</li> <li>3. For this purpose, the auditor may examine the communication in the post-audit period and obtain a written confirmation to the effect that all incoming advices have been accounted for.</li> <li>4. The auditor should also verify claims provisions and claims paid with reference to advice received from the Lead insurer.</li> </ol> <p><b>Outgoing Co-Insurance</b></p> <ol style="list-style-type: none"> <li>1. The auditor should scrutinise the transactions relating to the outgoing business, i.e. where the company is the Lead Insurer.</li> <li>2. These should be checked with reference to the relevant risks assumed under policies and correspondingly for debits arising to the co-insurer on account of their share of claims.</li> </ol>	<p>Trade Credit insurance provides protection to suppliers against the risk of non-payment of goods or services by their buyers who may be situated in the same country (domestic risk) or in another country (export risk) against non -payment as a result of insolvency of the buyer or non-payment after an agreed number of months after due date. Trade credit insurance product is offered subject to following requirements:</p> <ol style="list-style-type: none"> <li>1. Policyholder's loss arises due to non-receipt of trade receivable..</li> <li>2. Policyholder is a supplier of goods or services for a consideration.</li> <li>3. Buyer is liable to pay a trade receivable to the policyholder in return for the goods and services received by him from the policyholder.</li> <li>4. Premium for the entire Policy Period has been paid.</li> <li>5. Other requirement that may be specified by the Authority from time to time.</li> </ol>

## Verification of reinsurance inward

1. Evaluate internal control system in the area of reinsurance accepted to ensure determination of correct amount for reinsurance accepted, proper valuation of assets and liabilities arising out of reinsurance transaction and adherence to legal provisions and regulations.
2. Ascertain whether adequate guidelines and procedures are established with respect to granting reinsurance.
3. Reconcile reinsurance underwriting returns received from various units with the figures of premium, claims paid and outstanding claims for the company as a whole.
4. Examine whether premium received and commission paid on reinsurance accepted is as per the terms of the agreement with the Principal Insurer.
5. Examine whether claims paid have been accounted on a regular basis.
6. Examine whether remittances from foreign Principal Insurer are as per foreign exchange regulations.
7. Examine whether confirmations have been obtained regarding balances with Principal Insurer.
8. Review individual accounts of Principal Insurers.

## Verification of reinsurance outward

1. Evaluate internal control system in the area of reinsurance ceded to ensure determination of correct amount for reinsurance ceded, proper valuation of assets and liabilities arising out of reinsurance transaction and adherence to legal provisions and regulations.
2. Ascertain whether adequate guidelines and procedures are established with respect to obtaining reinsurance.
3. Reconcile reinsurance underwriting returns received from various units with the figures of premium, claims paid and outstanding claims for the company as a whole.
4. Examine whether commission on reinsurance ceded is as per the terms of the agreement with the re-insurers.
5. Examine the computation of profit commission for automatic treaty arrangements in the light of the periodic accounts rendered and in relation to outstanding loss pertaining to the treaty.
6. Examine whether loss recoveries have been claimed and accounted on a regular basis.
7. Examine whether outstanding losses recoverable have been confirmed by re-insurers.
8. Examine whether remittances to foreign re-insurers are as per foreign exchange regulations.
9. Examine whether confirmations have been obtained regarding balances with re-insurers.
10. Review individual accounts of re-insurers to evaluate whether any provision/write off or write back is required.

## Facultative and Treat Reinsurance

<b>Facultative</b>	Reinsurance whereby contract relates to one particular risk and is expressed in the reinsurance policy. Each transaction has to be negotiated individually. The Insurance is used when: <ul style="list-style-type: none"> <li>Automatic cover has exhausted.</li> <li>Risk is excluded from treaties</li> <li>Reinsurance treaties have not to be over burdened.</li> <li>Insurer has no automatic cover.</li> <li>Technical guidance is required at each stage of acceptance of risk.</li> </ul>
<b>Treaty</b>	A treaty type of coverage is in effect for a specified period of time, rather than on a per risk, or contract basis. For the duration of the contract, the reinsurer agrees to cover all or a portion of the risks that may be incurred by the insurance company being covered.
<b>Proportional Treaty</b>	<ul style="list-style-type: none"> <li>The reinsurer will receive a prorated share of the premiums of all the policies sold by the insurance company being covered. Consequently, when claims are made, the reinsurer will also bear a portion of the losses. The proportion of the premiums and losses that will be shared by the reinsurer will be based on an agreed percentage.</li> <li>In a proportional coverage, the reinsurance company will also reimburse the insurance company for all processing, business acquisition and writing costs.</li> </ul>
<b>Non Proportional Treaty</b>	<ul style="list-style-type: none"> <li>The reinsurer will only get involved if the insurance company's losses exceed a specified amount, which is referred to as priority or retention limit. Hence, the reinsurer does not have a proportional share in the premiums and losses of the insurance provider.</li> <li>The priority or retention limit may be based on a single type of risk or an entire business category.</li> </ul>

