

Ans.



- (i) **Provision:-** Section 139(8) of the Companies Act, 2013 provides that any **casual vacancy** in the office of an auditor **shall be filled** by the **Board of Directors within 30 days**.
- However, if such casual vacancy is as a **result of the resignation** of an auditor, such appointment shall **also be approved by the company** at a general meeting convened **within 3 months** of the recommendation of the Board and **he shall hold the office** till the conclusion of the **next annual general meeting**.
- (ii) **In the present case:-** Mr. X had been **validly appointed** and thereafter he had **resigned**. Consequently, the **casual vacancy** has been created on account of resignation.
- (iii) **Conclusion:-** Therefore, the Board of Directors will have to **fill the vacancy within 30 days** and such appointment shall be **approved by the company** at the general meeting **within 3 months** of the recommendations of the board. The new auditor so appointed **shall hold office** only till the conclusion of the **next AGM**.

16.

**Sec 139(10) - Board of Directors power to Fill the Vacancy**

C.A. Ashwin was appointed as auditor of Bristol Ltd. for the year 2021-22. Since he declined to accept the appointment, the Board of Directors appointed C.A. John as the Auditor in place of C.A. Ashwin and the appointment was accepted by C.A. John. Discuss in light of Companies Act, 2013 and Chartered Accountant Act, 1949. (May-2015)

Ans.



- (i) **As per provisions of Companies Act-2013:**  
**Board of Directors** of the company has been **empowered to appoint the auditor other than first auditor** in the following cases:
- **Section 139(2)** – Appointment of auditor is not ratified by the members of the company in AGM.
  - **Section 139(8)** – Any casual vacancy arises in the office of auditor.
  - The present case does not fall under any of the circumstances; hence **BOD does not have power to fill up the vacancy**.
  - Under the circumstances, **it may be deemed that no auditor appointed at AGM** and provisions of **Section 139(10)** may be invoked which provides that where at any AGM, no auditor is appointed or re-appointed, the **existing auditor shall continue** to be the auditor of the company.
- (ii) **As per Clause (9) of Part I of the First Schedule to the Chartered Accountants Act, 1949**  
 A member in practice shall be **deemed to be guilty of professional misconduct** if he:
- **Accepts an appointment** as auditor of a company **without first ascertaining** from it whether the requirements of **Section 139 and 140** read with **Section 141 of the Companies Act, 2013**, in respect of such appointment have been duly complied with.
- (iii) **In the present case:-** CA Ashwin was appointed as an auditor of **Bristol Ltd.**, however he **declined to accept the appointment**. Resulting to such decline, the **board appointed CA. John** as an auditor and such appointment was **accepted by him**.
- (iv) **Conclusion:-** Board of Directors are **not authorised to fill up the vacancy** in case the auditors appointed at the AGM refuse to accept the appointment. Accordingly, **C.A. John is guilty of professional misconduct as per Clause (9) of Part I of the First Schedule**, as he accepted the appointment without verification of statutory requirements.

17.

**Validity of Appointment**

What are the steps to be taken by a firm of Chartered Accountant to ensure that its appointment as Statutory Auditor of a Company is valid?

Ans.



- Validity of Appointment as a Statutory Auditor:** To ensure that the appointment is valid, the incoming auditor should take the following steps before accepting his appointment: (CRC2)
- (i) **Ceiling limit:** Ensure that a **certificate has been issued under section 139** of the Companies Act, 2013 so that the **total number of company audits** held by the firm (including the new appointment) **will not exceed** the specified number.

- (ii) **Resolution at AGM:** Verify that at AGM of the Company, a **proper resolution is passed**. Inspect general meeting **minutes book** to see that the appointment is duly recorded.
- (iii) **Compliance with law:** Satisfy that the legal procedure contemplated in **section 139 and 140** of the said Act, dealing with the **appointment and removal** of existing auditor, **have been followed**.
- (iv) **Code of conduct:** **Communicate** with the **previous auditor**, if any, **in writing**, to ascertain if there are any **professional reasons** for **not accepting** the appointment.

**18. Re- appointment**  
 Under what circumstances the **retiring auditor cannot be reappointed?** **(Jan-2021-Old)**

**Ans.**



**Circumstances where Retiring Auditor cannot be Reappointed:** In the following circumstances, the retiring auditor cannot be reappointed-

- (i) A **specific resolution** has not been passed to **reappoint the retiring auditor**.
- (ii) The **auditor proposed** to be reappointed **does not possess the qualification** prescribed under section 141 of the Companies Act, 2013.
- (iii) The proposed auditor **suffers from the disqualifications** under section 141(3), 141(4) and 144 of the Companies Act, 2013.
- (iv) He has given to the company **notice in writing of his unwillingness** to be reappointed.
- (v) **A resolution has been passed in AGM** appointing somebody else or providing expressly that the retiring auditor shall not be reappointed.
- (vi) **A written certificate has not been obtained** from the proposed auditor to the effect that the appointment or reappointment, if made, will be in accordance within the limits specified under **section 141(3)(g)** of the Companies Act, 2013.

#### 5.2 - Section-140 Removal & Resignation of Auditor

**19. Removal of First Auditor**  
 A, B & C Company Ltd. removed its first auditor before the expiry of his term without obtaining approval of the Central Government. Comment

**Ans.**



- (i) **Provision: As per Section 140(1)** of the Companies Act, 2013, an **auditor appointed** under section 139 may be **removed** from his office **before the expiry of his term** only by :
  - A **special resolution** of the company,
  - After obtaining the **prior approval** of the **Central Government**
- (ii) **As per Rule 7 prescribed under Companies (Audit & Auditors) Rules, 2014:-**
  - The application to the Central Government **for removal of auditor** shall be made in **Form ADT-2** and shall be **accompanied with fees as provided** for this purpose under the Companies (Registration Offices and Fees) Rules, 2014.
  - The application shall be made to the **Central Government within 30 days** of the resolution passed by the Board.
  - The company shall hold the **general meeting within 60 days of receipt of approval** of the Central Government for passing the special resolution. (For **IFSC company** if no decision given by **CG within 60 days** of submission of application then deemed that **approval has been given**)

It is important to note that before taking any action for removal before expiry of terms, the auditor concerned shall be given a **reasonable opportunity of being heard**.
- (iii) **In the instant case:-** The first auditor was **removed by the company before the expiry of his term without obtaining approval** of the Central Government in spite of the Special resolution as per the requirement of section 140(1) along with the prior approval of the Central Government in that behalf.
- (iv) **Conclusion:-** it may be concluded that the **action of the company for removal of the auditor before expiry of term is not justified** and auditor may be removed from his office only by following the above mentioned procedure.

20.

**Permission of Central Government for Removal of Auditor**

Why Central Government permission is required, when the auditors are to be removed before expiry of their term, but the same is not needed when the auditors are changed after expiry of their term?

Ans.


**(i) Provision:- As per Section 140(1) of Companies Act, 2013**

- **Removal of auditor before expiry of his term** i.e. before he has submitted his report is a **serious matter** and **may adversely affect his independence**. Further, in case of **conflict of interest** the shareholders may remove the auditors in their own interest.
- Therefore, **law has provided this safeguard** so that central government may **know the reasons** for such an action and **if not satisfied**, may not accord approval.
- **On the other hand if auditor has completed his term** i.e. has submitted his report and thereafter he is not re-appointed then the matter is not serious enough for central government to call for its intervention.

**(ii) Conclusion:-** In view of the above, **the permission of the Central Government is required** when auditors are removed before expiry of their term and **the same is not needed** when they are not re-appointed after expiry of their term.

21.

**Sec. 140 - Appointment of Sole Auditor**

M/s. PQR, audit firm has been re-appointed as sole statutory auditor of a listed company in the AGM, where till last year M/s. LMN, audit firm was also one of the joint auditors along with M/s. PQR. One tenure of consecutive five years of both the firms get completed in the mentioned AGM. Mention the steps that should be taken by M/s. PQR before commencing the audit. **(RTP-Nov-2015)**

**OR**

You have been appointed the sole auditor of a company where you were one of the joint auditors for the immediately preceding year and the said joint auditors is not re-appointed.

Ans.



When one of the joint auditors of the previous years is **considered for reappointment** by the members as the **sole auditor** for the next year, it is **similar to non-re-appointment** of one of the retiring joint auditors.

**(i) Provision:-** As per **Section 140(4)** of the Companies Act, 2013, **special notice** shall be required for a resolution at an **annual general meeting** appointing as auditor a **person other than a retiring auditor**, or providing expressly that a **retiring auditor shall not be re-appointed**.

**(ii) Exception:-** **Except where** the retiring auditor has completed a **consecutive tenure of five years or ten years**, as the case may be, as provided u/s 139(2)

**(iii) Steps to comply:-** Accordingly, provisions of the Companies Act, 2013 to be complied with areas under:

- **Special Notice:-** Ascertain that special notice **u/s 140(4)** of the Companies Act, 2013 was **received by the company** from such number of members **holding not less than one percent of total voting power** or **holding shares on which an aggregate sum of not less than ₹ 5 lakh** has been paid up on the date of the notice not earlier than **3 months** but **at least 14 days before** the AGM date.
- **Sending copy of notice:-** Check whether the said notice has been sent to all the members **at least 7 days before** the date of the AGM.
- **Contents of Notice:-** Verify the notice contains an **express intention of a member** for proposing the resolution for **appointing a sole auditor** in place of both the joint auditors who retire at the meeting but are **eligible for re-appointment**.
- **Notice to Auditor:-** The notice is **also sent to the retiring auditor** as per Section 140(4)(ii) of the Companies Act, 2013.
- **Sending the Representation:-** Verify whether any representation, received from the retiring auditor was **sent to the members** of the company.
- **Consideration of representation:-** Verify from the **minutes book** whether the representation received from the retiring joint auditor was **considered at the AGM**.

22.

**Power of Tribunal in case Auditor acted in a Fraudulent Manner**

Vivan Ltd is a company engaged in the business of software development. It is one of the largest companies in this sector with a turnover of INR 25,000 crores. The operations of the company are increasing constantly, however, the focus of the management is more on cost cutting in the coming years to improve its profitability. In respect of the financial statements of the company which are used by various stakeholders, some fraud was observed in respect of assets reported therein due to which those stakeholders suffered damages. As a result, those stakeholders applied to Tribunal for change of auditor on the basis that auditor is colluded in the fraud.

Elucidate the power of Tribunal to change the auditor of a company if found acting in a fraudulent manner as provided under sub-section (5) of section 140 of the Companies Act, 2013.

(MTP-Nov-2019, RTP-Nov-2019, Nov-2019-Old)

Ans.



- (i) **Provision:-Section 140(5) of the Companies Act, 2013**, the Tribunal **either suo motu** or on an **application made to it** by the **Central Government** or by **any person concerned**, if it is satisfied that the **auditor** of a company has, whether **directly or indirectly**, acted in a **fraudulent manner** or abetted or colluded in any fraud by, or in relation to, the **company or its directors or officers**, it may, by order, direct the company to change its auditors.
- (ii) **When application made by CG:-** if the application is made by the **Central Government** and the **Tribunal is satisfied that any change of the auditor is required**, it shall within **fifteen days of receipt** of such application, make an order that he shall **not function as an auditor** and the Central Government may appoint another auditor in his place.
- (iii) **When final order passed:-** It may be noted that an auditor, **whether individual or firm**, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of any company **for a period of five years** from the date of passing of the order and the auditor shall also be liable for action under **section 447 of the said Act**.
- (iv) **In case of Firm:-** It is hereby clarified that **in the case of a firm**, the liability shall be of the **firm** and that of **every partner or partners who acted in a fraudulent manner** or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

23.

**Power of Tribunal in case Auditor acted in a Fraudulent Manner**

Direction by Tribunal in case auditor acted in a fraudulent manner.

(RTP-May-2021)(May-2018-Old)

OR

The Auditor of M/s Quick Limited succumbed to the pressure of the management in certifying the financials with an over stated figure of turnover by not adhering to the cut-off principles of the time scale for the transactions of the year. On taking cognizance of this act of the auditor, the Tribunal under the Companies Act, 2013 initiated the proceedings against him. Briefly list the powers of the Tribunal in this respect including those relating to making orders against the Auditor found to be guilty.

(May-2018-New)

OR

Elucidate the power of Tribunal to change the auditor of a company if found acted in a fraudulent manner as provided under section 140(5) of the Companies Act, 2013.

(RTP-May-2017, MTP-May-2018)

Ans.



- (i) **Provision:-Section 140(5) of the Companies Act, 2013**, the Tribunal **either -**
- **suo-motu** or
  - on an **application made to it** by the **Central Government** or
  - by **any person concerned**,
- if it is satisfied that the **auditor** of a company has, whether **directly or indirectly**, acted in a **fraudulent manner** or abetted or colluded in any fraud by, or in relation to, the **company or its directors or officers**, it may, by order, direct the company to change its auditors.
- (ii) **When application made by CG:-** if the application is made by the **Central Government** and the **Tribunal is satisfied that any change of the auditor is required**, it shall within **fifteen days of receipt** of such application, make an order that he shall **not function as an auditor** and the Central Government may appoint another auditor in his place.

- (iii) **When final order passed:-** It may be noted that an auditor, **whether individual or firm**, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of any company **for a period of five years** from the date of passing of the order and the auditor shall also be liable for action under **section 447 of the said Act**.
- (iv) **In case of Firm :-** It is hereby clarified that **in the case of a firm**, the **liability shall be** of the **firm** and that of **every partner or partners who acted in a fraudulent manner** or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

### 5.3 - Section-141 Qualification & Disqualification of Auditor

24.

#### Disqualifications of an Auditor

Mr. Ajay, a Chartered Accountant has been appointed as an auditor of Bharat Ltd. in the Annual General Meeting of the company held in September, 2021, which assignment he accepted. Subsequently in February, 2022, he joined Mr. Bajaj, another Chartered Accountant, who is the Manager Finance of Bharat Ltd., as partner. Comment. (Study Material)

OR

A, a chartered accountant has been appointed as auditor of Laxman Ltd. in the Annual General Meeting of the company held in September, 2021, which assignment he accepted. Subsequently in January, 2022 he joined B, another chartered accountant, who is the Manager Finance of Laxman Ltd., as partner. Comment.

Ans.



- (i) **Provision:- Section 141(3)(c)** of the Companies Act, 2013 prescribes that
- **Any person who is a partner or**
  - **In employment of an officer or employee of the company** will be disqualified to act as an auditor of a company.
  - **Section 141(4)** provides that an auditor who **incurs any of the disqualifications** mentioned in **section 141(3)** after his appointment, **he shall vacate his office** as such auditor.
- (ii) **In the present case:-** Mr. Ajay, an auditor of Bharat Ltd., joined as partner with Mr. Bajaj, who is **Manager Finance of Bharat Limited**
- (iii) **Conclusion:-** He has attracted **Section 141(3)** and, therefore, he shall be deemed to have vacated office of the auditor of Bharat Limited. [Specific mention of S. 141(3)(c) should be given]

25.

#### Auditor Holding Securities of a Company

Ram and Hanuman Associates, Chartered Accountants in practice have been appointed as Statutory Auditor of Krishna Ltd. for the accounting year 2014-2015. Mr. Hanuman, a partner of the Ram and Hanuman Associates, holds 100 equity shares of Shiva Ltd., a subsidiary company of Krishna Ltd. Comment.

(Study Material, RTP-Nov-2018)

Ans.



- (i) **Provision:- As per Section 141(3)(d)(i)** of the Companies Act, 2013 **along with Rule 10 of the Companies (Audit and Auditors) Rule, 2014**, a person shall not be eligible for appointment as an auditor of a company,
- **Who, or his relative or partner**
  - **is holding any security of or interest** in the company or
  - **its subsidiary, or of its holding or associate company or a subsidiary of such holding company.** (associate company includes a **Joint Venture company** under company law)
  - **Exception:-** Provided that the **relative may hold security or interest** in the company of **face value not exceeding rupees one lakh**.
    - ❖ **Section 141(4)** provides that an auditor who **incurs any of the disqualifications** mentioned in **section 141(3)** after his appointment, **he shall vacate his office** as such auditor. and such vacation shall be deemed to be a **casual vacancy in the office of the auditor**.
- (ii) **In the present case:-** Mr. Hanuman, Chartered Accountant, a partner of M/s Ram and Hanuman Associates, **holds 100 equity shares of Shiva Ltd.** which is a **subsidiary of Krishna Ltd.**
- (iii) **Conclusion:-** Therefore, the firm, **M/s Ram and Hanuman Associates would be disqualified** to be appointed as statutory auditor of Krishna Ltd. as per **section 141(3)(d)(i)**, which is the holding company of Shiva Ltd., because Mr. Hanuman one of the partner is holding equity shares of its subsidiary.

26.

**Relative Holding Securities of a Company**

"M/s Bhavin & Co." is an Audit Firm having partners "Mr. Bala" and "Mr. Chandu". "Mr. A" the relative of "Mr. Chandu", is holding securities of "AMD Ltd." having face value of ₹ 1,00,100/-. Whether "M/s Bhavin & Co." is qualified for being appointed as an auditor of "AMD Ltd."? **(Study Material)**

Ans.



- (i) **Provision:-** As per Section 141(3)(d)(i) of the Companies Act, 2013 along with Rule 10 of the Companies (Audit and Auditors) Rule, 2014, a person shall not be eligible for appointment as an auditor of a company,
- **Who, or his relative or partner**
  - is holding **any security of or interest** in the company or
  - its **subsidiary**, or of its **holding** or **associate** company or a **subsidiary of such holding company**. (associate company includes a **Joint Venture company** under company law )
  - **Exception:-** Provided that the **relative may hold security or interest** in the company of **face value not exceeding rupees one lakh**.
- (ii) **Conclusion:-** In the instant case, **M/s Bhavin & Co, will be disqualified for appointment as an auditor** of AMD Ltd as the relative of **Mr. Chandu** (i.e. partner of M/s Bhavin & Co.), is holding the securities in AMD Ltd **which is exceeding the limit mentioned** in proviso to section 141(3)(d)(i).

27.

**Relative Holding Securities of a Company**

M/s Rajamohan & Co. is an audit firm having partners CA. Raja and CA. Mohan. The firm has been offered the appointment as an auditor of Inn Ltd. for the Financial Year 2021-22. Mr. Bee, the relative of CA. Raja, is holding 8,000 shares (face value of ₹ 10 each) in Inn Ltd. having market value of ₹ 1,60,000. Whether M/s Rajamohan & Co. is disqualified to be appointed as auditors of Inn Ltd.? **(Study Material)**

Ans.



- (i) **Provision:-** As per Section 141(3)(d)(i) of the Companies Act, 2013 along with Rule 10 of the Companies (Audit and Auditors) Rule, 2014, a person shall not be eligible for appointment as an auditor of a company,
- **Who, or his relative or partner**
  - is holding **any security of or interest** in the company or
  - its **subsidiary**, or of its **holding** or **associate** company or a **subsidiary of such holding company**.
  - **Exception:-** Provided that the **relative may hold security or interest** in the company of **face value not exceeding rupees one lakh**.
- (ii) **In the present case:-** M/s Rajamohan & Co. is an audit firm having partners CA. Raja and CA. Mohan. Mr. Bee is a relative of CA. Raja and he is holding shares of Inn Ltd. of face value of ₹ 80,000 only (8,000 shares x ₹ 10 per share).
- (iii) **Conclusion:-** Therefore, **M/s Rajamohan & Co. is not disqualified for appointment as an auditors of Inn Ltd.** as the relative of CA. Raja (i.e. partner of M/s Rajamohan & Co.) is holding the securities in Inn Ltd. which is within the limit mentioned in proviso to section 141(3)(d)(i) of the Companies Act, 2013.

28.



**Indebted to the Holding Company**




Mr. Amar, a Chartered Accountant, bought a car financed at ₹ 7,00,000 by Chaudhary Finance Ltd, which is a holding company of Charan Ltd. and Das Ltd. He has been the statutory auditor of Das Ltd. and continues to be even after taking the loan. Comment. **(RTP-Nov-2016, Study Material)**

Ans.



- (i) **Provision:-** Section 141(3)(d)(ii) of the Companies Act, 2013 specifies that a **person shall be disqualified** to act as an auditor **if he is indebted** to the company, or its **subsidiary**, or its **holding** or **associate** company or a **subsidiary of such holding** company for an amount **exceeding five lakh rupees**.
- (ii) **In the given case:-** **Mr. Amar** is disqualified to act as an auditor under section 141(3)(d)(ii) as he is **indebted to M/s Chaudhary Finance Ltd.** for more than **₹ 5,00,000**. Also, according to section 141(3)(d)(ii) **he cannot act as an auditor of any subsidiary of Chaudhary Finance Ltd.** i.e. he is **also disqualified to work in Charan Ltd. & Das Ltd.** Therefore he has to vacate his office in Das Ltd. Even though it is a subsidiary of Chaudhary Finance Ltd.

	<p>(iii) <b>Conclusion:-</b> Hence <b>audit work performed by Mr. Amar as an auditor is invalid, he should vacate his office immediately</b> and Das Ltd should appoint <b>another auditor for the company.</b></p>
29.	<p><b>Purchase of Goods on Credit by the Auditor</b></p> <p>An auditor purchased goods worth ₹ 501,500 on credit from a company being audited by him. The company allowed him one month's credit, which it normally allowed to all known customers. Comment.</p>
Ans. 	<p>(i) <b>Provision:-</b> Section 141(3)(d)(ii) of the Companies Act, 2013 specifies that a <b>person shall be disqualified</b> to act as an auditor <b>if he is indebted</b> to the company for an amount <b>exceeding five lakh rupees.</b></p> <ul style="list-style-type: none"> <li>Where an auditor <b>purchases goods or services</b> from a company <b>audited by him on credit, he is definitely indebted</b> to the company and if the amount outstanding <b>exceeds rupees five lakh</b>, he is disqualified for appointment as an auditor of the company.</li> <li><b>It will not make any difference</b> if the company allows him the same <b>period of credit</b> as it allows to <b>other customers</b> on the normal terms and conditions of the business. <b>The auditor cannot argue</b> that he is enjoying only the <b>normal credit period</b> allowed to other customers.</li> </ul> <p>(ii) <b>Conclusion:-</b> In such a case he has <b>become indebted</b> to the company and <b>consequently</b> he has <b>deemed to have vacated his office.</b></p>
30.	<p><b>Indebtness to the Company</b></p> <p>CA Adroit was indebted to Infructuous (P) Limited for a sum of ₹ 6,00,000 as on April, 1 2021. However, CA Adroit having come to know that he might be appointed as auditor of the company, he squared up the amount on July 10, 2021. Later on, he was appointed as auditor of the company for the year ended March 31, 2022 at the Annual General Meeting held on July 16, 2021. Subsequently, one of the shareholders complains that the appointment of CA adroit as an auditor is invalid because he incurred disqualification under section 141 of the Companies Act, 2013. Comment <b>(RTP-Nov-2015, Nov-2016, MTP-May-2018)</b></p> <p style="text-align: center;"><b>OR</b></p> <p>Mr. Y was appointed as an auditor of PQR Ltd. for the year ended 31.3.2022 at the Annual General Meeting held on 16.08.2021. Mr. Y has been indebted to the company for sum of ₹ 5,10,000 as on 01.04.2021, the opening date of accounting year which has been subject to his audit. However, Mr. Y having come to know that he might be appointed as auditor, he repaid the amount on 10.8.2021. One of the shareholders, complains that the appointment of Mr. Y as an auditor was invalid because he incurred disqualification u/s 141 of the Companies Act, 2013. Whether the complaint is valid.</p>
Ans. 	<p>(i) <b>Provisions:-</b></p> <ul style="list-style-type: none"> <li><b>As per section 141(3)(d)(ii)</b> of the Companies Act, 2013, a person who is <b>indebted to the company</b> for an amount <b>exceeding ₹ 5,00,000</b> shall be <b>disqualified to act as an auditor</b> of such company</li> <li><b>As per section 141(4)</b> he shall <b>vacate his office</b> of auditor when he <b>incurs this disqualification</b> subsequent to his appointment.</li> <li>However, where the person has <b>liquidated his debt before the appointment</b> date, there is <b>no disqualification</b> to be construed for such appointment.</li> </ul> <p>(ii) <b>In the given case:-</b> CA Adroit was <b>indebted</b> to Infructuous (P) Ltd. for a <b>sum of ₹ 6,00,000</b> as on <b>01.04.2021</b>. He was appointed as an auditor of the company for the year ended <b>31.03.2022</b> at the Annual General Meeting held on <b>16.07.2015</b>. He also <b>repaid the loan</b> amount fully to the company on <b>10.7.2015</b> i.e. before the date of his appointment.</p> <p>(iii) <b>Conclusion:-</b> Hence, the <b>appointment of CA Adroit as an auditor is valid</b> and the <b>shareholder's complaint is not acceptable.</b></p>
31.	<p><b>Indebtness to the Subsidiary Company</b></p> <p>Sri &amp; Company, a firm of Chartered Accountants was appointed as statutory auditors of Aaradhana Company Ltd. Aaradhana Company Ltd. holds 51 % shares in Sarang Company Ltd. Mr. Sri, one of the partners of Sri &amp; Company, owed ₹ 1,500 as on the date of appointment to Sarang Company Ltd. for goods purchased in normal course of business. Comment.</p>

Ans. 	<p>(i) <b>Provision:-</b> As per <b>Section 141(3)(d)(ii)</b> of the Companies Act, 2013,</p> <ul style="list-style-type: none"> <li>• <b>A person who, or his relative or partner</b></li> <li>• <b>Is indebted to the company, or its subsidiary, or its holding or associate company, or a subsidiary of its holding company, for an amount exceeding ₹ 5,00,000/-,</b></li> <li>• <b>Then he is not qualified for appointment</b> as an auditor of a company.</li> </ul> <p>(ii) <b>In the given case:-</b> Sri &amp; Company, a firm of Chartered Accountants was appointed as statutory auditors of Aaradhana Company Ltd. where the company holds 51% shares in Sarang Company Ltd. Mr. Sri, one of the partners of Sri &amp; Company owed ₹ 1,500 as on the date of appointment to Sarang Company Ltd. for goods purchased.</p> <p>(iii) <b>Conclusion:-</b> The partner <b>Mr. Sri is not disqualified to be appointed</b> as auditor of the company as he is indebted to the company for an <b>amount not exceeding ₹ 5,00,000.</b> Due to this, Sri &amp; Co., is not disqualified to be appointed as an auditor of Aaradhana Company Ltd.</p>
32.	<p><b>Indebtness to the Subsidiary Company</b></p> <p>Navy and Cavy Associates, a Chartered Accountant firm, has been appointed as Statutory Auditor of Poor Ltd. for the financial year 2021-2022. Mr. Savy, the relative of Mr. Navy, a partner in Navy and Cavy Associates, is indebted for ₹ 6,00,000 to Wealthy Ltd., a subsidiary company of Poor Ltd. Comment <b>(RTP-May 2015)</b></p>
Ans. 	<p>(i) <b>Provision:-</b> As per <b>Section 141(3)(d)(i)</b> of the Companies Act, 2013 <b>along with Rule 10 of the Companies (Audit and Auditors) Rule, 2014</b>, a person shall not be eligible for appointment as an auditor of a company,</p> <ul style="list-style-type: none"> <li>• <b>A person who, or his relative or partner</b></li> <li>• <b>Is indebted to the company, or its subsidiary, or its holding or associate company, or a subsidiary of its holding company, for an amount exceeding ₹ 5,00,000/-,</b></li> <li>• <b>Then he is not qualified for appointment as an auditor of a company.</b> <ul style="list-style-type: none"> <li>➤ <b>Section 141(4)</b> provides that an auditor who <b>incurs any of the disqualifications</b> mentioned in <b>section 141(3)</b> after his appointment, <b>he shall vacate his office</b> as such auditor. and such vacation shall be deemed to be a <b>casual vacancy in the office of the auditor.</b></li> </ul> </li> </ul> <p>(ii) <b>In the present case:-</b> Mr. Savy, the relative of Mr. Navy, a partner in Navy and Cavy Associates, has been <b>indebted to Wealthy Ltd.,</b> a subsidiary company of Poor Ltd., <b>for ₹ 6 lakhs.</b></p> <p>(iii) <b>Conclusion:-</b> Therefore, the firm, Navy and Cavy Associates <b>would be disqualified to be appointed as statutory auditor of Poor Ltd.</b> as per section 141(3)(d)(ii), which is the holding company of Wealthy Ltd., because Mr. Savy, the relative of Mr. Navy, a partner in Navy and Cavy Associates, has been indebted to Wealthy Ltd. for an amount exceeding the minimum approved limit.</p>
33.	<p><b>Section 141 – Disqualification-Indebtedness (Computer Bought on Credit)</b></p> <p>Mr. E, proprietor of M/s. E &amp; Co. is the statutory auditor of a Company which owns a store dealing in computer equipments. During the year 2021-22, E purchased a computer from the store costing ₹ 25,000 for his son. He did not make any payment for the same, but asked the company to adjust the same against the audit fees payable of ₹ 50,000. Whether auditor is disqualified?</p>
Ans. 	<p>(i) <b>Provision:-</b> As per <b>Sec. 141(3)(d)(ii)</b> of the Companies Act, 2013 read with Rule 10 of Companies (Audit and Auditor's) Rules, 2014, a <b>person who is indebted</b> to the company for an <b>amount exceeding ₹5 Lacs</b> shall be <b>disqualified to be appointed</b> as auditor.</p> <p>(ii) <b>In the present case:-</b> Mr. E, Proprietor of M/s E &amp; Co. is the <b>statutory auditor</b> of a company which owns a store dealing in computer equipment's, <b>purchased a computer from the store and adjusted the payment</b> for the same against his audit fee.</p> <p>(iii) <b>Conclusion:-</b> Therefore, <b>the contention of Mr. E that he does not incur disqualification is correct</b> as he has purchased a computer of the <b>value of 25,000</b> which is not exceeding the prescribed limit of 5,00,000. <b>Thus, Mr. E will not be held liable for guilty of contravention</b></p>

34.

**Auditor's Disqualifications as to Business Relationship**

PQ and Co. is an audit firm with P and Q as partners. For the financial year 2021-22, the firm has been appointed as statutory auditor of M/s Mango Orchards Hotel Ltd. The audit firm is a regular customer of the hotel and the partners usually stay in the same hotel at various locations in the course of travelling for their various professional assignments. Normally, payments for such stay are settled against quarterly bills raised by the company. Give your comment with respect to the Companies Act, 2013. **(May-2019-New)**

Ans.


**(i) Provision:-**

- **As per Sec. 141(3)(d)(ii)** of the Companies Act, 2013 read with Rule 10 of Companies (Audit and Auditor's) Rules, 2014, a **person who is indebted** to the company for an **amount exceeding ₹5 Lacs** shall be **disqualified to be appointed** as auditor.
- **As per section 141(3)(e)** of Companies Act, 2013, a person or a firm who, **whether directly or indirectly**, has **business relationship with the company**, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed, is **disqualified to be appointed** as auditor of that company.

**(ii) As per Rule 10 of Companies (Audit and Auditor's) Rules, 2014:-** The term "business relationship" shall be **construed as any transaction** entered into for a **commercial purpose**, except:

- Commercial transactions **which are in the nature of professional services permitted to be rendered by an auditor** or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;
- Commercial transactions **which are in the ordinary course of business** of the company **at arm's length price** - like sale of products or services to the auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.

**(iii) In the present case:-** Audit firm is a **regular customer of the client running a hotel** and the partners **usually stay in the same hotel** at various locations in the course of travelling for their various professional assignments. Normally, payments for such stay are settled against quarterly bills raised by the company.

**(iv) Conclusion:-** **No disqualification arises** as the services availed are in ordinary course of business of client and cannot be considered as business relationship. **(It is assumed that outstanding does not exceed ₹5 Lacs.)**

35.

**Implications of Relatives' Securities Holding on the Appointment of the Auditor**

Mr. Y, a practising Chartered Accountant, has been appointed as an auditor of M/s Z Ltd on 12th June, 2021 for the year ended 31st March, 2022. The following persons have done following transactions in securities of M/s Z Ltd.:

- Daughter of Mr. Y: Purchase of Securities on 10<sup>th</sup> September, 2021 of face value of ₹ 45,000 (market value ₹ 90,000)
- Husband of daughter of Mr. Y: Purchase of Securities on 10<sup>th</sup> December 2021 of face value of ₹ 90,000 (market value ₹ 1,90,000)

All the above securities were sold on 10<sup>th</sup> March, 2022 for ₹ 3,00,000. Discuss the implications of the above on the appointment of Mr. Y. **(RTP-May-2022)(May-2019-Old)**

Ans.


**(i) Provision:-** **As per Section 141(3)(d)(i)** of the Companies Act, 2013 **along with Rule 10** of the **Companies (Audit and Auditors) Rule, 2014**, a person shall not be eligible for appointment as an auditor of a company,

- **Who, or his relative or partner**
- Is holding **any security of or interest** in the company or
- Its **subsidiary**, or of its **holding** or **associate** company or a **subsidiary of such holding company**.
- **Exception:-** Provided that the **relative may hold security or interest** in the company of **face value not exceeding rupees one lakh**.

- **Section 141(4)** provides that an auditor who **incurs any of the disqualifications** mentioned in **section 141(3)** after his appointment, **he shall vacate his office** as such auditor. and such vacation shall be deemed to be a **casual vacancy in the office of the auditor**.
- Further the **definition of relative also includes daughter and a daughter's husband**. Both are covered in the definition of relative as defined by the Companies Act 2013.
- Thus, the **disqualifications will be applicable** as the relative/s are holding securities of face value of more than ₹ 100,000 and **market value is not important**.
- It is also to note that in the event of acquiring any security or interest by a relative above the threshold prescribed, the **corrective action to maintain the limits as specified above can be taken by the auditor within 60 days of such acquisition or interest**. The same has however not been done.

(ii) **In the instant case:- Daughter of Mr. Y** purchased the securities on **10th September 2021** of face value of **rupees 45,000** and **husband of daughter of Mr. Y** purchased the securities on **10th of December, 2021** of face value of **rupees 90,000**. Aggregating the value of holding of securities exceeds the limits mentioned in proviso to section 141(3)(d)(i) **i.e. rupees 1,00,000**.

Further, **corrective action** taken by Husband of Daughter of Mr. Y on 10th March, is **also not in accordance with prescribed grace period of 60 days**.

(iii) **Conclusion:- Therefore, CA. Y will be disqualified for appointment** as an auditor of **M/s. Z Ltd.** as per section 141(3)(d)(i) and **he shall vacate his office**.

36.

#### Sec. 141 – Disqualification Relative of Director

Mrs X is a Director of ABC Pvt. Ltd. During the year 2021-22, the company appointed CA Mr Y, Mrs X's spouse, as its statutory auditor Mr Y used to deliver audit report without any comments or disclosures, thereupon Comment.

(Study Material)

Ans.



(i) **Provision:- Section 141(3)(f) of the Companies Act 2013**

**As per Section 141(3)(f)** of the Companies Act, 2013, **aperson shall not be eligible** for appointment as an auditor of a company

- **Whose relative is a director or**
- **Is in the employment of the company as director or**
- **Key managerial personnel.**

The definition of 'Relative' **includes husband and wife**.

(ii) **As per Clause:- Clause (9) of Part I of the First Schedule to the Chartered Accountants Act, 1949**

A member in practice shall be **deemed to be guilty of professional misconduct** if he **accepts an appointment** as auditor of a company **without first ascertaining** from it whether the **requirements of Section 139, 140 and 142 read with Section 141 of the Companies Act, 2013, in respect of such appointment have been duly complied with**.

(iii) **In this case:- Mrs. X is a Director** of ABC Pvt. Ltd. and the company has appointed **Mr. Y, Chartered Accountant**, Mrs. X's spouse, **as its statutory auditor**.

(iv) **Conclusion:- Mr. Y should not accept the appointment** as statutory auditor of the company, where **his wife Mrs. X is a director**. This is **contravention of section 141** of the Companies Act, 2013. Therefore, **Mr. Y is liable for misconduct** under the said clause since he accepted the appointment without first verifying the compliance of statutory requirements.

37.

#### Ceiling on Number of Audit

M/s ABC and Co., a firm of Chartered Accountants, comprising of three partners A, B, and C, is Statutory Auditors of 50 Companies as per details given below:

- (i) Small Companies - 10
- (ii) Private Companies having paid up share capital of less than ₹ 100 Crores - 20
- (iii) Private Companies having paid up share capital of more than ₹ 100 Crores - 15
- (iv) Public Companies - 5

Mr. A signs the Balance Sheet of 10 Small Companies and 10 Private Companies having paid up share capital of less than ₹ 100 Crores. Mr. B signs the Balance Sheet of 10 Private Companies having paid up share capital of less than ₹ 100 Crores and 5 Private Companies having paid up share capital of more than ₹ 100 Crores. Mr. C signs the Balance Sheet of 10 Private Companies having paid up share capital of more than ₹ 100 crores and 5 Public Companies.

What is the maximum number of audits that the firm as a whole can accept and what is the maximum number of audits each individual partner can accept? Answer in light of CA, 2013. **(May-2018-Old)**

Ans.



**(i) Provision:- As per section 141(3)(g)** of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor if he:

- Is in **full time employment** elsewhere or
- A person or a partner of a firm **holding appointment** as its auditor if such person or partner is at the date of such **appointment or reappointment** holding appointment as auditor of **more than twenty companies** other than:
  - One person companies,
  - Dormant companies,
  - Small companies and
  - Private companies having paid-up share capital less than ₹ 100 crore.

**which has not committed default in** filing its financial statements under **section 137** or annual return under **section 92** of the Companies Act with the Registrar.

**(ii) Interpretation of Provision:** -As per section 141(3)(g), **this limit of 20 company audits is per person**. In the case of an audit firm having 3 partners, the **overall ceiling will be  $3 \times 20 = 60$**  company audits.

**(iii) In the given case:-** CA A is holding appointment in **20 companies** i.e. 10 small companies and 10 private companies having paid up share capital of less than ₹ 100 crore, whereas CA B is having appointment in **15 Companies** i.e. 10 private companies having paid up share capital of less than ₹ 100 crore and 5 private companies having paid up share capital of more than ₹ 100 crore and CA C is having appointment in **5 public companies and 10 private companies** having paid up share capital of more than ₹ 100 crore. In aggregate all three partners are having **50 audits**.