*Compiled by: CA. Pankaj Garg*

# Audit of NBFC – Basics

## TYPES OF NBFC

- (a) **Asset Finance Company:**
  - Hire Purchase Finance Company
  - Equipment Leasing Finance Companies.
- (b) **Investment company.**
- (c) **Loan Company.**
- (d) **Infrastructure Finance Company.**
- (e) **Core Investment Company.**
- (f) **Infrastructure debt Fund-NBFC.**
- (g) **NBFC-Micro Finance Institution.**

### INFRASTRUCTURE FINANCE COMPANIES

Non deposit taking NBFC that fulfills criteria mentioned below:

- (i) Min. 75% of total assets deployed in infrastructure loans;
- (ii) Net owned funds of Rs. 300 crore or above;
- (iii) Min. credit rating 'A' or equivalent of CRISIL, FITCH, CARE, ICRA or equivalent rating;
- (iv) Capital to Risk Asset Ratio (CRAR) of 15%.

### CORE INVESTMENT COMPANIES

NBFC carrying on the business of acquisition of shares and securities which satisfies the following conditions:

- (a) Min. 90% of total assets is in form of investment in equity shares, preference shares, debt or loans in group companies;
- (b) Investments in equity shares in group companies constitutes not less than 60% of its total assets;
- (c) No trading in shares, debt or loans in group companies except through block sale for disinvestment;
- (d) It does not carry on any other financial activity except investment in bank deposits, money market instruments, govt securities, loans & investments in debt issuances of group companies.

## ASPECTS OF AUDIT PROCEDURE

<b>Ascertain the business of NBFC</b>	<p>Study the following:</p> <ul style="list-style-type: none"> <li>• MOA &amp; AOA</li> <li>• Business Policies</li> <li>• Minutes of Board / Committee meetings</li> </ul>
<b>Evaluation of I.C. System</b>	<ul style="list-style-type: none"> <li>• To examine whether I.C. exist, effective and continued.</li> <li>• Review the effectiveness of system of recovery and periodical review of advances.</li> </ul>
<b>Regn. with RBI</b>	Obtain a copy of certificate of registration granted by the RBI
<b>Public deposit Directions</b>	<ol style="list-style-type: none"> <li>1. <b>Credit Rating:</b> Obtain a copy of credit rating assigned to NBFC.</li> <li>2. <b>Interest and Brokerage payments:</b> to ensure that it is not paid in excess.</li> <li>3. <b>Written application:</b> ensure that deposits has accepted with written application.</li> <li>4. <b>Deposit register:</b> Examine that correct particulars entered in the register.</li> <li>5. <b>Repayment of deposits:</b> Examine - regular repayment of deposits on due date.</li> <li>6. <b>Custody of investments:</b> Obtain certificate that investments are kept in safe custody.</li> <li>7. <b>Submission of accounts:</b> Audited accounts, F.S. &amp; Auditor's report submitted on time.</li> <li>8. <b>Filing of annual return:</b> Annual Return is filed in specified time.</li> <li>9. <b>Board Resolution in case of non-acceptance of deposits.</b></li> </ol>
<b>Prudential Norms</b>	<ol style="list-style-type: none"> <li>1. Verification of compliance of prudential norms w.r.t.                             <ul style="list-style-type: none"> <li>• Income recognition</li> <li>• Income from investments</li> <li>• Asset classification</li> <li>• Capital Adequacy norms</li> <li>• Granting loan against own shares</li> <li>• Norms for concentration of credit</li> </ul> </li> <li>2. Policy for granting Demand loans: has been framed by BOD.</li> <li>3. Classification of advances: has been made in accordance with the directions.</li> <li>4. Income from NPA: Ensure that income from NPA has not been recognized.</li> <li>5. Recovery from NPA: Check the recovery made in the NPAs account.</li> </ol>

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# Audit of NBFC - Check List