**(iv) Conclusion:-** As per above provisions, an **individual auditor can accept** more appointments as auditor

= ceiling limit as per section 141(3)(g) XX

Less - already holding appointments as an auditor.(XX)

Hence

(1) CA A can accept: 20 more audits.

(2) CA B can accept  $20 - 5 = 15$  more audits and

(3) CA C can accept  $20 - 15 = 5$  more audits.

**M/s ABC & Co. can accept appointment as an auditor of 40 more companies as under:**

Total Number of Audits available to the Firm	= $20 \times 3$	=	60
Number of Audits already taken by all the partners in their individual capacity	= $0 + 5 + 15$	=	20
Remaining number of Audits available to the Firm		=	40

38.

### Ceiling on Number of Audit

MSY & Company is an Audit Firm having partners CA Mukti, CA Shakti and CA Yukti. CA Mukti, CA Shakti and CA Yukti are holding appointment as an Auditor in 4, 6 and 10 companies respectively.

(i) Provide the maximum number of audits remaining in the name of MSY & Company

(ii) Provide the maximum number of audits remaining in the name of individual partner i.e. CA Mukti, CA Shakti, CA Yukti.

- (iii) Can MSY & Company accept the appointment as an auditor in 60 private companies having paid-up share capital less than ₹100 crore, 2 small companies and 1 dormant company?
- (iv) Would your answer be different, if out of those 60 private companies, 45 companies are having paid-up share capital of ₹ 110 crore each?

(RTP-Nov-2014, RTP-May-2016, MTP-Nov/May-2018, RTP Nov-2019)

OR

"PQRST & Co." is an Audit Firm having partners "Mr. P", "Mr. Q", "Mr. R", "Mr. S" and "Mr. T", Chartered Accountants. "Mr. P", "Mr. Q", "Mr. R", "Mr. S" and "Mr. T" are holding appointment as an Auditor in 4, 5, 6, 10 and 15 Companies respectively.

- (i) Provide the maximum number of Audits remaining in the name of "PQRST & Co."
- (ii) Provide the maximum number of Audits remaining in the name of individual partner i.e. "Mr. P", "Mr. Q", Mr. R, Mr. S and Mr. T.
- (iii) Can PQRST & Co. accept the appointment as an auditor in 80 private companies having paid-up share capital less than ₹ 100 crore which has not committed default in filing its financial statements under section 137 or annual return under section 92 of the Companies Act with the Registrar, 2 small companies and 1 dormant company?
- (iv) Would your answer be different, if out of those 80 private companies, 65 companies are having paid-up share capital of ₹ 115 crore each?

(Study Material)

Ans.



- (i) **Provision:- As per section 141(3)(g)** of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor if he:

- **Is in full time employment elsewhere or**
- **A person or a partner of a firm holding appointment as its auditor if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies other than:**
  - **One person companies,**
  - **Dormant companies,**
  - **Small companies and**
  - **Private companies having paid-up share capital less than ₹ 100 crore.**

**Which has not committed default in** filing its financial statements under **section 137** or annual return under **section 92** of the Companies Act with the Registrar.

- (ii) **Interpretation of Provision:** -As per section 141(3)(g), **this limit of 20 company audits is per person.** In the case of an audit firm having 3 partners, the **overall ceiling will be  $3 \times 20 = 60$**  company audits. Sometimes, a chartered accountant is a partner in a number of auditing firms. In such a case, all the firms in which he is partner or proprietor will be together entitled to 20 company audits on his account.

- (iii) **In the given case:-**

- **CA Mukti** is holding appointment in **4 companies**, whereas
- **CA Shakti** is having appointment in **6 Companies** and
- **CA Yukti** is having appointment in **10 Companies.**
- **In aggregate all three partners** are having **20 audits.**

- (1) Therefore, **MSY & Co. can hold appointment** as an auditor of **40 more companies:**

Total Number of Audits available to the Firm =  $20 \times 3$  = 60

Number of Audits already taken by all the partners  
in their individual capacity =  $4+6+10$  = 20

Remaining number of Audits available to the Firm = 40

- (2) **With reference to above provisions** an auditor can hold more appointment as auditor  
= ceiling limit as per section 141(3)(g)

Less- already holding appointments as an auditor.

Hence

(i) **CA Mukti can hold:**  $20 - 4 = 16$  more audits.

(ii) **CA Shakti can hold**  $20 - 6 = 14$  more audits and

(iii) **CA Yukti can hold**  $20 - 10 = 10$  more audits.

(3) In view of above discussed provisions **MSY & Co. can hold appointment** as an auditor in **all the 60 private companies** having paid -up share capital less than ₹ 100 crore, **2 small companies** and **1 dormant company** as these are excluded from the ceiling limit of company audits given under section 141(3)(g) of the Companies Act, 2013.

(4) **As per fact of the case, MSY & Co.** is already having **20 company audits** and they **can also accept 40 more company audits**. In addition, they can also conduct the audit of one person companies, small companies, dormant companies and private companies having paid up share capital less than rupees 100 crores. In the given case, out of the 60 private companies, MSY & Co. is offered 45 companies having paid -up share capital of ₹ 110 crore each.

**Therefore, MSY & Co. can also accept the appointment as an auditor for 2 small companies, 1 dormant company, 15 private companies** having paid-up share capital less than ₹ 100 crore and **40 private companies** having paid-up share capital of ₹ 110 crore each **in addition to above 20 company audits already holding.**

39.

#### Ceiling on Number of Company Audits

PQR & Company a firm of Chartered Accountants has three partners, P, Q and R; P is also in whole time employment elsewhere. The firm is already holding audit of 40 companies including audit of one foreign company. The firm is offered the audit of Z Ltd. and its 20 branches. Whether firm can accept?

Ans.



(i) **Provision:- As per section 141(3)(g)** of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor if he:

- Is in **full time employment** elsewhere or
- A person or a partner of a firm **holding appointment** as its auditor if such person or partner is at the date of such **appointment or reappointment** holding appointment as auditor of **more than twenty companies** other than:
  - **One person companies,**
  - **Dormant companies,**
  - **Small companies and**
  - **Private companies** having paid-up share capital **less than ₹ 100 crore.**
- **Which has not committed default in** filing its financial statements under **section 137** or annual return under **section 92** of the Companies Act with the Registrar

(ii) **Interpretation of Provision:-** As per section 141(3)(g), **this limit of 20 company audits is per person.** In the case of an audit firm having 3 partners, the **overall ceiling will be  $3 \times 20 = 60$**  company audits. . Sometimes, a chartered accountant is a partner in a number of auditing firms. In such a case, all the firms in which he is partner or proprietor will be together entitled to 20 company audits on his account.

(iii) **Analysis of case:-** In the given case of PQR & Co., **P is in whole-time employment** elsewhere. Hence he **will be excluded** in determining the number of company audits that the firm can hold. If Q and R do not hold any audits in their personal capacity or as partners of other firms, the total number of company **audits that can be accepted by PQR & Co. is  $20 \times 2 = 40$**  and in the given case, the firm is already holding 40 audits.

(iv) **Conclusion:-** Therefore, **PQR & Co. cannot accept audit of Z Ltd. and its 20 branches** as per section 141(3)(g) of the Companies Act, 2013.

40.

**Ceiling Limit for Holding Company Audits**

KSY & Company Chartered Accountants is an audit firm having two partners CA K and CA Y. KSY & Company is already holding appointment as auditors of 36 public companies.

KSY & Company seeks your advice in the following situations:

- (a) KSY & Company has been offered the appointment as Auditors of 7 more Private Limited Companies. Of the seven, one is a company with a paid up share capital of ₹ 150 crores, five are "Small companies" as per the Act and one is a "Dormant Company".
- (b) Would your answer be different, if out of those 7 Private Companies, 3 Companies have paid up capital of ₹ 90 crores each? Answer in light of CA, 2013

(May-2016)

Ans.



- (i) **Provision:- As per section 141(3)(g)** of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor if he:

- Is in **full time employment** elsewhere or
- A person or a partner of a firm **holding appointment** as its auditor if such person or partner is at the date of such **appointment or reappointment** holding appointment as auditor of **more than twenty companies** other than:
  - One person companies,
  - Dormant companies,
  - Small companies and
  - Private companies having paid-up share capital less than ₹ 100 crore.
- **Which has not committed default in** filing its financial statements under **section 137** or annual return under **section 92** of the Companies Act with the Registrar.
- **In the case of firm of auditors:-** It has been further provided that **specified number of companies** shall be construed as the number of companies specified for every partner of the firm **who is not in full time employment elsewhere.**

- (ii) **In the instant case:-** KSY & Co. is an audit firm having **two partners**, namely, CA. K and CA. Y. The total number of company audits that can be accepted by the firm is 40 (**2 partners x 20 companies each partner**). However, the firm is already holding appointment as auditors of **36 public companies**. Thus, the **remaining number of audits** that can be accepted by the firm is of **4 more companies**.

- (iii) **Conclusion:-**

- KSY & Co. can accept audit of **all 7 Private companies**, because **5 small companies** and **one dormant company** will not be considered for the purpose of ceiling limit. Total number of audits after acceptance of all seven **audits remains at 37.**
- **Answer will remain same**, as the private companies having **paid up capital less than 100 Crores** are not considered for the purpose of ceiling limit. Total number of audits after acceptance of **all seven audits remains at 40** assuming that other **four companies** having paid up capital in excess of ₹ 100 Crores.

**SJ Note:** The answer has been given **assuming none of the partners hold any company audits in their personal capacity or as partners with another firm.**

41.

**Ceiling on number of audit**

M/s XYZ & Co. is an Audit Firm having partners Mr. X, Mr. Y and Mr. Z, Chartered Accountants. Mr. X. Mr. Y and Mr. Z are holding appointment as Auditors in 5, 5 and 10 companies respectively.

- (i) Provide the maximum number of Audits remaining in the name of XYZ & Co.
- (ii) Provide the maximum number of Audits remaining in the name of individual partner i.e. Mr. X, Mr. Y and Mr. Z.
- (iii) Can XYZ & Co. accept the appointment as an auditor in 60 private companies having paid-up share capital less than 100 crore, 2 small companies and 2 dormant companies?
- (iv) Would your answer be different, if out of those 60 private companies, only 15 companies are having paid-up share capital of less than ₹ 100 crore each?

Discuss with reference to ceiling on member of audits as per Companies Act, 2013.

(July-2021-Old, MTP-May-2021)

Ans.


**Maximum number of Audits**

- (1) **Provisions and Explanations:** As per section 141(3)(g) of the Companies Act, 2013, a **person shall not be eligible for appointment as an auditor** if he is in **full time employment** elsewhere or a **person or a partner of a firm holding appointment as its auditor**, if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of **more than twenty companies** other than one person companies, dormant companies, small companies and private companies having **paid-up share capital less than ₹ 100 crore** (private company which has not committed a default in filing its financial statements under section 137 of the said Act or annual return under section 92 of the said Act with the Registrar).

**As per section 141(3)(g)**, this limit of 20 company audits is **per person**. In the case of an **audit firm having 3 partners**, the overall ceiling will be  $3 \times 20 = 60$  **company audits**. Sometimes, a chartered accountant is a partner in a number of auditing firms. In such a case, all the firms in which he is partner or proprietor will be together entitled to 20 company audits on his account.

- (2) **Fact of the Case:** In the instant case, **Mr. X** is holding appointment in **5 companies**, whereas **Mr. Y** is having appointment in **5 Companies** and **Mr. Z** is having appointment in **10 Companies**. In aggregate all three partners are having **20 audits**.

(3) **Conclusion:**

- (i) **Therefore, XYZ & Co. can hold appointment as an auditor of 40 more companies:** Total Number of Audits available to the Firm =  $20 \times 3 = 60$  Number of Audits already taken by all the partners In their individual capacity =  $5 + 5 + 10 = 20$  Remaining number of Audits available to the Firm = 40

- (ii) **With reference to above provisions an auditor can hold more appointment as auditor =** ceiling limit as per section 141(3)(g)-already holding appointments as an auditor.

Hence (1) Mr. X can hold:  $20 - 5 = 15$  more audits. (2) Mr. Y can hold  $20 - 5 = 15$  more audits and (3) Mr. Z can hold  $20 - 10 = 10$  more audits.

- (iii) **In view of above discussed provisions**, XYZ & Co. can hold appointment as an auditor in **all the 60 private companies** having paid-up share capital less than ₹ 100 crore (private company which has not committed a default in filing its financial statements under **section 137** of the said Act or annual return under **section 92** of the said Act with the Registrar.”), **2 small companies** and **2 dormant company** as these are excluded from the ceiling limit of company audits given under **section 141(3)(g)** of the Companies Act, 2013.

- (iv) **As per fact of the case**, XYZ & Co. is already having **20 company audits** and they can **also accept 40 more company audits**. In addition, they can also conduct the audit of one person companies, small companies, dormant companies and private companies having paid up share capital less than ₹ 100 crores. In the given case, **out of the 60 private companies** XYZ & Co. is offered, **15 companies** having paid-up share capital of less than **₹ 100 crore each**.

**Therefore, XYZ & Co.** can also accept the appointment as an auditor for **2 small companies, 2 dormant company, 15 private companies** having paid-up share capital less than ₹ 100 crores (private company which has not committed a default in filing its financial statements under **section 137** of the said Act or annual return under **section 92** of the said Act with the Registrar.”) and 40 private companies having paid-up share capital of ₹ 100 crore or more each in addition to above 20 company audits already holding.

42.

**Disqualification: Security & Indebtness**

Comment on the validity of the appointment of Mr. A as an auditor of ABC Ltd. in the following situations

- (i) Mr. B, a partner of Mr. A held shares of face value of ₹ 1,00,000 in DEF Ltd., the holding company of ABC Ltd. Mr. B has sold the securities after a period of 45 days from the date of appointment of Mr. A as an auditor of ABC Ltd.
- (ii) Mrs. A, wife of Mr. A had given a financial guarantee for the principal amount of a debt owed by Mr. X to ABC Ltd. for ₹ 6 lakhs. Mr. X has repaid ₹ 5 lakhs to ABC Ltd. 2 days before the date of appointment of Mr. A as an auditor of the company.

(Nov-2018-Old)

Ans.

**(i) Validity of appointment of Auditor**

- **Provision:-** According to **section 141(3)(d)(i)** of the companies act 2013, a person is disqualified to be appointed as auditor of the company if he or his relative or partner holds securities in the company or its holding company or subsidiary company, associate company or the subsidiary of the holding company.
- **Rule 10 of the Companies (Audit and Auditors) Rule, 2014:-** Permits relative alone to hold shares in the company **up to 1 Lakh**. It also provides a time limit of **60 days** to correct the situation where disqualification would otherwise incur
- **In the present case:-** Mr. B, a partner of Mr. A held shares of **face value of ₹ 1,00,000** in DEF Ltd., the holding company of ABC Ltd. Mr. B has sold the securities after a period of 45 days from the date of appointment of Mr. A as an auditor of ABC Ltd.
- **Conclusion:- Appointment of Mr. A as auditor in ABC Ltd. is not valid** as he is disqualified by virtue of provisions as stated in Sec. 141(3)(d)(i). Subsequent sale of securities by the partner is of no relevance in this case.

**(ii) Guarantee by the relative of Auditor:**

- **Provision:- Section 141 (3)(d)(iii)** of the Companies Act 2013 provides that a person is disqualified to be appointed as auditor of the company if he or his relative or partner has given guarantee or provided security to any 3<sup>rd</sup> person for his indebtedness with the company, its holding company, its subsidiary, associate company or subsidiary of its holding company for an amount the limit prescribed.
- **Rule 10 of the Companies (Audit and Auditors) Rule, 2014:-** Prescribes a limit of amount that **exceeds ₹ 1 Lakh**. As such, any guarantee or provision of security for an amount exceeding 1 Lakh will render a person to be disqualified
- **In the present case:-** At the time of appointment, the guarantee subsists only for the remaining ₹ 1 Lakh as ₹ 5 lakhs out of ₹ 6 Lakhs has been already discharged
- **Conclusion:- Appointment of Mr. A as auditor in ABC Ltd. is valid** as the amount of guarantee given by the Mrs. A for indebtedness of Mr. X in the company does not exceed ₹ 1 lac as on date of appointment

43.

**Disqualification Due to Holding of Securities**

Mr. Pratiq, a practicing Chartered Accountant, has been appointed as an auditor of Opus Ltd. He is holding securities of the company having face value of ₹ 89,000 only.

- You are required to state, whether Mr. Pratiq is qualified to be appointed as an auditor of Opus Ltd.
- Would your answer be different, if instead of Mr. Pratiq; Mr. Quresh, the step- father of Mr. Pratiq, is holding the securities?

Ans.

**(i) Provision:- As per Section 141(3)(d)(i) of the Companies Act, 2013 along with Rule 10 of the Companies (Audit and Auditors) Rule, 2014, a person shall not be eligible for appointment as an auditor of a company,**

- **Who, or his relative or partner**
- **Is holding any security of or interest in the company or**
- **its subsidiary, or of its holding or associate company or a subsidiary of such holding company.**
- **Exception:- Provided that the relative may hold security or interest in the company of face value not exceeding rupees one lakh.**
  - ❖ **Section 141(4)** provides that an auditor who **incurs any of the disqualifications** mentioned in **section 141(3)** after his appointment, **he shall vacate his office** as such auditor. and such vacation shall be deemed to be a **casual vacancy in the office of the auditor.**

**(ii) Definition of Relative :-** The term “relative” has been defined under the **Companies Act, 2013** which means **anyone who is related to another** as members of a **Hindu Undivided Family;**

- Husband and wife;
- Father (including step- father),
- Mother (including step-mother),
- Son (including step- son),
- Son's wife, Daughter, Daughter's husband,
- Brother (including step- brother),
- Sister (including step- sister).

(iii) **Conclusion:-** In the present situation,

- **Mr. Pratiq** is holding securities in **Opus Ltd.**, which is **not allowed as per the provisions** of section 141(3)(d)(i) of the Act. Therefore, Mr. Pratiq **will be disqualified to be appointed** as an auditor of Opus Ltd.
- **Mr. Quresh**, the step-father of Mr. Pratiq, is holding the securities in Opus Ltd. It may be noted that **step-father is included in the definition** of the term "relative" as per the Companies Act, 2013. Further, proviso to section 141(3)(d)(i) of the Act allows a relative of the auditor to hold securities in the company of face value not exceeding of ₹ 1,00,000. Here, Mr. Quresh is holding securities for **face value of ₹ 89,000** which is below the limit as prescribed under the said proviso. Therefore, **Mr. Pratiq will not be disqualified to be appointed as an auditor** of Opus Ltd.

44.

#### Disqualification due to Holding of Securities

M/s RM & Co. is an audit firm having partners CA. R and CA. M. The firm has been offered the appointment as an auditor of Enn Ltd. for the Financial Year 2021-22. Mr. Bee, the relative of CA. R, is holding 5,000 shares (face value of ₹ 10 each) in Enn Ltd. having market value of rupees 1,50,000. Whether M/s RM & Co. is disqualified to be appointed as auditors of Enn Ltd.

Ans.



- (i) **Provision:-** As per **Section 141(3)(d)(i)** of the Companies Act, 2013 **along with Rule 10** of the **Companies (Audit and Auditors) Rule, 2014**, a person shall not be eligible for appointment as an auditor of a company,
- **Who, or his relative or partner**
  - **Is holding any security of or interest in the company or**
  - **its subsidiary, or of its holding or associate company or a subsidiary of such holding company.**
  - **Exception:-** Provided that the relative may hold security or interest in the company of face value not exceeding rupees one lakh.
- (ii) **In the instant case:-** M/s RM & Co. is an audit firm having partners CA. R and CA. M. Mr. Bee is a relative of CA. R and he is holding shares of Enn Ltd. of face value of ₹ 50,000 only (5,000 shares × ₹10 per share).
- (iii) **Conclusion:-** Therefore, **M/s RM & Co. is not disqualified for appointment** as an auditors of **Enn Ltd.** as the relative of CA. R is holding the securities in Enn Ltd. **which is within the limit mentioned** in proviso to **section 141(3)(d)(i)** of the Companies Act, 2013.

#### 5.4 - Section-142 Remuneration of Auditors

45.

#### Restricting Scope of Audit

Y, is the auditor of X Pvt. Ltd. in which there are four shareholders only, who are also the Directors of the company. On account of bad trade and for reducing the expenses in all directions, the directors asked Y to accept a reduced fee and for that he has been offered not to carry out such full audit as he has done in the past. Y accepted the suggestions of the directors.

Ans.

- (i) **Provision:**
- **Section 142: Remuneration of Auditor**
    - Further, remuneration is a **matter of arrangement** between the auditor and the shareholders.
    - Section 142 **specifies the remuneration** of an auditor, shall be fixed by the company in



general meeting or

- **In such manner** as the company in general meeting may determine.
- His duties may not necessarily commensurate with his remuneration.

• **Section 143: Power & Duties of Auditor**

- Auditor's duties are governed by the provisions of **Section 143** of Companies Act 2013,
- **Which cannot be restricted** either by the **director** or even by the **entire body of shareholders?**

(ii) **Conclusion:-** Y, therefore, **should not accept the suggestions** of the directors **regarding the scope** of the work to be done. Even if Y accepts the suggestions of the directors regarding the scope of work to be done, **it would not reduce his responsibility** as an auditor under the law. Under the circumstances, **Y is violating the provisions** of the Companies Act, 2013.

### 5.5 - Section-143 Power & Duties of Auditor

46.

#### Restrictions on Powers of Statutory Auditors

At the Annual General Meeting of the Company, a resolution was passed by the entire body of shareholders restricting some of the powers of the Statutory Auditors. Whether powers of the Statutory Auditors can be restricted?

Ans.



(i) **Provision:- Section 143(1)** of the Companies Act, 2013 provides that an auditor of a company shall have

- **Right of access at all times** to the books and accounts and vouchers of the company
- Whether kept at the **Head Office or other places** and
- Shall be entitled to require from the offices of the company **such information and explanations** as the auditor may think necessary for the purpose of his audit.
- These specific rights have been **conferred by the statute** on the auditor to **enable him to carry out his duties and responsibilities** prescribed under the Act, **which cannot be restricted or abridged** in any manner.

(ii) **Conclusion:-** Hence, **any such resolution** even if passed by entire body of shareholders is **ultra virus and therefore void**.

47.

#### Comment on Matters Contained u/s 143(1) of the Companies Act, 2013

The auditor of Trilok Ltd. did not report on the matters specified in sub-section (1) of Section 143 of the Companies Act, 2013, as he was satisfied that no comment is required.

Ans.



(i) **Provision:- Section 143(1)** of the Act **deals with duties of an auditors** requiring auditor to make an enquiry in respect of **specified matters**.

- The **matters in respect of which the enquiry** has to be made by the auditor include relating to :
  - **loans and advances,**
  - transactions represented **merely by book entries,**
  - **investments** sold at less than cost price,
  - **loans and advances** shown as deposits, etc.

(ii) **Opinion of Institute:-** Since the law requires the auditor to **make an enquiry**, the Institute opined that the auditor is **not required to report** on the **matters specified 143(1) unless he has any special comments to make** on any of the items referred to therein. If the auditor is satisfied as a result of the enquiries, he has no further duty to report that he is so satisfied.

(iii) **Conclusion:-** Therefore, the **auditor of Trilok Ltd. is correct in non- reporting** on the matters specified in Section 143(1).

48.

#### Audit Report - Inquiry into Propriety Matters

While doing the audit, X, the Statutory Auditor of ABC Ltd. observes that certain loans and advances were made without proper securities, certain trade receivables and trade payables were adjusted inter se, and personal expenses were charged to revenue. Comment. **(Nov-2010, RTP-May-2015, Nov-2019-New)**

Ans.



- (i) **Provision:-** Section 143(1) of the Companies Act, 2013 requires the auditor to **conduct inquiry into certain matters** and if the auditor finds answer of any of these matters **in adverse**, auditor is **required to report**, otherwise no reporting is required.
- (ii) **In relation to observations stated in the question, auditor should inquire as follows:**
- **Clause (a) of Section 143(1)** requires the auditor to inquire "Whether **loans and advances made by the company** on the basis of security have been **properly secured** and whether the terms on which they have been made are **prejudicial to the interests of the company or its members**".
  - **Clause (b) of section 143(1)**, requires the auditor to inquire "whether transactions of the company which are **represented merely by book entries** are prejudicial to the interests of the company".
  - **Clause (e) of section 143(1)**, requires the auditor to inquire "Whether **personal expenses have been charged to revenue** account".
- (iii) **Audit Procedure:-**
- If the auditor finds that the **loans and advances have not been properly secured**, he may enter **an adverse comment** in the report **without modifying opinion** on financial statements if the loans and advances are **properly described and presented** in terms of **Part I of Schedule III** to the Companies Act.
  - If relation to his observation regarding inter se **adjustment of trade receivables and trade payables**, being a book entry, **auditor should have inquired** into the **legitimate interests of the company**. If appears prejudicial, **he may enter adverse comment** in the report.
  - Regarding **charging of personal expenses to revenue** account auditor should inquire whether such expenses are incurred **on the basis of the company's contractual obligations**, or in accordance with **accepted business practice**. If personal expenses incurred by the company are **not covered** by contractual obligations or by accepted business practice and charged to revenue account, **it would be the duty of the auditor to report thereon**.
- (iv) **Conclusion:-** Mr. X, the statutory auditor of ABC Ltd., **needs to enquire in light of above provisions**, as a result of the enquiries if he is satisfied then there is no further duty to report on these matters.

49.

**Sec. 143(1)-Inquiry Personal Expenses Foreign Trip of Director**

Director of T Ltd. draws an advance of US\$ 200 per day in connection with the foreign trip undertaken on behalf of the company. On his return he files a declaration stating that entire advance was expended without any supporting or evidence. T Ltd. books the entire expenses on the basis of such declaration. As the auditor of T Ltd. how do you deal with this?

(May-2011, RTP-May-2014)

Ans.



- (i) **AS per SA 500 "Audit Evidence"**  
It states that an auditor **should obtain sufficient appropriate audit evidence** to be able to draw reasonable conclusions on which to base his option.
- (ii) **Provison:- As per Section 143(1)(e) the Companies Act, 2013**  
It requires an auditor to enquire **whether personal expenses have been charged to revenue account**.
- (iii) **In the given case:-** Director of T Ltd. draws **an advance of US\$ 200 per day** in connection with the **foreign trip** undertaken on behalf of the company. On his return he files a declaration stating that **entire advance was expended without any supporting or evidence**. T Ltd. books the entire expenses on the basis of such declaration
- (iv) **Conclusion:-** In the context of the facts of case, ascertain whether the payment made by the company **for the foreign trip form an "allowance" or "reimbursement"**.  
An allowance is a fixed sum of money allowed or the basis of specified criteria. No evidence supporting the expenditure is required for payment of allowance to the director.  
**On the other hand**, if the payment is reimbursement should be against actual expenditure. The director concerned should provide proof of expenditure.

Since the director has given only a declaration the auditor should ascertain other relevant facts as to whether the advance paid is pursuant to the policy of the company which is based on director and the same is applicable to persons of a similar status within the company. If the auditor considers the advance taken is reasonable then the declaration can be considered adequate, otherwise he may have to call for additional documentary evidences.

50.

**Reimbursement of Personal Expenses of Director**

In the audit of ABC Private Limited, auditor came across cases of payments to Directors, whereby, expenses of a personal nature were reimbursed. As an auditor, how would you deal with the same?

( Nov-2020-Old)

Ans.


**(i) Provision:- Section 143(1)(e) of Companies Act, 2013**

- All payments to Directors as remuneration or perquisites whether in the case of a public or private company are required to be authorised both in accordance with the Companies Act and Articles of Association of the company.
- Articles may provide that such remuneration require sanction of the shareholders either by ordinary or special resolution while in some cases it may require only approval of Directors.
- If the terms of appointment of a Director include payment of expenses of a personal nature, then such expenses can be incurred by the company; otherwise, no such expense can be incurred or reimbursed by the company.

**(ii) In the given case:-** In the audit of ABC Private Limited, auditor came across cases of payments to Directors, whereby, expenses of a personal nature were reimbursed

**(iii) Conclusion:-** In the instant case the auditor has to ensure that the above is complied with, without which, if such expenses are paid, he has to disclose the fact in his report, as also in the accounts. In this regard attention is invited to section 143(1)(e) of the Companies Act, 2013 wherein auditor has to inquire into whether personal expenses have been charged to revenue.

51.

**Areas of Propriety u/s 143(1) of Companies Act 2013**

Tee & Co., a firm of Chartered Accountants had been appointed by C & AG to conduct statutory audit of M/s Rare Airlines Limited, a Public Sector Company. They would like to check certain mandatory propriety points as required under section 143(1) of the Companies Act, 2013. List the areas of check to meet these requirements.

(May-2018-New, MTP-May-2019)

Ans.



**Section 143(1)** of the Companies Act, 2013 requires the auditor to make an enquiry into certain specific areas. In some of the areas, the auditor has to examine the same from propriety angle as to:

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

52.

**Enquiring into Propriety Matters of the Company as required by Section 143(1)**

Mr. Raj, the engagement partner of R.O.K. & Co., in connection with statutory audit of Waria Ltd., had assigned the responsibility of enquiring into propriety matters of the Company as required by section 143(1) of the

Companies Act, 2013, to Mr. Samay, an engagement team member. Mr. Samay while making such enquiries, was having following queries, as tabulated below, which he ought to get resolved from Mr. Raj, as follows:-

Sr. No.	Query of Mr. Samay
1	What documents to be seen in case of loan given by the company in lieu of hypothecation of goods from lender as a security for the purpose of reporting as per clause (a) of section 143(1) of the Companies Act, 2013?
2	What shall be the cost of Debentures and Bonus Shares sold by the company for which the cost is not ascertainable for the purpose of reporting as per clause (c) of section 143(1) of the Companies Act, 2013?
3	Whether the shares allotted by Waria Ltd. against a loan taken by it from a NBFC can be considered to be allotted for cash for the purpose of reporting as per clause (f) of section 143(1) of the Companies Act, 2013?

Assuming that you are Mr. Raj the engagement partner, please provide answer to the queries of Mr. Samay?  
**(MTP-May-2021)**

**Ans.**

As a engagement partner I will provide answer to queries as follows:



Sr. No.	Query of Mr. Samay	Response to Query
1	What documents to be seen <b>in case of loan given by the company in lieu of hypothecation of goods</b> from lender as a <b>security</b> for the purpose of <b>reporting as per clause (a) of section 143(1)</b> of the Companies Act, 2013?	Mr. Samay should see <b>deed of Hypothecation</b> or <b>other document creating the charge</b> , together with a <b>statement of stocks</b> held at the balance sheet date in order.
2	What shall be the cost of Debentures and Bonus Shares sold by the company for which the cost is not ascertainable for the purpose of reporting as per clause (c) of section 143(1) of the Companies Act, 2013?	<p><b>(i) For Debentures sold:</b> Where the <b>cost of debentures</b> sold is <b>not ascertainable</b>, the <b>book value</b> thereof at the <b>date of sale</b> may be <b>treated as the cost</b> for the purposes of this clause.</p> <p><b>(ii) For Bonus Shares sold:</b> When <b>bonus shares are received</b>, the number of shares in the portfolio would be <b>increased by the bonus shares</b> while the <b>cost of the total portfolio</b> would <b>remain the same</b> as before. The result would be that the <b>average cost per unit</b> of the total holding would <b>come down proportionately</b>. The usual accounting practice for apportioning the cost of a part of the total holding on the sale thereof is to take it <b>at its average cost</b>.</p>
3	Whether the shares allotted by Waria Ltd. against a loan taken by it from a NBFC can be considered to be allotted for cash for the purpose of reporting as per clause (f) of section 143(1) of the Companies Act, 2013?	<p>The law on the subject has hitherto been that, where the <b>consideration for the issue of shares is an adjustment against a bona fide debt payable</b> in money on demand by the company, the <b>shares are deemed to have been subscribed in cash</b> (<b>vide the decision in Spargo's Case - 1873, 8, Ch. A. 407</b>). According to the <b>legal opinion obtained by the ICAI</b>, the expression "<b>shares allotted for cash</b>" may also include <b>shares allotted against a debt</b>.</p> <p>Therefore, in cases which are covered by the decision in Spargo's case, <b>no comment is required by the auditor</b>, even though the company may have in the <b>Return of Allotment under Section 75</b>, shown such shares as allotted against adjustment of a debt.</p> <p><b>Thus, the shares allotted by Waria Ltd. against a loan taken by it from a NBFC can be considered to be allotted for cash.</b></p>

53.

**Power of Auditor - Sec 143(1)-Rights of Auditor to Access Books & Vouchers**

While conducting the audit of a limited company for the year ended 31st March, 2022, the Auditor wanted to refer to the Minute Books. The Board of Directors refused to show the Minute Books to the auditor. Comment.

**(Study Material)**

Ans.



(i) **Provision:-** Section 143(1) of the Companies Act, 2013 **grants powers** to the auditor that **every auditor has a right of access, at all times, to the books and account** including all statutory records **such as minute books**, fixed assets register, etc. of the company for conducting the audit.

In order to verify actions of the company and to **vouch and verify some of the transactions** of the company, it is **necessary for the auditor to refer to the decisions** of the shareholders and/or the directors of the company.

(ii) **In the present case:-** While conducting the **audit of a limited company** for the year ended **31st March, 2014**, the Auditor **wanted to refer to the Minute Books**. The Board of Directors refused to show the Minute Books to the auditor.

(iii) **Conclusion:-**

- It is, therefore, **essential for the auditor to refer to the Minute Books**. In the absence of the **Minute Books**, the auditor **may not be able to vouch/verify certain transactions** of the company.
- **In case the directors have refused** to produce the **Minute Books**, the auditor may **consider extending the audit procedure** as also consider **qualifying his report** in any appropriate manner

54.

**Sec 164(2) - Disqualification of a Director**

One of the directors of Hitech Ltd. is attracted by the disqualification under Section 164(2) of the Companies Act, 2013. State auditor's responsibility in this regard.

Ans.



(i) **Provision:-** Section 143(3)(g) of the Companies Act, 2013

- Imposes a **specific duty on the auditor** to report **whether any director is disqualified** from being appointed as directors under **section 164(2)** of the Companies Act, 2013.
- The auditor has to ensure that **written representation** have been **obtained by the Board** from each director that one is not hit by Section 164(2).

(ii) **Conclusion:-** Since in this case, **one of the director is attracted by disqualification** under section 164(2) of the Act, the auditor shall **state in his report as per section 143** about the disqualification of the particular director.

55.

**Sec 164(2) - Disqualification of a Director**

Mr. X, a Director of KP Private Ltd., is also a Director of another company viz., GP Private Ltd., which has not filed the financial statements and annual return for last three years 2019-20 to 2021-22. Mr. X is of the opinion that he is not disqualified u/s 164(2) of the Companies Act, 2013, and auditor should not mention disqualification remark in his audit report. Comment as auditor of the company.

Ans.



(i) **Provision:-** Section 143(3)(g) of the **Companies Act, 2013** imposes a specific duty on the auditor to report **whether any director is disqualified** from being appointed as director **under section 164(2)** of the Companies Act, 2013.

(ii) **Section 164(2):-** If a director is already holding a directorship of a company which has **not filed the financial statements or annual returns** for any **continuous period of three financial years** shall not be eligible to be **reappointed** as a director of that **company** or **appointed in other company** for a period of **five years** from the date on which the said company fails to do so.

(iii) **In the given case:-** Mr. X is a director of **KP Private Ltd.** as well as of **GP Private Ltd.**, and, GP Private Ltd., has not filed the financial statements and annual return for **last three years**.

(iv) **Conclusion:-** Hence the provisions of **section 164(2)** are applicable to him and as such **he is disqualified from directorship** of KP private Ltd. Therefore, the auditor shall **report about the disqualification** under section 143(3)(g) of the Companies Act, 2013.

56.

**Audit of Government Companies**

What are the relevant sections of the Companies Act, 2013 and steps involved in auditor of Government Companies?  
 (Nov-2016, MTP-May/Nov-2018, MTP-May-2019, Nov-2019-New)

OR

Ceta Ltd is a company in which 58% of the paid up share capital is held by Rajasthan Government. The company is engaged in the business of providing consultancy services in relation to construction projects. The audit of the financial statements of Ceta Ltd for the financial year ended 31<sup>st</sup> March 2022 got completed with lot of intervention of Comptroller & Auditor General of India, wherein C&AG was giving directions to the auditors on the manner in which audit should be conducted in respect of certain areas. Further, it also received comments from C&AG on the audit report of the auditors. Ceta Ltd. is seeking advice to go against C&AG so that they can avoid unnecessary interference of C&AG. You are required to advise Ceta Ltd. with respect to role of C&AG in the audit of a Government company.  
 (MTP-May-2020)

Ans.



**Relevant Sections and Steps involved in Audit of Government Companies:** Section 143(5), 143(6) and 143(7) of the Companies Act, 2013 are relevant sections in case of Audit of Government Companies.

**The following steps are involved in the audit of government companies:**

- (i) **Appointment of Auditors under Section 139(5) and 139(7) read with section 143(5) of the Companies Act, 2013** - Statutory auditors of Government Company are **appointed or re-appointed** by the **Comptroller and Auditor General of India**. The C&AG may direct the appointed auditor the manner in which the accounts of the Government company are required to be audited and thereupon the auditor so appointed shall **submit a copy of the audit report** to the Comptroller and Auditor-General of India which, among other things, **include the directions**, if any, issued by the Comptroller and Auditor-General of India, the **action taken thereon** and **its impact** on the accounts and financial statement of the company.
- (ii) **Supplementary audit under section 143(6)(a) of the Companies Act, 2013** - The Comptroller and Auditor-General of India shall **within 60 days from the date of receipt** of the audit report have a **right to conduct a supplementary audit** of the financial statement of the company by such person or persons as he may authorize in this behalf; and for the purposes of such audit, require **information or additional information** to be furnished to any person or persons, so authorised, on such matters, by such person or persons, and in such form, as the Comptroller and Auditor-General of India may direct.
- (iii) **Comment upon or supplement such Audit Report under section 143(6)(b) of the Companies Act, 2013** - Any comments given by the **Comptroller and Auditor-General of India** upon, or supplement to, the audit report shall be **sent by the company to every person** entitled to copies of audited financial statements under **section 136(1) of the said Act** i.e. **every member** of the company, to **every trustee** for the **debenture-holder** of any debentures issued by the company, and to all persons **other than** such member or trustee, being the person so entitled and also be placed before the annual general meeting of the company at the same time and in the same manner as the audit report.
- (iv) **Test audit under section 143(7) of the Companies Act, 2013** - **Without prejudice** to the provisions relating to audit and auditor, **the Comptroller and Auditor-General of India** may, in case of any company covered under **section 139(5) or (7)** of the said Act, if he considers necessary, by an order, cause **test audit** to be conducted of the accounts of such company and the provisions of **the Comptroller and Auditor-General's (Duties, Powers and Conditions of Service) Act, 1971**, shall apply to the report of such **test audit**.