Equipment Leasing Finance Co.	Hire Purchase Company	Loan Company	Investment Company
<p>(i) <b>Credit appraisal System:</b> Ascertain whether the NBFC has an adequate appraisal system for extending equipment leasing finance.</p> <p>(ii) <b>Physical verification:</b> Verify existence of adequate system to ensure installation of assets and their periodic physical verification.</p> <p>(iii) <b>Maintenance of assets:</b> Ascertain whether the NBFC has an adequate system for monitoring whether the assets have been adequately insured against and regular maintenance of the leased assets is being carried out by the lessee.</p> <p>(iv) <b>Verification of Lease Agreement:</b> Verify the lease agreement entered into with the lessee to ascertain the terms &amp; conditions.</p> <p>(v) <b>Compliance of AS-19:</b> Verify whether the AS 19 issued by the ICAI in respect of "Leases" has been complied with.</p>	<p>(i) <b>Credit Appraisal System:</b> Ascertain existence of an adequate appraisal system for hire-purchase finance.</p> <p>(ii) <b>Verifications of Payments:</b> Verify that payments for assets are made directly to vendor and assets are property charged in name of NBFC.</p> <p>(iii) <b>Physical Verification:</b> Ascertain the adequacy of system in place to ensure installation of the asset and their periodic physical verification.</p> <p>(iv) <b>Verification of Endorsement:</b> If the finance is against vehicles, the registration certificate should contain an endorsement in favor of the NBFC.</p> <p>(v) <b>Regularity of HP Installments:</b> Check whether installments are received regularly. In case of any overdue, examine whether adequate provision has been made.</p> <p>(vi) <b>Insurance of Asset:</b> The auditor should verify that hire purchase assets are adequately insured.</p> <p>(vii) <b>Valuation aspects:</b> Ensure that goods sold on hire purchase &amp; goods repossessed valued properly.</p> <p>(viii) <b>Recognition of finance charges:</b> Examine the method of accounting followed for appropriation of finance charges over the period of contract.</p>	<p>(i) <b>Sanctioning:</b> Examine whether loan or advance has been properly sanctioned.</p> <p>(ii) <b>Security:</b> Verify the security obtained and the agreements entered into, if any.</p> <p>(iii) <b>Balance Confirmations:</b> Obtain balance confirmations from the concerned parties.</p> <p>(iv) <b>Maintenance of Records in case of bills discounting:</b> Verify that proper records have been maintained.</p> <p>(v) <b>Ceiling Limits:</b> Ensure that NBFC has not lent in excess of the specified limits.</p> <p>(vi) <b>Loans against own shares:</b> Ensure NBFC has not advanced any loans against the security of its own shares.</p> <p>(vii) <b>Monitoring and follow up:</b> Verify existence an adequate system of appraisal and follow up of loans and advances.</p> <p>(viii) <b>Compliance of prudential norms:</b> Ensure classification of loans and advances into Standard, Sub-Standard, doubtful and loss assets and the provision for bad and doubtful debts are being made as per NBFC Prudential Norms Directions.</p>	<p>(i) <b>Physical Verification:</b> of all the shares and securities held by a NBFC.</p> <p>(ii) <b>Compliance with Prudential Norms:</b> NBFC Prudential Norms are:</p> <ul style="list-style-type: none"> <li>• <b>Lending:</b> ≤ 15% of its owned funds to any single borrower and ≤ 25% to any single group of borrower.</li> <li>• <b>Investment:</b> ≤ 15% of owned funds in a single entity and ≤ 25% of owned funds in a single group of entities.</li> <li>• <b>Lending and Investment:</b> ≤ 25% of owned funds in a single entity &amp; ≤ 40% of owned funds in a single group.</li> </ul> <p>(iii) <b>Income from Investments:</b> NBFC prudential norm requires dividend on shares of companies &amp; units of mutual funds to be recognised on cash basis.</p> <p>(iv) <b>Classification of investments:</b> into current or long term investments.</p> <p>(v) <b>Valuation of Investments:</b> in accordance with NBFC Prudential Norms. Ensure compliance of AS 13 (to the extent they are not inconsistent with the directions).</p> <p>(vi) <b>Investment in group companies:</b> Obtain a list of subsidiary/group companies from the management and verify.</p> <p>(vii) Obtain a confirmation from third parties where the investments are kept deposited with them.</p>

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# Audit of NBFC – NBFC Auditor’s Report (Reserve Bank) Directions, 2008