57.

**Audit of Government Companies - Supplementary Audit u/s 143(6)**

On receipt of statutory audit report on 30-04-2022 of M/S Sunlight Ltd., a government company. C & AG on 25-05-2022 appointed M/s Veeru & Associates to conduct supplementary audit u/s 143(6)(a) of the Companies Act, 2013. They submitted their report to C&AG as per their scope of work. The Company held its AGM on 01-09-2022 but directors did not think it necessary to discuss supplementary auditor's report and comment of the C&AG. Is the approach of the directors of Sunlight Ltd. correct ? Guide the company with the provisions related to supplementary audit.  
 (May-2019-New)

Ans.



- (i) **Provision:-** The CAG shall within 60 days from the date of receipt of the audit report have a right to,
- Conduct a **supplementary audit of the financial statement** of the company by such person or persons as **he may authorize in this behalf**; and for the purposes of such audit, require **information or additional information** to be furnished to any person or persons, so authorised, on such matters, by such person or persons, and in such form, as the CAG may direct; and
  - Comment upon or supplement such audit report:**  
Provided that any comments given by the CAG upon, or supplement to, the audit report shall be **sent by the company to every person** entitled to copies of audited financial statements **u/s 136(1)** i.e. **every member** of the company, to **every trustee** for the **debenture holders**, and to **all other entitled persons** and also be placed before the AGM of the company at the same time and in the same manner as the audit report
- (ii) **In view of above provisions:-** The approach of directors of **Sunlight Ltd.** is not correct. They are required to **mandatory send the Supplementary Audit Report** and **comments of C&AG** to every member of the company etc. as prescribed and also be **placed before the annual general meeting** of the company in the same manner as in case of audit report.
- (iii) **Conclusion:-** Since in the given case **neither the report has been distributed nor discussed** in the Annual General Meeting, the **directors of the company will be liable for contravention** of aforesaid sections.

58.

**Branch Audit**

D. Ltd., a Delhi based company having turnover of ₹ 25 crores, has a branch at USA having a turnover of ₹ 10 lakhs (as converted from US dollars). The area where the branch office is located in USA was severely affected by storms and the office along with all accounting records was completely destroyed. Due to the unavailability of records, the financial statements of D. Ltd, for the financial year 2021-22 did not include the figures pertaining to the said branch. As the statutory auditor of D. Ltd., how will you report on the same?

(Nov-2017)

Ans.



- (i) **Provision:- As per section 143(8)** of the Companies Act, 2013 if a company has a **branch office**, the accounts of that office shall be audited either by:
- The **auditor appointed for the company** (herein referred to as the company's auditor) under this Act or
  - Any other **person qualified for appointment** as an auditor of the company under this Act and appointed as such under section 139, or
  - Where the branch office is situated in a **country outside India**, the accounts of the branch office shall be audited either by
    - the **company's auditor** or
    - by **an accountant** or
    - by **any other person duly qualified** to act as an auditor of the accounts of the branch office in accordance with the laws of that country.
- (ii) **In the given case:-** D Ltd. is a Delhi based company, having **total turnover of ₹ 25 crores**. The company is having a **branch office in USA** (having a **turnover of rupees 10 lakhs** i.e. as converted from US dollars) in an area which is recently **affected by storm** and the office along with all **accounting records** was **completely destroyed**. Due to unavailability of records, the financial statements of D Ltd. for the financial year 2021 -22 **did not include** the figures pertaining to the said branch.
- (iii) **Conclusion:-** Under such a circumstance **beyond the control of the entity** when the entity's accounting records have been **destroyed** the **auditor's opinion has to be modified**. The auditor has also to **mention in his report** the effect on the financial statements **due to non-inclusion of financial data** pertaining to the branch.

59.

**Branch Audit**

Lakshya Ltd. has a branch office located outside India Company is in the process of appointment of non-Chartered Accountant as an auditor but otherwise qualified person from country where the branch office is situated. Statutory auditor is of the opinion that non-Chartered Accountant cannot be appointed as branch auditor. Comment.

You are also required to discuss the applicability of SA 600 using the work of another auditor by the head office auditor in regard to branch located outside India, if Non-Chartered Accountant is appointed?

(Answer involves SA-600 reference)

(RTP-May-2016)

Ans.



(i) **Provision:- As per section 143(8)** of the Companies Act, 2013 if a company has a **branch office**, the accounts of that office shall be audited either by:

- The **auditor appointed for the company** (herein referred to as the company's auditor) under this Act or
- Any other **person qualified for appointment** as an auditor of the company under this Act and appointed as such under section 139, or
- Where the branch office is situated in a **country outside India**, the accounts of the branch office shall be audited either by:
  - the **company's auditor** or
  - by **an accountant** or
  - by **any other person duly qualified** to act as an auditor of the accounts of the branch office in accordance with the laws of that country.

(ii) **As per Standard:-**

- **As per SA 600, "Using the work of another auditor:-** When the accounts of the branch are audited by a person other than the company's auditors, there is **need for a clear understanding of the role of such auditor and the company's auditor in relation to the audit of accounts of the branch and the audit of the company as a whole**. Also, there is great necessity for a proper rapport between these two auditors for the purpose of an effective audit.
- In recognition of these needs, the Council of the Institute of Chartered Accountants of India has dealt with these issues in SA 600, "Using the Work of another auditor". It makes clear that in certain situations, the statute governing the entity **may confer the right on the principal auditor to visit a component and examine the books of accounts and other records of the said component, if he thinks it necessary to do so**. Where another auditor has been appointed for the component, **the principal auditor would normally be entitled to rely upon the work of such auditor unless there are special circumstances to make it necessary for him to visit the component and/or to examine the books of accounts and other records** of the said component.
- Further, it requires that the principal auditor should perform **procedures to obtain sufficient appropriate audit evidence**, that the **work of the other auditor Is adequate for the principal auditors' purpose**, in the specific assignment.

(iii) **In the instant case:-** Lakshya Ltd. has a **branch office located outside India**. Company is in the process of appointment of **Non-Chartered Accountant as an auditor** but otherwise qualified person from country where the branch office is situated. Statutory auditor is of the opinion that non-Chartered Accountant cannot be appointed as branch auditor.

(iv) **Conclusion:-** Thus, a **Non- Chartered Accountant can be appointed** as an auditor of branch office located outside In. **Provided he is qualified for appointment as an auditor in that country.**

60.

**Requirement of Branch Audit**

A company has a branch office which recorded a turnover of ₹1,90,000 in the financial year 2021-22 No audit of the branch has been carried out. The statutory auditor of the company has made no reference of above branch in his report. The total turnover of the company is ₹10 crores for the year 2021-22. Comment

( MTP-Nov-2017)

OR

Alappa ltd. is a Chennai based company. The total turnover of the company is ₹10 crores for the year 2021-22. The company has a branch office at an area which was recently affected by tsunami. The transportation services are not available due to destruction caused by tsunami. The branch office recorded turnover of ₹ 2,50,000 in the Financial Year 2020-21. No audit of branch has been carried out. The statutory auditor of the company has made no reference of the above branch in his report. comment. **(RTP-May-2016)**

Ans.



- (i) **Provision:- As per section 143(8)** of the Companies Act, 2013 if a company has a **branch office**, the accounts of that office shall be audited either by:
- The **auditor appointed for the company** (herein referred to as the company's auditor) under this Act or
  - Any other **person qualified for appointment** as an auditor of the company under this Act and appointed as such under section 139, or
  - Where the branch office is situated in a **country outside India**, the accounts of the branch office shall be audited either by:
    - the **company's auditor** or
    - by **an accountant** or
    - by **any other person duly qualified** to act as an auditor of the accounts of the branch office in accordance **with the laws of that country**.
- (ii) **In the given situation:-** A company has a branch office which recorded a **turnover of ₹1,90,000** in the **financial year 2021-22** No audit of the branch has been carried out. The statutory auditor of the company has made no reference of above branch in his report. The total turnover of the company is **₹10 crores** for the year 2021-22. Comment
- (iii) **Conclusion:-**
- Therefore, if any office is described by the **company as branch office**, the company has to get its **branch audited by a person specified u/e 143(8)**.
  - **In case accounts of the branch has not been audited**, company's auditor is required to **mention this fact** in the audit report and **deal appropriately**.
  - In this case company's auditor is required to **state the fact of non-audit of branch office in his report** and deal appropriately

61.

#### Dispatch of Auditor's Report to Shareholders

The members of C. Ltd. preferred a complaint against the auditor stating that he has failed to send the auditor's report to them. Comment.

Ans.



- (i) **Provision:- Section 143** of the Companies Act, 2013 lays down the **powers and duties of auditor**.
- As per provisions of the law, **it is no part of the auditor's duty to send a copy of his report to members** of the company. The auditor's duty concludes once **he forwards his report** to the company.
  - It is the **responsibility of company** to send the report to every member of the company.
- (ii) **Case study:- In Re Allen Graig and Company (London) Ltd., 1934** it was held that duty of the auditor after having **signed the report** to be annexed to a Balance Sheet is confirmed only to **forwarding his report** to the secretary of the company.
- It will be for the **secretary or the director** to convene a **general meeting** and send the Balance Sheet and report **to the members** (or other person) entitled to receive it.
- (iii) **Conclusion:-** Hence in the given case, the **auditor cannot be held liable** for the failure to send the report to the shareholders.

62.

#### Right of Access of Company Auditor for Branch Records

M/s Seeman & Company had been the company auditor for Amudhan Company Limited for the year 2021-22. The company had three branches located at Chennai, Delhi and Mumbai. The audits of branches-Chennai, Delhi were looked after by the company auditors themselves. The audit of Mumbai branch had been done by

another auditor M/s Vasan & Company, a local auditor situated at Mumbai. The branch auditor had completed the audit and had given his report too. After this, but before finalization, the company auditor wanted to visit the Mumbai branch and have access to the inventory records maintained at the branch. The management objects to this on the grounds of the company auditor is transgressing the scope of audit areas agreed. Comment.

Ans.



- (i) **Provision:-** As per **Section 143(8)** of the **Companies Act, 2013** the audit of the branches can be done by:
- the **company auditor** himself or
  - by **another auditor**.
  - Even where, the branch accounts are audited, the company auditor **has right to visit the branch** if he deems it necessary to do so for the performance of his duties as auditor
    - He has also **right of access at all times** to the **books and accounts and vouchers** of the company maintained at the branch office.
    - **He can appropriately deal with the report** of the branch auditor in framing his main report.
    - **He will disclose** how he had dealt with the branch audit report.
- (ii) **In the given case:-** The audits of two branches were done by the company auditor and one branch was done by a separate branch auditor.
- (iii) **Conclusion:-**
- Applying the above provisions, to the instant case, **management's objection that the company auditor is transgressing the scope of audit areas agreed, is absolutely, wrong.**
  - The right of company auditor in visiting and accessing the records of branch **cannot be forfeited**.
  - Even where the branch accounts are **audited by another local auditor**, the company auditor has **right to visit the branch** and can have **access to the books and vouchers** of the company maintained at the branch office.

63.

#### **Appointment of Branch Auditor**

During the year 2021-22, it was decided for the first time that the accounts of the branch office of AAS Company Limited be audited by qualified Chartered Accountants other than the company auditor. Accordingly, the Board had appointed branch auditors for the ensuing year. One of the shareholders complained to the Central Government that the appointments was not valid as the Board of Directors do not have power to appoint auditors, be they Company Auditor or Branch Auditors?

Ans.



- (i) **Meaning of Branch:-** The **Companies Act, 2013** leaves it to the company **to designate or not to designate** any establishment of the company as '**branch office**'. Under the Companies Act, 2013, only establishment "**described as such by the company**" shall be treated as a 'branch office'.
- (ii) **Provisions:-**
- (a) **As per section 143(8)** of the Companies Act, 2013 if a company has a **branch office**, the accounts of that office shall be audited either by:
- The **auditor appointed for the company** (herein referred to as the company's auditor) under this Act or
  - Any other **person qualified for appointment** as an auditor of the company under this Act and appointed as such under section 139, or
  - Where the branch office is situated in a **country outside India**, the accounts of the branch office shall be audited either by
    - the **company's auditor** or
    - by an **accountant** or
    - by **any other person duly qualified** to act as an auditor of the accounts of the branch office in accordance with the **laws of that country** and the **duties and powers of the company's auditor** with reference to the **audit of the branch** and the **branch auditor**, if any, shall be such as may be prescribed.

**(b) Section 139(1) of the Companies Act, 2013:**

- Provides that **every company** shall, at the **first annual general meeting**, appoint an **individual or a firm** as an auditor who shall **hold office** from the conclusion of that meeting **till the conclusion of its sixth annual general meeting** and thereafter till the conclusion of every sixth meeting.
- The **shareholders** in general meeting, **instead of appointing branch auditor**, may **authorize the board of directors** to appoint branch auditors.

**(iii) In the present case:-** The board has appointed branch auditors **without obtaining authorization from the shareholders** in general meeting. The board had appointed the auditor where it did not have authority to do so.

**(iv) Conclusion:-** The **appointment is invalid**. The **shareholder's complaint is right**. The branch auditor should ascertain **before accepting the audit** whether his appointment is valid.

64.

**Branch Auditor's Report**

P Ltd. of whom you are the Statutory Auditor appoints M/s XYZ as Branch Auditors for one of its branches. M/s XYZ conducted the audit of the branch without visiting the branch and instead getting the books at the H.O. M/s XYZ has submitted their Branch Audit Report to you. Discuss whether to rely on branch auditor's report.

Ans.



**(i) Provision:-** As per section 143(8) of the Companies Act, 2013 if a company has a **branch office**, the accounts of that office shall be audited either by:

- the **company's auditor** or
- by **any other person duly qualified** to act as an auditor of the company.

**(ii) Rights of Branch Auditor:-**

- It is **not necessary** for branch auditor M/s XYZ to **visit the branch** and conduct the audit only at branch's premises.
- It is a **matter of professional judgement** for the branch auditor to decide as to whether he needs to visit the branch.
- At the same time, the statutory auditor **has the right to visit branch offices** and to **have access to the books of accounts and vouchers** maintained at the branch office in this case.

**(iii) In the present case:-** The **principal auditor** i.e. the statutory auditor of **Head Office P Ltd.** is entitled to **rely on the work of branch auditor** unless there are **special circumstances to make it essential for him to visit the branch** and examine the books of account and voucher records.

**(iv) As per Standard:-**

- As per SA 600, "Using the work of another auditor", the principal auditor is not required to **evaluate professional competence** because branch auditor happens to be member of ICAI.
- The statutory auditor is also required to deal with the **Branch Auditor's report** in the manner, he considers necessary.

**(v) Conclusion:-** Therefore, the statutory auditor is required to deal with **M/s XYZ's report in the manner it considers fit under the circumstances**.

65.

**Appointment of Branch Auditor**

Bhishm Limited decided to appoint Mr. Rajvir, chartered accountant, as the branch auditor for the audit of its Lucknow branch accounts for the year 2021-22. The decision to appoint branch auditor was taken by way of Board Resolution in the meeting of Board of Directors of the company, held in April 2021, subject to shareholders' approval in AGM of the company scheduled to be held in June 2021. Meanwhile, the Principal Auditor of the company raised an objection that the branch auditor cannot be appointed without his consent. Advise, whether the objection raised by company auditor is valid. **(RTP-Nov-2019)**

Ans.

**(i) Provisions:-** Section 143 (8) of the Companies Act, 2013, prescribes the **duties and powers of the company's auditor** with reference to the **audit of the branch** and the **branch auditor**.

- Where a company has a branch office, the accounts of that office shall be audited either by the



- **auditor appointed** for the company under this Act or
- by **any other person qualified** for appointment as an auditor of the company under this Act and appointed as such **under section 139**.
- In case of **subsequent appointment of auditor**, section 139(1) of the Act provides that **every company** shall, at the **first annual general meeting** appoint an **individual or a firm** as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting.
- (ii) **In the instant case:-** Bhishm Limited decided to appoint **Mr. Rajvir, chartered accountant**, as the **branch auditor** for the audit of its **Lucknow branch** accounts and the decision to appoint branch auditor was taken by way of **Board Resolution** in the meeting of **Board of Directors** of the company subject to **shareholders' approval in AGM** of the company.
- (iii) **Conclusion:-** Thus, **objection raised by company auditor is not valid** as per section 143(8) of the companies Act, 2013 and the **Board has authority** to appoint branch auditor but should be **approved by shareholders** in General Meeting.

66.

**Branch Audit**

ABC Ltd. having turnover of ₹ 100 crores during financial year 2021-22, need not get its branch audited whose turnover is ₹ 1.5 crores during the same year.

Ans.



- (i) **Provision:-** As per **section 143(8)** of the Companies Act, 2013 if a company has a **branch office**, the accounts of that office shall be audited either by:
  - The **auditor appointed for the company** (herein referred to as the company's auditor) under this Act or
  - Any other **person qualified for appointment** as an auditor of the company under this Act and appointed as such under section 139, or
  - Where the branch office is situated in a **country outside India**, the accounts of the branch office shall be audited either by:
    - the **company's auditor** or
    - by **an accountant** or
    - by **any other person duly qualified** to act as an auditor of the accounts of the branch office in accordance with the laws of that country.
- (ii) **Conclusion:-** ABC Ltd. has to get its branch audited.

67.

**Bank Audit – Audit Report & Reporting under Co. Act, 2013**

M/s GH & Associates have been appointed as Central Statutory Auditors of BNB Bank a nationalized bank, headquartered in New Delhi for the F.Y. 2021-2022. Bank functions in automated environment using “FLC Software”. While preparing audit report, one of the partner highlighted that some matters covered by Companies Act, 2013 and the requirements of Companies (Auditor's Report), Order, 2020 reporting. You are required to answer the following:

- (i) To which authority auditors should submit their audit report
- (ii) List the matters covered under Companies Act, 2013 and
- (iii) Reporting under Companies (Auditor's Report), Order, 2020.

(July-2021-New)

Ans.



- (i) **Authority to whom Auditors to submit their Audit Report -** In the case of a **nationalised bank**, the auditor is required to make a report to the **Central Government**. So, **GH & Associates, Central Statutory Auditors** of BNB Bank- a nationalized bank, would be required to submit their report to **Central Govt**.
- (ii) The auditor of a banking company is also required to state in the report the matters covered by Section 143 of the Companies Act, 2013.
  1. **Report on adequacy and operating effectiveness of Internal Controls over Financial Reporting** in case of banks which are registered as companies under the Companies Act in terms of **Section 143(3)(i) of the Companies Act, 2013** which is normally to be given as an **Annexure**

to the main audit report as per the Guidance Note on **Audit of Internal Financial Controls over Financial Reporting** issued by the ICAI.

2. **Report on whether any serious irregularity was noticed** in the working of the bank which requires immediate attention (**in accordance with sec 143(12) of the Companies Act, 2013.**)
3. **As per reporting requirements cast through Rule 11 of the Companies (Audit and Auditors) Rules, 2014** the auditor's report shall also include their views and **comments on the following matters**, namely:
  - (a) Whether the bank has disclosed the impact, if any, of the **pending litigations on its financial position** in its financial statements.
  - (b) Whether the bank has made **provision, as required under the law or accounting standards**, for material foreseeable losses, if any, on long term contracts including derivative contracts.
  - (c) Whether there has been **any delay in transferring amounts, required to be transferred to the Investor Education and Protection Fund** by the bank.
  - (d) (i) Whether the management has represented that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts, **no funds have been advanced or loaned or invested** (either from borrowed funds or share premium or any other sources or kind of funds) by the company to or in any other person(s) or entity(ies), including foreign entities ("Intermediaries"), with the understanding, whether recorded in writing or otherwise, that the Intermediary shall, whether, directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the company ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries;
  - (ii) Whether the management has represented, that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts, **no funds have been received by the company** from any person(s) or entity(ies), including foreign entities ("Funding Parties"), with the understanding, whether recorded in writing or otherwise, that the company shall, whether, directly or indirectly, lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Funding Party ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries; and
  - (iii) Based on such audit procedures that the auditor has **considered reasonable and appropriate in the circumstances**, nothing has come to their notice that has caused them to believe that the representations under sub-clause (i) and (ii) contain any material mis-statement.
  - (e) Whether the **dividend declared or paid** during the year by the company is **in compliance with section 123** of the Companies Act, 2013.
  - (f) [Whether the company, in respect of financial years commencing on or after the 1<sup>st</sup> April, 2022,] has used **such accounting software for maintaining its books of account** which has a feature of **recording audit trail (edit log) facility** and the same has been **operated throughout the year** for all transactions recorded in the software and the **audit trail feature has not been tampered** with and the audit trail has been preserved by the company as per the statutory requirements for record retention.

- (iii) Reporting requirements relating to the **Companies (Auditor's Report) Order, 2020** are **not applicable to a banking company** as defined in clause (c) of section 5 of the Banking Regulation Act, 1949.

68.

**Obligation of the Statutory Auditor to Report Frauds**

In the course of audit of Kishan Ltd. for the financial year 2021-22, its auditor M/s Zen & Co. observed that the management has passed certain forged transactions against the company amounting to ₹ 50 lakh at the year end. Suspecting fraud, the auditors requested explanations and documentary supporting, for which the management remained silent. You are required to guide the auditor of the company stating the fraud reporting requirements as provided under the Companies Act, 2013. **(MTP-May-2018)**

**OR**

You have been appointed statutory auditor of a company for the financial year ended 31<sup>st</sup> March, 2022 in place of the retiring auditor. During the course of audit. You observe that a fraud had been committed by a general manager who retired in March 2022. While going into further details. It was found that the fraud was going on since last 2-3 years and the total amount misappropriated was likely to exceed ₹ 100 lakhs. As statutory auditor, what would be your reporting responsibilities to the government? **(Nov-2017)**

**OR**

Write short note on: Obligation of the statutory auditor to report frauds to the Central Government during the audit carried out under the Companies Act, 2013. **(Nov-2015, MTP-May-2016)**

**OR**

An auditor observed a fraud committed by an employee of the company. State the manner and timing of reporting of the fraud by the auditor. **(MTP-Nov-2016, Nov-2016)**

**Ans.**

(i) **Provision:- As per section 143(12)** of the Companies Act, 2013,

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

- **In case of a fraud below ₹ 1 Cr.:-** The auditor shall report the matter to the **audit committee** constituted u/s 177 or **to the Board** in other cases within such time and in such manner as may be prescribed;
- The companies, whose **auditors have reported frauds** to the audit committee or the Board but **not reported to the Central Government**, shall **disclose the details** about such frauds in the **Board's report** in such manner as may be prescribed.

(ii) **Rule 13 of Companies (Audit and Auditors) Rules, 2014:-** Prescribes the **manner of Reporting of Frauds** in various cases.

- The auditor shall **report the matter to the CG as under:**
  - (a) the auditor shall report the matter to the **Board or the Audit Committee**, as the case may be, immediately **but not later than 2 days** of his knowledge of the fraud, seeking their reply or observations within 45 days;
  - (b) on receipt of such **reply or observations**, the auditor shall **forward his report** and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the CG within 15 days from the date of receipt of such reply or observations;
  - (c) in case the auditor **fails to get any reply or observations** from the Board or the Audit Committee within the **stipulated period of 45 days**, he shall forward his report to the **CG along with a note containing the details of his report** that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;
  - (d) the report shall be sent to the **Secretary, Ministry of Corporate Affairs** in a sealed cover by **Registered Post with Acknowledgement Due** or by **Speed Post** followed by an email in confirmation of the same;
  - (e) the report shall be on the **letter-head of the auditor** containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number; and
  - (f) the report shall be in the form of a statement as specified in **Form ADT-4**.

- **In case of a fraud below ₹ 1Cr:-** The auditor shall report the matter to **Audit Committee constituted u/s 177** or to the **Board** immediately but **not later than 2 days** of his knowledge of the fraud and he shall report the matter specifying the following:
  - (a) **Nature of Fraud** with description;
  - (b) **Approximate amount** involved; and
  - (c) **Parties involved**.
- The following details of each of the fraud reported to the **Audit Committee or the Board** during the year shall be **disclosed in the Board's Report:-**
  - (a) **Nature of Fraud** with description;
  - (b) **Approximate Amount** involved;
  - (c) **Parties involved**, if remedial action not taken; and
  - (d) **Remedial actions** taken.

69.

**Obligation of the Cost Auditor to Report Frauds**

RX Ltd. is a sugar manufacturing company. The company appointed Mr. Suresh, a practicing cost accountant, to conduct cost audit of its cost records under section 148 of the Companies Act, 2013. While conducting audit, Mr. Suresh found some misstatement resulting into fraud committed by the officers of the company amounting ₹1.5 crore. However, he did not report the matter to the Central Government believing that liability for such reporting lies only with statutory auditor of the company. Advise.

Ans.



- (i) **Provision:- As per section 143(12) & Rule-13** of the Companies Act, 2013, if an auditor of a company in the course of the performance of his duties as auditor, has **reason to believe** that an **offence of fraud**, which involves or is expected to involve individually an amount of **rupees 1 crore or above**, is being or has been committed **against the company** by its **officers or employees**, the auditor shall report the matter to the **Central Government**.
- (ii) **As per section 143(14):-** The provisions related to **reporting of fraud** shall also apply, **mutatis mutandis**, to a **cost accountant** conducting cost audit u/s 148 of the Companies Act, 2013.  
**Further As per section 143(15):-** If any **auditor, cost accountant, or company secretary** in practice does not comply with the provisions, **he shall,—**
- (a) **in case of a listed company**, be liable to a penalty of **five lakh rupees**; and
  - (b) **in case of any other company**, be liable to a penalty of **one lakh rupees**
- (iii) **Facts of the case:-** Mr. Suresh, being the cost auditor of RX Ltd., found misstatement resulting into fraud amounting ₹1.5 crore committed by the officers of the company. He was required to report the fraud to the Central Government.
- (iv) **Conclusion:-** As per above given facts and provisions Mr. Suresh is failed to perform his duties to report the fraud to C.G. **Further** he is also liable to a penalty of **five lakh rupees** (assumed listed company)

**5.6 - Section 144 Services not to be rendered by the Auditor**

70.

**Restricted Services**

Contravene Ltd. appointed CA Innocent as an auditor for the company for the current financial year. Further the company offered him the services of actuarial, investment advisory and investment banking which was also approved by the Board of Directors. Advise.

**(May-2015, Nov-2016, May-2018, MTP-May-2016, Nov-2017, Nov-2018, Nov-2019, Study Material)**

Ans.



- (i) **Provision:- Section 144** of the **Companies Act, 2013** prescribes certain services not to be rendered by the auditor. An auditor appointed under this Act shall provide to the company **only such other services as are approved by the Board of Directors** or the **audit committee**, as the case may be, but **which shall not include any of the following services** (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company), namely:

- **accounting and book keeping services;**
- **internal audit;**
- **design and implementation** of any financial information system;
- **actuarial services;**
- investment **advisory** services;
- investment **banking** services;
- rendering of **outsourced financial services;**
- **management services;** and
- **any other kind of services** as may be prescribed.

- (ii) **Disqualification:-** Section 141(3)(i) of the Companies Act, 2013 also disqualify a person for appointment as an auditor of a company **who is engaged as on the date of appointment** in consulting and specialized services **as provided in section 144.**
- (iii) **In the given case:-** CA Innocent was appointed as an auditor of **Contravene Ltd.** He was offered additional services of **actuarial, investment advisory and investment banking** which was also approved by the Board of Directors.
- (iv) **Conclusion:-** The **auditor is advised not to accept the services** as these services are specifically notified in the services not to be rendered by him as an auditor as per **section 144 of the Act.**

71.

**Section 141 & 144– Disqualification on Prohibited Services (Designing & Implementing FIS)**

CA P is providing the services of design and implementation of any financial information system to C Ltd. Later on, he was also offered to be appointed as an auditor of the company for the current year. Advise.

(Study Material)

Ans.



- (i) **Provision:-**
- **Section 141(3)(i) of the Companies Act, 2013**  
A person is **disqualified for appointment** as an auditor of a company **who is engaged as on the date of appointment** in consulting and specialized services as provided in section 144.
  - **Section 144 of the Companies Act, 2013**  
Certain services not to be rendered by the auditor which **includes Design and Implementation of any financial information system.**
- (ii) **In the above case:-** CA. P is providing the services of **Design and implementation** of any financial information system to C Ltd. Later on, **he was also offered to be appointed as an auditor** of the company for the current financial year.
- (iii) **Conclusion:-** Therefore, **CA. P is advised not to accept the assignment** of auditing as the service he is rendering is specifically notified in the list of services not to be rendered by him as per section 141(3)(i) read with section 144 of the Companies Act, 2013.

72.

**Prohibited Services**

M/s Duster & Co., Chartered Accountants, appointed as a statutory auditor of R Ltd. for the financial year 2021-22. The company is also in need of some actuarial services. Consequently, the Board of Directors of the company offered the same to M/s Srivastava & Co., an associate to M/s Duster & Co., which has been duly accepted by the firm. Comment.

Ans.



- (i) **As per Section 144 of Companies Act, 2013:-** An auditor appointed under this Act **shall not provide certain service**, directly or indirectly to the **company or its holding company or subsidiary company.** List of such services include **actuarial services.**
- (ii) **Section 141(3)(i) of the Companies Act, 2013:-** Disqualify a person **who, directly or indirectly, renders any service referred to in Section 144** to the company or its holding company or its subsidiary company.
- (iii) **Section 141(4) of the Act** provides that **where a person appointed** as an auditor of a company **incurs any of the disqualifications** mentioned in **section 141(3)** after his appointment, he **shall vacate his office** as such auditor and such vacation shall be deemed to be a **casual vacancy** in the office of the auditor.

- (iv) **In the given case:-** M/s Duster & Co., Chartered Accountants, was appointed as an auditor of R Ltd. and the company offered actuarial services to M/s Srivastava & Co., an associate to M/s Duster & Co., which has also been duly accepted by the firm.
- (v) **Conclusion:-** M/s Duster & Co. is **disqualified** to hold office as an auditor of R Ltd. u/s 141(3)(i), as its associate is involved in providing such services, to R Ltd, as mentioned in Section 144. Subsequently, M/s Duster & Co. shall have to vacate the office of auditor of R Ltd.

### 5.7 - Section 145 Signature on Audit Report

73. Mr. Rajendra, a fellow member of the Institute of Chartered Accountants of India, working as Manager of Shrivastav & Company, a Chartered Accountant firm, signed the audit report of Om Ltd. on behalf of Shrivastav & Company. Comment.

Ans.



#### Signature on Audit Report:

##### (i) Provision:-

- **Section 145** of the Companies Act, 2013 requires that the **person appointed as an auditor** of the company shall sign the auditor's report or sign or certify any other document of the company
- In accordance with the provisions of **section 141(2)** i.e. where a **firm including a limited liability partnership** is appointed as an auditor of a company, **only the partners who are chartered accountants** shall be authorized to act and sign on behalf of the firm.

##### (ii) Conclusion:

- **Mr. Rajendra**, a fellow member of the Institute and a **manager of M/s Shrivastav & Co.**, Chartered Accountants, **cannot sign on behalf of the firm** in view of the specific requirements of the Companies Act, 2013.

##### (iii) In case of contravention:

If any **auditor's report or any document** of the company is **signed or authenticated** otherwise than in conformity with the requirements of **Section 145**, the **auditor concerned** and the **person**, if any, other than the auditor **who signs the report or signs or authenticates** the document shall, **if the default is willful, be punishable with a fine.**

### 5.8 - Section 146 Auditor's Duty to attend General Meeting

74. **Auditor's Attendance at Annual General Meeting**  
The Board of Directors of a company have filed a complaint with the Institute of Chartered Accountants of India against their statutory auditors for their failing to attend the Annual General Meeting of the Shareholders in which audited accounts were considered. Comment.

Ans.



##### (i) Provision:- As per **Section 146** of the Companies Act, 2013,

- It is **right of the auditor** to **receive notices and other communications** relating to any general meeting and to be heard at such meeting, relating to the matter of his concern
- However, **it is duty of the auditor to attend the same** or through his authorised representative **unless otherwise exempted.**

##### (ii) In the instant case:- The **Board of Directors** of a company have **filed a complaint** with the Institute of Chartered Accountants of India against their statutory auditors **for their failing to attend the Annual General Meeting** of the Shareholders in which audited accounts were considered.

##### (iii) Conclusion:- In view of above discussed provisions of section 146, **the statutory auditor of the company should attend the general meetings** either through himself or through his authorised representative.

75. **Auditors to Attend General Meeting**  
Mr. Budha, Statutory Auditors of Secret Ltd. was not permitted by the Board of Directors to attend general meeting of the company on the ground that his right to attend general meetings is restricted only to those meetings at which the accounts audited by him are to be presented and discussed. Comment.

Ans.



- (i) **Provision:-** As per **Section 146** of the Companies Act, 2013, the auditor of a company are **under an obligation to attend any general meeting** of the company and not only those meetings **at which the accounts audited by them** are to be presented and discussed.
- (ii) **In the instant case:-** The board of directors of **Secret Ltd. have no right to restrict Mr. Buddha** from attending the general meeting and Mr. Buddha **has every right to attend such meeting** as conferred by Section 146.
- (iii) **Conclusion:-** The action of the board of directors is **contrary to the provisions of law** and **curtails the right of the auditor.**

76.

**Auditor's Duties w.r.t. Subsequent Events**

An auditor became aware of a matter regarding a company, only after he had issued his audit opinion. Had he become aware of the same prior to his issuing the audit report, he would have issued a different opinion.

**(Further refer SA 560)**

Ans.



- (i) **Provision:-** As per **Section 146** of the Companies Act, 2013, the auditor of a company are **under an obligation to attend any general meeting** of the company and not only those meetings **at which the accounts audited by them** are to be presented and discussed.
- (ii) **Analysis of the provision:**
- Provision required the auditors of a company **to attend the general meeting** of the company **unless otherwise exempted** by the company.
  - Auditor shall **have the right to be heard at such meeting** on any part of the business which concerns him as auditors.
  - The **discovery of a fact after issuance** of the financial statements that existed at the date of the audit report which **would have caused the revision** of the audit report, requires the auditor to **bring this to the notice of shareholders.**
  - **Further SA 560 "Subsequent Event"** also prescribes the procedures which the auditor is required to perform.
- (iii) **Conclusion:-** It will be **advisable for the auditor to attend the meeting** with a view to bringing to the **notice of the shareholders** the matter which came to his knowledge **subsequent to his signing the report** and **perform procedures** as per the **requirement of SA 560.**

**5.9 - Section 147 Penalty in case of Contravention**

77.

**Contravention by Management & Auditor in case of Appointment**

AB & Co. were appointed auditors for NOME Limited, a listed company, for the term of two five consecutive years from 2011-12, 2012-13, 2013-14, 2014-15, 2015-16, 2016-17, 2017-18, 2018-19, 2019-20, 2020-21 As per the provision of the section 139(2)(b) "No listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint an audit firm as auditor for more than two terms of five consecutive years".

Hence, Management of NOME Limited reached out (based on the recommendation of Audit Committee) to BCD & Co. for their nomination as the appointment of Statutory Auditor for the financial year 2021-22. However, BCD & Co. did not provide any written consent to such appointment neither they provided a certificate that the appointment, if made, shall be in accordance with the conditions laid in the Act and Rules therein.

Still the management went ahead and proposed an appointment in AGM and BCD & Co. were appointed as an auditor for the financial year 2021-22. Post appointment, those charged with governance identified that majority of the partners in the BCD & Co. are same which were there in AB & Co. Now, fearing the contravention of the provision of Companies Act, 2013. Management, on guidance of those charged with governance, decided to file a complaint with tribunal under section 140(5) of the Companies Act against statutory auditors.

You are required to guide the BCD & Co. regarding the contravention of the provisions of the Companies Act, 2013 with respect to appointment of Auditor.

**(RTP-Dec-2021)**

Ans.

**(i) Provisions:**

- As per section 139(1) of the Companies Act, 2013, **every company** shall, at the **first annual general meeting**, appoint an **individual or a firm as an auditor** who shall hold office from the conclusion of that meeting till the conclusion of its **sixth annual general meeting** and thereafter till the conclusion of **every sixth meeting** and the manner and procedure of selection of auditors by the members of the company at such meeting shall be such as may be prescribed.
- **It may be noted further** that before such appointment is made, the **written consent of the auditor to such appointment**, and a **certificate from him** or it that the appointment, if made, shall be in accordance with the conditions as may be prescribed, shall be **obtained from the auditor**.
- It may also be noted that the **certificate shall also indicate** whether the auditor satisfies the criteria provided in section 141 of the Companies Act, 2013.
- **Further, as per section 139(2)**, No listed company or a company belonging to **such class or classes of companies** as may be prescribed, shall appoint or re-appoint:
  - (a) an individual as auditor for **more than one term** of five consecutive years; and
  - (b) an audit firm as auditor for **more than two terms** of five consecutive years.
- **It may also be noted further that** as on the **date of appointment no audit firm having a common partner or partners** to the other audit firm, **whose tenure has expired** in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years:"

**(ii) In the current case:**

- While appointing the auditors of the company a **written consent** of the auditor to such appointment **was not obtained**.
- Moreover a **certificate from him** that the appointment if made shall be in accordance with the conditions laid down in the Act and Rules **was also not obtained**.
- Further, **majority of the partners of AB & Co. were partners in BCD & Co.** AB & Co. already served two terms of five consecutive years i.e., from 2012-13 to 2020-21 as a statutory auditor of the company.

**(iii) Conclusion:**

- Hence, **BCD & Co. were not eligible to be appointed as an auditor of NOME Limited** as all partners of BCD & Co are partner of AB & Co. who have **already served two terms** of five consecutive years as an auditor of NOME Limited.
- Since, before the appointment of Statutory Auditor, the **management should have obtained the required certification and written consent** from BCD & Co., therefore, **in this case both, the management and the auditors have contravened** the provision of the Companies Act, 2013

**(iv) Penalty- (Section 147)**

- As per section 147 of Companies Act will be applicable i.e. if any of the provisions of sections 139 to 146 (both inclusive) is contravened,
- the **company** shall be punishable with **fine** which **shall not be less than twenty-five thousand rupees** but which may extend to **five lakh rupees** and
- **every officer of the company** who is in default shall be punishable with fine which shall **not be less than ten thousand rupees** but which may **extend to one lakh rupees**.
- If an auditor of a company contravenes **any of the provisions of section 139, section 144 or section 145**, the auditor shall be **punishable with fine** which shall **not be less than twenty-five thousand rupees**, but which may extend to **five lakh rupees** or **four times the remuneration** of the auditor, **whichever is less**.