	<b>All NBFC</b>	<ol style="list-style-type: none"> <li>1. Whether the companies engaged in business of non-banking financial institution has obtained a Certificate of Registration (CoR) from the Bank (RBI).</li> <li>2. Whether company is entitled to continue to hold CoR in terms of its asset/income pattern.</li> </ol>
<b>Para 3</b>	<b>NBFC accepting Public Deposits</b>	<ol style="list-style-type: none"> <li>1. Whether public deposits accepted by the company are within the limits as per NBFC Acceptance of Public Deposits (Reserve Bank) Directions, 1998;</li> <li>2. Whether the public deposits held in excess of permissible amount are regularised.</li> <li>3. Whether an Asset Finance Company having Capital to Risk Assets Ratio (CRAR) less than 15%.</li> <li>4. Whether the NBFC is accepting "public deposit" without credit rating from approved agency;</li> <li>5. In respect of Asset Finance Company, whether the credit rating, for each of the fixed deposits schemes that has been assigned by Credit Rating Agencies (a) is in force; and (b) whether the aggregate amount of deposits outstanding as at any point during the year has exceeded the limit specified by Credit Rating Agency;</li> <li>6. In case of NBFCs having Net Owned Funds of Rs. 25 lakh and above but less than Rs. 200 lakhs, whether the public deposit held by the companies is in excess of the quantum of such deposit permissible.</li> <li>7. Whether the company has defaulted in paying to its depositors the interest and /or principal amount of the deposits after such interest and/or principal became due;</li> <li>8. Whether the company has complied with the prudential norms on income recognition, asset classification, provisioning for bad and doubtful debts, and concentration of credit/investments.</li> <li>9. Whether the capital adequacy ratio as disclosed in the return submitted to the Bank has been correctly determined.</li> <li>10. Whether the company has complied with the liquid assets requirement as prescribed.</li> <li>11. Whether the company has furnished to the Bank within the stipulated period the return on deposits.</li> <li>12. Whether the company has furnished to the Bank within the stipulated period the half-yearly return on prudential norms.</li> <li>13. Whether, in the case of opening of new branches or offices to collect deposits or in the case of closure of existing branches/offices or in the case of appointment of agent, the company has complied with the requirements.</li> </ol>
	<b>NBFC not accepting public deposits</b>	<ol style="list-style-type: none"> <li>1. Whether the BOD has passed a resolution for non- acceptance of any public deposits.</li> <li>2. Whether the company has accepted any public deposits during the relevant period/year;</li> <li>3. Whether the company has complied with the prudential norms relating to income recognition, asset classification and provisioning for bad and doubtful debts.</li> <li>4. In respect of Systemically Important Non-deposit taking NBFCs:                         <ol style="list-style-type: none"> <li>(a) whether the capital adequacy ratio as disclosed in the return submitted to the Bank, has been correctly arrived at; and</li> <li>(b) whether the company has furnished to the Bank the annual statement of capital funds, risk asset ratio within the stipulated period.</li> </ol> </li> </ol>
<b>Para 4</b>	<b>Reasons to be stated for unfavorable or qualified statements</b>	<ul style="list-style-type: none"> <li>• Where, in the auditor’s report, the statement regarding any of the items referred to in paragraph 3 above is unfavourable or qualified, the auditor’s report shall also state the reasons for such unfavourable or qualified statement, as the case may be.</li> <li>• Where the auditor is unable to express any opinion on any of the items referred to in paragraph 3 above, his report shall indicate such fact together with reasons therefore.</li> </ul>
<b>Para 5</b>	<b>Exception Report</b>	<p>Where, in the case of a NBFC, the statement regarding any of the items referred to in Para 3, is unfavourable or qualified, or in the opinion of the auditor the company has not complied with:</p> <p>(a) the provisions of Chapter III B of Reserve Bank of India Act, 1934; or</p> <p>(b) the NBFC Acceptance of Public Deposits (Reserve Bank) Directions, 1998; or</p> <p>(c) Non-Banking Financial (Deposit Accepting or Holding) Companies Prudential Norms (RBI) Directions, 2007; or</p> <p>(d) Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (RBI) Directions, 2007;</p> <p>it shall be the obligation of auditor to make a report containing details of such unfavourable/qualified statements and non-compliance in respect of the company to the concerned Regional Office of the Department of Non-Banking Supervision of the Bank under whose jurisdiction the registered office of the company is located.</p>

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