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

## 5.10 - Section 148 Cost Audit &amp; Cost Audit Rules

78.

**Cost Records & Cost Audit Rules**

Petro Ltd. is engaged in generation of electricity for captive consumption through Captive Generating Plant. The Company also maintains cost records in its books of account as required under Cost Records and Audit Rules. Mr. Xylo, friend of Managing Director of the Company, suggested name of his brother, who is a Cost accountant, for the purpose of cost audit. However, the statutory auditor of the company, is of the view that the Company is not legally required to conduct cost audit. Now, the Managing Director is in dilemma about the requirement of cost audit. Being an expert in cost records and audit rules, you are required to guide in this regard.  
**(RTP-Nov-2020) (RTP-May-2017)**

Ans.



**(i) Provision:- Section 148 of the Companies Act, 2013 read with the Companies (Cost Records and Audit) Rules, 2014.**

- The provisions relating to **cost records and audit** are governed by **section 148** of the **Companies Act, 2013** read with the **Companies (Cost Records and Audit) Rules, 2014**.
- **The audit conducted** under this section shall be in **addition** to the audit conducted under **section 143**.

**(ii) As per Rule:-** Rule 3 of the **Companies (Cost Records and Audit) Rules, 2014** provides the **classes of companies**, engaged in the **production of goods or providing services**, required to include cost records in their books of account.

**Exception:-** The requirement for cost audit under these rules **shall not be applicable to a company which is covered under Rule 3**, and,

- Whose **revenue from exports**, In foreign exchange, **exceeds 75 per cent of its total revenue**; or
- Which is **operating from a special economic zone**.
- Which is **engaged in generation of electricity** for captive consumption through Captive Generating Plant.

**(iii) In the Instant case:-** Petro Ltd. is **engaged in generation of electricity for captive consumption through Captive Generating Plant**. The Company also maintains **cost records in their books of account** as required under Cost Records and Audit Rules. **Mr. Xylo, friend of Managing Director** of the company, suggested **name of his brother**, who is a **Cost accountant**, for the purpose of cost audit. However, the statutory auditor of the company is of the view that the company is not legally required to conduct cost audit. Now, the Managing Director is in dilemma about the requirement of cost audit.

**(iv) Conclusion:-** Petro Ltd. is engaged in generation of electricity for captive consumption through Captive Generating Plant. **Therefore, Petro Ltd. is not required to conduct cost audit** as it is falling under the **exemption criteria**. Hence, the opinion of statutory auditor of the company regarding non-applicability of cost audit is correct and the management should follow the same.

79.

**Cost Audit Rules**

Pearl Ltd. is an exporter of precious and semi-precious stones. The turnover of the company is ₹ 150 crore, out of which ₹ 105 crore is from export business and remaining ₹ 45 crore from domestic sales. Amount received from export business is all in foreign currency. Directors of Pearl Ltd. are of the opinion that cost audit is not applicable to their company as maximum revenue has been generated from export business. Give your opinion.  
**(May-2019-New, Study Material)**

Ans.



**(i) Provisions:-** Provisions relating to cost audit are governed by **section 148** of the Companies Act, 2013 read with the **Companies (Cost Records and Audit) Rules, 2014**.

**(a) Applicability of Cost Audit:-** Rule 4 of **Companies (Cost Records and Audit) Rules, 2014** requires audit of cost records in case of **non-regulated sector industries** if

- Annual **turnover from all products and services** in immediately preceding financial year is **₹ 100 Cr. or more** and
- The turnover of **individual product or service** is **₹ 35 Cr. or more**.

- (b) **Exception:-** The requirement for cost audit shall not be applicable to a company
- Whose **revenue from exports**, in foreign exchange, exceeds **75 per cent of its total revenue**,
  - Which is **operating from SEZ** and
  - Which is engaged in the **generation of electricity for captive consumption** through captive generating plant.
- (ii) **In the instant case:- Pearl Ltd. is an exporter** of precious and semi-precious stones and the turnover of the company is rupees 150 crore out of which rupees 105 crore i.e. **70% is from export business** and remaining rupees 45 crore i.e. 30% from domestic sales. It is neither operating from SEZ nor involved in captive power generation.
- (iii) **Conclusion:- Thus, opinion of director is not tenable** as **revenue from exports** in foreign exchanges is **below prescribed limit**. Therefore, cost audit is applicable on Pearl Ltd. as per Rule 4 of the Companies (Cost Records and Audit) Rules, 2014. **Pearl Ltd. has to appoint cost auditor** to get the cost accounts of the company audited.

80.

**Cost Audit Rules**

Mithas Ltd is a top sugar manufacturer and exporter in India operating from Noida Specific Economic Zone, Uttar Pradesh Its revenue from sale/export for the current year is given below:

Sale within India	₹153 lakhs
Sale outside India (Export)	₹357 lakhs
Total Revenue	₹510 lakhs

Mr X, the statutory auditor of Mithas Ltd, is of the view that the company is mandatorily required to include cost records in their books of account and consequently conduct cost audit. He also suggested the name of his friend, who is a Cost accountant, for the purpose of such cost audit. However, the management is of the view that the company neither required including cost records in their books of account nor conduct cost audit. Being an expert in cost records and audit rules, you are required to guide the management in this regard.

(RTP-Nov-2015)

Ans.



- (i) **Provision:-** The provisions relating to **cost records and audit** are governed by **section 148 of the Companies Act, 2013** read with the **Companies (Cost Records and Audit) Rules, 2014**. The audit conducted under this section **shall be in addition** to the audit conducted under section 143.
- (ii) **Rule 3 of the Companies (Cost Records and Audit) Rules, 2014:-** Provides the **classes of companies**, engaged in the **production of goods or providing services**, required to include **cost records in their books of account**. The said rule has **divided the list of companies into regulated sectors and non-regulated sectors**.
- Company **belonging to sugar industry** is one of the types of companies **prescribed under the regulated sectors**. However, the requirement for **cost audit** under these rules **shall not be applicable to a company which is covered under Rule 3, and**,
- (1) whose **revenue from exports**, in foreign exchange, **exceeds 75 percent** of its total revenue; or
  - (2) which is **operating from a special economic zone**.
- (iii) **In the given case:- Mithas Ltd., a sugar manufacturer and exporter in India**, is operating from **Noida Specific Economic Zone, Uttar Pradesh**.
- (iv) **Conclusion:-** Therefore, **Mithas Ltd. is required to include cost records** in their books of account in accordance with **Rule 3 of the Companies (Cost Records and Audit) Rules, 2014**. However, the company is **not required to conduct cost audit** as it is operating from a **special economic zone**. **The facts given on revenue are not relevant here.**

81.

**Appointment of Cost Auditor**

Expro Ltd. is engaged in the production of steel. A Chartered Accountant Firm 'M/s Manan & Co.' was appointed as the statutory auditor of Expro Ltd. for the current financial year. During the year, the management of the company realised that the company is required to maintain cost records in their books of

account and get it audited. Therefore, in a general meeting, the members of the company appointed M/s Manan & Co. as the cost auditor of the company. You are required to examine the validity of appointment of M/s Manan & Co, as the cost auditor  
**(RTP-May-2016)**

Ans.



- (i) **Provision:-** According to **section 148(3) of the Companies Act, 2013** read with Companies (Audit & Auditors) Rules, 2014
- **In the case of companies which are required to constitute an audit committee:-** The Board shall appoint an **individual, who is a cost accountant, or a firm of cost accountants in practice**, as cost auditor on the recommendations of the Audit committee;
  - **In the case of other companies which are not required to constitute an audit committee:-** The Board shall appoint an individual who is a cost accountant or a firm of cost accountants in practice as cost auditor.
  - It is also provided that **no person appointed under section 139** as an auditor of the company **shall be appointed for conducting the audit of cost records.**
- (ii) **In the given case:-** The members of **Expro Ltd. appointed M/s Manan & Co.**, a practicing Chartered Accountant Firm and the **statutory auditor of the company, as the cost auditor.**
- (iii) **Conclusion:-** Therefore, the **appointment of the CA firm as cost auditor made by the company is not valid.** The Board shall appoint a cost accountant or a firm of cost accountants in practice to conduct such cost audit.

82.

### Cost Auditor - Certificate

On 30.08.2021, the Board of SRE Ltd. proposed to appoint Mr. Elex, a Cost accountant, for conducting cost audit for the financial year 2021-22. The management came to know about the certificate which needs to be obtained from the auditor before such appointment is made. However, the management is unaware about what certification is required from the auditor. Please guide.

Ans.



**As per Rule 6 of Companies (Cost Records and Audit) Rules, 2014:-** Companies required to get the **cost records audited**, shall **within 180 Days** of the commencement of every financial year, appoint a cost auditor. Before such appointment is made, the **written consent of cost auditor** to such appointment and a certificate from him or it shall be obtained.

**The Cost Auditor appointed shall submit certificate that-**

- The **individual or the firm**, as the case may be, is **eligible for appointment** and is **not disqualified** for appointment under the Act, the **Cost and Works Accountants Act, 1959** and the **Rules or regulations** made there under.
- The **individual or the firm**, as the case may be, **satisfies the criteria provided in Sec. 141**, so far as may be applicable.
- The proposed appointment is **within the limits** laid down by or under the authority of the Act.
- The **list of proceedings against the cost auditor** or audit firm or any partner of the audit firm pending with respect to **professional matters of conduct**, as disclosed in the certificate, is true and correct.

83.

### Submission of Cost Audit Report

Elucidate the provisions relating to submission of Cost Audit Report to the Board and the Central Government as per the Companies Act, 2013.

Ans.



- As per Section 148(5) of Companies Act 2013:-** The cost auditor to submit the report on the audit of cost records to the Board of Directors of the company.
- As per Section 148(6) of Companies Act 2013:-** The company shall **within 30 days** from the **date of receipt** of a copy of the cost audit report **furnish the Central Government** with such report along with full information and explanation on every reservation or qualification contained therein.
- Section 148(7) of Companies Act, 2013** provides that if, after considering the **cost audit report** and the **information and explanation** furnished by the company, the **Central Government** is of the opinion that any **further information or explanation** is necessary, it may call for such further

information and explanation and the **company shall furnish the same** within such time as may be specified by that Government.

(iv) **Rule 6 of Companies (Cost Records and Audit) Rules, 2014:-** Provides the following in this regard:

- **Every cost auditor**, who conducts an audit of the cost records of a company, **shall submit the cost audit report** along with his or its reservations or qualifications or observations or suggestions, if any, **in, Form CRA-3**.
- **Every cost auditor** shall forward his report to the **Board of Directors** of the company within a period of **180 days from the closure** of the **financial year** to which the report relates and the Board of Directors shall **consider and examine such report** particularly any reservation or qualification contained therein.
- **Every company** covered under these rules shall, within a period of **thirty days from the date of receipt** of a copy of the cost audit report, furnish the **Central Government** with such report along with **full information and explanation** on every **reservation or qualification** contained therein, in **Form CRA-4** along with specified fees.

## Notes




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## UNIT-2 : BOOK OF ACCOUNTS (SECTION 128 TO 138)

### 5.11 -Section 128 Books of Account

- 84. Proper Books of Account Not Maintained**  
 When can a company be said to have 'Not maintained' proper books of account? What is the role of the statutory auditor for the same?
- OR**
- Write short note on: Proper Books of Accounts as per Companies Act, 2013 **(May-2017)**
- OR**
- The auditor report of company states that proper books of accounts as required by law have been maintained by the company. What is the role of statutory auditor of the company, when a company be said to have not maintained proper books of account? **(May-2015)**

- Ans.**
- 

**(i) Provisions:-**

(a) **As per Section 128** of the Companies Act, 2013,


  - Every company shall **prepare and keep** at its **registered office** books of account and
  - **Other relevant books and papers** and financial statement for every financial year
  - Which give a **true and fair view** of the **state of the affairs** of the company, including that of **its branch office or offices**, if any, and
  - Explain the transactions **effected both at the registered office and its branches** and such books shall be kept on **accrual basis** and according to the **double entry system** of accounting.

(b) **Section 143(3)(b)** of Companies Act, 2103 requires that the auditor's report shall state whether:

  - In his opinion, **proper books of account as required by law have been kept** by the company so far as appears from his examination of those books and
  - **Proper returns adequate** for the purposes of his audit **have been received** from branches not visited by him.

**(ii) Conclusion:-** The Auditor is required to **check that the company has complied with all the provisions** related to **maintenance of books of accounts** prescribed under **section 128**. If the statutory auditor finds that the books are **not maintained properly**, he will have to **modify his report** and shall **state the reasons** for the same.

- 85. Preparation of Financial Statements**  
 Ganga-Kaveri Project Ltd. was incorporated on 1.7.2022. During the year ended 31.3.2023 there was no manufacturing or trading activity except raising of share capital, purchase of land, acquisition of plant and machinery and construction of factory sheds. Therefore the Chief Accountant of the company contends that for the relevant year there was no need to prepare a statement of profit or loss or any other statement except a Balance Sheet as at 31.3.2023. Comment as an auditor. (Date restated)

- Ans.**
- 

**(i) Provision:-** Section 128 of the Companies Act, 2013 requires

  - **Every company** to prepare its financial statements for **every financial year**
  - Which gives a **true and fair view** of the state of the affairs of the company and
  - Such books shall be **kept on accrual basis**, and
  - According to the **double entry system** of accounting.

**(ii) Financial Statement definition:-** As per **section 2(40)** of the Companies Act, 2013, includes

  - balance-sheet,
  - statement of profit and loss,
  - cash flow statement,
  - a statement of change in equity, if applicable and explanatory note as annexure.

- (iii) **In the given case:-** Ganga-Kaveri Project Ltd. did not carry any **manufacturing or trading activity** except raising of share capital, purchase of land, acquisition of plant and machinery, etc.  
 Though the company did not carry any manufacturing or trading activity, the company has **carried on certain activities like** construction of factory shed, acquisition of plant and machinery etc. In such a case, it is necessary to provide for depreciation and other expenses.
- (iv) **Conclusion:-** The mere fact that there was no manufacturing or trading activity **cannot be the basis for not preparing the Statement of Profit and Loss**. Therefore, the **contention of the Chief Accountant is not correct**.

86. **Shifting of Books of Account**  
 X Ltd. has its Registered Office at Mumbai. During the current accounting year it shifted its Corporate Office to Delhi. The Managing Director of the Company wants to shift company's books of account to Delhi because he holds the view that there is no legal bar in doing so. Comment.


- Ans. (i) **Provision:- As per section 128(1)** of The Companies Act 2013,
- Every company shall keep at **its registered office** proper books of accounts.
  - **It is permissible**, however, for **all or any of the books** of accounts
  - To be kept at **such place in India** as the **Board of Directors may decide** but, when a decision in this regard is taken, the company must file **within 7 days** of such decision with the **Registrar of Companies** a notice in writing giving **full address** of the other place.
- (ii) **Conclusion:-** In view of the above provisions, **X Ltd should maintain its books of account at its registered office at Mumbai**. The Managing Director is **not allowed to shift its books** of account to Delhi **unless decision in this behalf is taken** by the Board of Directors and a **notice is also given** to the Registrar of Companies in form AOC 5.

87. **Right to Lien**  
 Write short notes on - Auditor's right to Lien as per Companies Act, 2013. (May-2017)


- Ans. (i) **Auditor's Right to Lien & Books of accounts**
- **Definition:-** Lien refers to the right of a person for lawful possession of somebody's else property on which he has worked.
  - Right of lien is exercised for **non-payment of his dues** for the work done.
  - The auditors **can exercise right of lien** on the client's books and documents in his possession for non-payment of fees by the client, for the work done on the books and documents.
  - **In respect of auditor exercising the lien**, The Institute of Chartered Accountants of England and Wales has **expressed a similar view subject to the following conditions**:
    - (a) Documents must belong to the client who owes the money,
    - (b) These documents must come to the possession of the auditor on the client's authority.
    - (c) The auditor can retain such documents, only if he has done work on such documents, on which fees have not been paid.
- (ii) **As per Provision:-** Under **section 128** of the Act, books of account of a company **must be kept at the registered office**. These provisions ordinarily **make it impracticable** for the auditor **to have possession of the books** and documents. The company provides reasonable facility to auditor for inspection of the books of account by directors and others authorised to inspect under the Act.
- (iii) **As per Ethical Standard Board of ICAI:-** A chartered accountant **cannot exercise lien over the client documents/records** for non-payment of his fees.
- (iv) **Conclusion:-** Taking an overall view of the matter, it seems that though legally, **auditor may exercise right of lien** in cases of companies, **it is mostly impracticable for legal and practicable constraints**. His working papers being his own property, the question of lien, on them does not arise.

## 5.12 -Section 129 Financial Statements

88. **Applicability of AS/Ind AS**  
 As an auditor of a company registered under section 8 of the Companies Act, 2013 you find that as per the notification of the ministry of Corporate Affairs regarding applicability of Indian Accounting Standards (Ind-AS). The company has to prepare its financial statements for the year ended 31st March, 2022 under Ind-AS. The management of the company is however of the strong view that being a section 8 company having charitable objects, Ind-AS cannot apply to the company. The financial statements are therefore prepared by the management under the earlier GAAP and a note for the same is given in the financial statements. How would you report on these financial statements? **(Nov-2017), (Nov-2019)**

- Ans.**
- 
- (i) **Provision:- Section 129(1)** of the Companies Act, 2013, governs the requirements to be satisfied by financial statements. **The provisions there under which should be complied with are:**
- Financial statements shall, **give a true and fair view** of the state of affairs of the company or companies as at the end of financial year, comply with the notified **accounting standards under section 133** and be in such form or forms specified in **Schedule III to the Companies Act, 2013** and
  - The items contained in such financial statements shall be in accordance with the accounting standards.
- (ii) **AS notified by Central Government:-** As per **section 133** of the Companies Act, 2013, the Central Government has notified **Companies (Indian Accounting Standards) Rules, 2015** dated 16.02.2015 in exercise of the **powers conferred by section 133**.
- (iii) **Companies (Indian Accounting Standards) Rules, 2015:-**
- The said rules list the Indian Accounting Standards (Ind AS) and the **class of companies required to comply with the Ind AS** while preparation of their **financial statements**.
  - Here, it may be noted that the **companies covered under Section 8 are required to comply the provisions** of the **Companies Act, 2013**, unless and until any exemption is provided.
  - Companies registered under **Section 8 are not exempted from the requirements** of **section 133** and **section 129** of the Companies Act, 2013.
- (iv) **Conclusion:-** In the given case, only **contention of management that being a section 8 company** having charitable object, **Ind-AS cannot apply to the company**, therefore financial statements prepared under the **earlier GAAP** and a **note for the same is given, is not tenable**.  
 However, the auditor is required to **ensure the applicable monetary limits w.r.t Ind-AS** and need to advise the management to prepare the financial statements as per Ind-AS accordingly. **In case of non-compliance the auditor should report accordingly.**

89. **Depreciation ignoring Schedule II to the Co. Act, 2013**  
 XYZ Limited has prepared the financial statements for the year 2021-22 and mentioned in the significant accounting policies that depreciation on tangible fixed assets is provided on the straight line method over the useful lives of the assets as estimated by the management. The company has ignored the useful life of the assets mentioned in Schedule II of the Companies Act, 2013. As a statutory auditor of the company how would you deal with this ? **(Nov-2020-Old)**

- Ans.**
- 
- (i) **Section 129 of the Companies Act, 2013**, requires that the financial statements **shall give a true and fair view** of the state of affairs of the company and **are in compliance with Accounting Standards**.
- (ii) **As per Schedule II to the Companies Act, 2013:-** on 'Useful Lives to Compute Depreciation', the useful life of an asset shall not ordinarily be different from the useful life specified therein.
- (iii) However, if such a company uses a useful life of the asset **which is different from the above limits**, it shall disclose the **justification for the same** in its financial statement
- (iv) **In the given case:-** M/s IT Limited has **mentioned in the significant accounting policies** that the depreciation on **tangible fixed assets is provided on the straight line method** over the useful lives

of the assets as estimated by the management and ignored the useful lives of the assets as provided under Schedule II to the Companies Act, 2013.

- (v) **Conclusion:-** Therefore, **the statutory auditor of the company should ensure that the management has disclosed the justification** for consideration of different useful life of the assets from that as indicated **under Schedule II**. If the justification has not been provided then the auditor of the company shall suggest the management for the same and **if management refuses**, the auditor **should qualify his report** accordingly.

90.

#### Deviations from Accounting Standards

State the disclosure required to be made in the financial statements if these do not comply with the accounting standards.

Ans.



**Provision:-** As per **Section 129(5)** of the Companies Act, 2013, if the financial statements of a company **do not comply with the accounting standards**, the company shall **disclose in its financial statements** the following namely-

- The **deviation** from the accounting standards,
- The **reasons for such deviation**, and
- The **financial effects**, if any, arising out of such deviation.

91.

#### Audit report - Wrong anticipation of Tax Liability & Provision not made

ABC Ltd. has been dealing in tyres since 1995. The Company envisaged to expand its business and wanted to manufacture the tyres besides trading. Accordingly, the machinery imported, installed and manufacturing operations commenced. The Government also gave certain incentives like power subsidy, land acquisition subsidy, etc. After 2 years of operations, Company received a notice from the Income Tax authorities to pay tax on incentive received in the form of power subsidy. The demand notice was served for ₹ 150.00 Lakhs. The Company, however filed an appeal with higher tax authorities against the demand and the matter is undecided as on 31.03.2022.

Legal team of the Company anticipated that tax liability might mature. The Company has not made a provision of anticipated tax liability. Considering the provisions of Companies Act, 2013, how an auditor of ABC Ltd. should see this matter and report in audit report, if required? **(July-2021-New)**

Ans.



The Council of the **Institute of Chartered Accountants of India** has taken note of the fact that there is a practice prevalent whereby companies **do not make provision for tax** even when **such a liability is anticipated**. It has expressed the view that on an overall consideration of the relevant provisions of law, **non-provision for tax** (where a liability is anticipated) would amount to **contravention of the provisions of Sections 128 and 129 of the Companies Act, 2013**. Accordingly, it is necessary for the auditor to **qualify his report** and such qualification should bring out the manner in which the accounts do not disclose a “**true and fair**” view of the state of affairs of the company and the profit or loss of the company.

**Conclusion -Applying the above to the facts given in the question:** - auditor should **qualify his report**.

An example of the manner in which the report on the **balance sheet** and the **Statement of Profit and Loss** may be **qualified** in this respect is given below:

*“The company has not provided for taxation in respect of its profits and the estimated aggregate amount of taxation not so provided for is ₹ .....including.....for the Year ended on .....To the extent of such non-provision for the year, the profits of the Company for the financial year under report have been overstated and to the extent of such aggregate non-provision, the reserves of the company appearing in the said balance sheet have been over-stated and the current liabilities and provisions appearing in the said balance sheet have been understated”*

#### 5.13 - Section 130 Re-opening of Accounts on Court's or Tribunal's orders

92.

#### Recasting of FSs - Re-opening of Accounts on Court's or Tribunal's orders

M/s ALM Ltd. is into the business of trading of toys since 2001. The company was performing well till year 2017 and after that sales started showing downward trend. The Company had borrowed \ working capital funds from LP Bank Ltd. On 01.08.2022, account of the borrower was classified as NPA. Bank appointed

forensic auditor, to identify, if any diversion of funds is there or not. Forensic auditor confirmed the diversion of funds. Matter went to the court of law and company was asked to recast its financial statements for the last 5 years. Management contended that Companies Act, 2013 does not allow recasting for more than three preceding financial years. Do you agree with the views of the management?

(July-2021-New, MTP-Nov-2022)

Ans.



(1) **Provision Section 130 of the Companies Act, 2013** states that a company shall **not re-open its books of account and not recast its financial statements**, unless an application in this regard is made by the **Central Government, the Income-tax authorities, the Securities and Exchange Board of India (SEBI)**, any other statutory regulatory body or authority or any person concerned **and** an order is made by a **court of competent jurisdiction** or the **Tribunal** to the effect that—

- (i) the relevant earlier accounts were prepared in a **fraudulent manner**; or
- (ii) the **affairs of the company were mismanaged** during the relevant period, casting a doubt on the reliability of financial statements.

The Order for reopening of accounts **not to be made beyond eight financial years** immediately preceding the current financial year **unless** and until Government has, under Section 128(5), **issued a direction for keeping books of account longer than 8 years**, reopening of accounts can be made for such longer period.

However, **a notice shall be given by the Court or Tribunal** in this regard and shall take into consideration the representations, if any.

(2) **Conclusion:** -Keeping in view above, the **contention of the ALM Ltd that the Companies Act, 2013 does not allow recasting for more than three preceding financial years is incorrect.**

#### 5.14 -Section 132 NFRA

93.

**Companies and Bodies Corporate governed by NFRA**

M/s PC & Co., Chartered Accountants are the statutory auditors of various categories of companies and bodies corporate. In exercise of the powers conferred under sub-sections (2) and (4) of section 132, of the Companies Act, 2013 the Central Government made the National Financial Reporting Authority Rules, 2018 (NFRA Rules) (MCA Notification dated 13 November 2018). The audit firm seeks your guidance on the applicability of those categories of companies and bodies corporate which are covered by NFRA Rules.

(Nov-2020-New)

Ans.



- (a) **Companies whose securities are listed** on any stock exchange in India or outside India;
- (b) **Unlisted public companies**
  - having paid-up capital of **not less than ₹500 crores** or
  - having annual turnover of **not less than ₹1,000 crores** or
  - having, in aggregate, outstanding loans, debentures and deposits of **not less than ₹500 crores as on the 31st March** of immediately preceding financial year;
- (c) **Insurance companies, banking companies, companies engaged in the generation or supply of electricity, companies governed by any special Act** for the time being in force or bodies corporate incorporated by an Act in accordance with clauses (b), (c), (d), (e) and (f) of sub-section (4) of section 1 of the Act;  
 Explanation – Banking company includes ‘corresponding new bank’ as defined in respective acts.
- (d) **Any body corporate or company or person**, or any class of bodies corporate or companies or persons, on a reference made to the Authority by the Central Government in public interest; and
- (e) **A body corporate** incorporated or registered outside India, which is a subsidiary or associate company of any company or body corporate incorporated or registered in India as referred to in clauses (a) to (d), if the income or net worth of such subsidiary or associate company **exceeds 20% of the consolidated income or consolidated net worth** of such company or the body corporate, as the case may be, referred to in clauses (a) to (d).

94.

**Applicability of NFRA**

You are doing audit of unlisted public limited company, Perfect Limited As per National Financial Reporting Authority Rules, 2018, NFRA has power to monitor and enforce compliance with accounting standards and auditing standards, oversee the quality of service under sub-section (2) of section 132 or undertake investigation under sub-section (4) of such section, of the auditors. Discuss about the class of companies and bodies corporate, where NERA is applicable. **(July-2021-Old)**

**Ans.**

As per NFRA rules, NFRA shall have **power to monitor and enforce compliance with accounting standards and auditing standards**, oversee the quality of service under subsection (2) of section 132 or undertake investigation under sub-section (4) of such section of the **auditors of the following class of companies and bodies corporate**:

- (a) Companies **whose securities are listed on any stock exchange** in India or outside India;
- (b) **Unlisted public companies** having:
  - **Paid-up capital of not less than rupees five hundred crores** or
  - Having **annual turnover of not less than rupees one thousand crores** or
  - Having, in aggregate, outstanding loans, debentures and deposits of **not less than rupees five hundred crores** as on the 31st of March of immediately preceding financial year;
- (c) **Insurance companies, banking companies, companies engaged in the generation or supply of electricity, companies governed by any special Act** for the time being in force or bodies corporate incorporated by an Act in accordance with clauses (b), (c), (d), (e) and (f) of section 1 (4) of the Companies Act, 2013; "Explanation.- For the purpose of this clause, "banking company" includes 'corresponding new bank'
- (d) **Any body corporate** or company or person, or any class of bodies corporate or companies or persons, on a reference made to the NFRA by the Central Government in public interest; and
- (e) **A body corporate incorporated or registered outside India**, which is a subsidiary or associate company of any company or body corporate incorporated or registered in India as referred to in clauses (a) to (d) above, if the income or net-worth of such subsidiary or associate company exceeds 20% of the consolidated income or consolidated net-worth of such company or the body corporate, as the case may be, referred to in clauses (a) to (d) above.

### 5.15 -Section 133 Accounting Standard

95.



**EPS Disclosure**

X Ltd. did not follow the applicable Accounting Standard for disclosing Earnings per Share (EPS) in the financial statements. The fact of such non-disclosure was however, mentioned in the notes forming part of accounts. As the statutory auditor of X Ltd., how would you report in the above case?

**Ans.**

- (i) **As per Accounting Standard:- Disclosure of EPS** is required for **all companies** as per AS 20 "Earnings per Share".
- (ii) **As per Section 133:-** AS 20 is also one of the AS notified by **Section 133** of the Companies Act, 2013 read with the clarification given by the **Ministry of Corporate Affairs (MCA)** vide General Circular that the **existing Accounting Standards** notified under the Companies Act, 1956 shall continue to apply till it is prescribed by Central Government.
- (iii) **Auditor's Reporting responsibility:-** If the **disclosures required** by AS 20 **are not made**, it is the duty of the auditor to **qualify in his report** "Whether Accounting Standards under the clause as notified u/s 129(1) have been followed?" **Mere disclosure by company in notes does not absolve him of his duty.** The same is, however, not a qualification to affect the "True & Fair" position of financial results of the company.

## 5.16 - Section 134 Board Report

96.	<b>Authentication of Financial Statements</b> Discuss the provisions of Section 134 of the Companies Act, 2013 regarding the authentication of financial statements. <span style="float: right;">(May-2016)</span>
Ans. 	<p>(i) <b>Provision:-</b> Section 134(1) of the Companies Act, 2013 provides that the <b>financial statements, including consolidated financial statement</b>, if any, shall be <b>approved by the board</b> of directors before they are <b>signed on behalf of the board at least by the following</b>:</p> <ul style="list-style-type: none"> <li>• <b>Chairperson</b> of the company where he is authorized by the Board; or</li> <li>• <b>By two directors</b> out of which <b>one shall be Managing Director</b>, if any and the <b>Chief Executive Officer</b>; and</li> <li>• The <b>Chief Financial Officer</b> and the <b>Company Secretary</b> of the company, wherever they are appointed.</li> </ul> <p>(ii) <b>In the case of a one person company:-</b> The financial statement <b>shall be signed by only one director</b>, for submission to the auditor for his report thereon.</p> <p>(iii) <b>Distribution/Circulation:-</b> According to <b>section 134(7)</b> of the Companies Act, 2013, a <b>signed copy of every financial statement</b>, including consolidated financial statement, if any, shall be <b>issued, circulated or published</b> along with a copy each of -</p> <ul style="list-style-type: none"> <li>• <b>Any notes annexed</b> to or forming part of such financial statement;</li> <li>• The <b>auditor's report</b>; and</li> <li>• The <b>board's report</b></li> </ul>
97.	<b>Signing of FS &amp; Board Report</b> Dharam & Karam Company Ltd. had prepared its financial statements for the financial year 2021-22 which were approved by the Board of Directors of the company and thereafter they were signed by the Chairperson of the company as authorized by the Board, as well as by its CEO, CFO and CS, respectively. Also, its board report was signed by its Managing Director as well as by an Executive Director. You are required to comment whether financial statements and the Board's report of the company have been signed by the persons mandatorily required to sign, as prescribed by the relevant Act. <span style="float: right;">(MTP-May-2022)</span>
Ans. 	<p>(i) <b>Provision:-</b> As per <b>section 134</b> of the Companies Act, 2013</p> <ul style="list-style-type: none"> <li>• The financial statements, including <b>consolidated financial statements</b>, if any, shall be approved by the Board of Directors <b>before they are signed</b> on behalf of the Board by the <b>Chairperson</b> of the Company where he is authorized by the <b>Board or by two directors</b> out of which <b>one shall be Managing Director</b>, if any, and the <b>Chief Executive Officer</b>, the <b>Chief Financial Officer</b> and the Company Secretary of the Company, wherever they are appointed, or in the case of One Person Company, only by one director, for submission to the auditor for his report thereon.</li> <li>• <b>The Board's report shall be signed by its chairperson</b> of the company if he is authorised by the <b>Board</b> and where he is not so authorised, shall be <b>signed by at least two directors</b>, one of whom shall be a <b>Managing Director</b>.</li> </ul> <p>(ii) <b>In the given case:-</b> Dharam and Karam Company Ltd. had prepared its financial statements for the financial year 2021-22 which were approved by the <b>Board of Directors</b> of the company and thereafter they were <b>signed by the Chairperson</b> of the company as <b>authorised by the Board</b>, as well as by its <b>CEO, CFO and CS, respectively</b>. Also, its board report was signed by its Managing Director as well as by an Executive Director.</p> <p>(iii) <b>Conclusion:-</b> Hence, it can be said that the <b>financial statements and the Board's report</b> of the Dharam and Karam Company Ltd. have been <b>signed are in accordance with section 134</b> of the Companies Act, 2013.</p>
98.	<b>Explain the terms</b> (i) 'Internal Financial Control' and (ii) 'Internal Financial Controls over Financial Reporting'

Ans.

**(i) Internal Financial Control:**

- **Definition:- As per explanation to section 134(5) of Companies Act, 2013**

The term Internal Financial Controls means the policies and procedures adopted by the company for ensuring:

- **Safeguarding** of its assets,
- **Orderly and efficient conduct of its business**, including adherence to Company's policies,
- **Prevention and detection** of frauds and errors,
- **Accuracy and completeness** of the accounting records, and
- **Timely preparation** of reliable financial Information.

**(ii) Internal Financial Control over Financial Reporting:**

**Guidance Note issued by ICAI:- Guidance Note on Audit of Internal Financial Controls Over Financial Reporting"**

- **Definition**

"A Process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes In accordance with generally accepted accounting principles".

- **Policy & Procedures**

A Company's internal financial control over financial reporting includes those policies and procedures:

- Pertain to the **maintenance of the records** that, in reasonable detail, **accurately and fairly reflect the transactions and dispositions** of the assets of the company
- **It provides reasonable assurance** that transactions are **recorded as necessary to permit preparation of financial statement** in accordance with generally accepted accounting principles, and those receipts and expenditures of the company are being made only in accordance with authorizations of management and director of the company.
- Provide **reasonable assurance** regarding **prevention or timely detection** of unauthorized acquisition, use or disposition of the **company's assets** that could have a material effects of the financial statement.

99.

**Director's Responsibility Statement (DRS)**

What are the matters to be included in Director's Responsibility statement?

(May-2016)

Ans.



**Matters to be included in Director's Responsibility Statement:** The provisions related to the **Director's responsibility** under **section 134(5)** of the Companies Act, 2013 are as under:

- 1) **Accounting Standards:-** In the preparation of the annual accounts, the **applicable accounting standards had been followed** along with proper explanation relating to material departures;
- 2) **Accounting Policies:-** The directors had **selected such accounting policies and applied them consistently** and made adjustments and estimates that are **reasonable and prudent** so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the profit and loss of the company for that period;
- 3) **Internal Control:-** The directors had taken **proper and sufficient care** for the maintenance of **adequate accounting records** in accordance with the provisions of this act for **safeguarding the assets** of the company and for preventing and detecting frauds and other irregularities;
- 4) **Going Concern:-** The directors had prepared the annual accounts **on a going concern basis**;
- 5) **Internal financial controls:-** The directors, **in the case of a listed company**, had laid down internal financial controls to be **followed by the company** and that such internal financial controls are adequate and were **operating effectively**;
- 6) **Compliance of law:-** The directors had devised proper system to **ensure compliance with the provisions of all applicable laws** and that such systems were **adequate and operating effectively**.

**5.17 –Section 135 Corporate Social Responsibility**

100.

**Corporate Social Responsibility - Expenses**

Beneath minerals Limited is a Public Sector Company engaged in extraction of minerals from land. It has to pump out water in the first layer of the soil if the minerals are to be excavated. The Company pumps out water and diverts the water through a water course constructed by it to nearby villages and the water is allowed to be used by villagers for drinking purposes. The cost of construction of water course amounted to ₹ 5.25 crores and the Company had disclosed this amount as CSR expenses in the Statement of Profit and Loss. Comment. (May-2018-New)

Ans.



(i) **Provision:-** As per **Section 135** of Companies Act, 2013,

- The Board of directors of **every company** referred to in **Section 135(1)**, shall ensure that the company spends, in every financial year,
- At least **two percent of the average net profits** of the company
- Made during the **three immediately preceding financial years**, in pursuance of its Corporate Social Responsibility Policy.

(ii) **As per Rule:- Company (Corporate Social Responsibility Policy) Rules, 2014** mandated the corporate entities that the expenditure incurred for **Corporate Social Responsibility (CSR) should not be the expenditure** incurred for the activities in the **ordinary course of business**. If expenditure incurred is for the activities in the ordinary course of business, then **it will not be qualified** as expenditure incurred on CSR activities.

(iii) **In the instant case:- Beneath minerals Limited** is a **public sector company** which is engaged in **extraction of mineral from land**, for that it has to **pump out water in the first layer** of the soil if the minerals are to be excavated. The company pumps out water and diverts the water through a water course constructed by it to nearby villages and the **water is allowed to be used by villagers for drinking purposes**.

(iv) **Conclusion:-** Company has disclosed the cost of construction of water course as CSR expenses in the statement of Profit and Loss, **which is not correct as this expenditure incurred for the construction of water course** is included in the **ordinary course of activities of business**. So, expenditure **cannot be classified as CSR Expense** and hence auditor should **state the fact** in the report and **qualify the report**.

**5.18 -Section 138 Internal Audit**

101.

**Applicability of Provisions of Internal Audit**

JKH Pvt. Ltd. who is into the business of imparting coaching to CA students did not appoint any internal auditor for the year ended 31st March, 2022. As on 31st March, 2021, the company had paid up capital of ₹ 50 lakhs and reserves of ₹ 10 crores. Its turnover for the 3 years preceding the year ended 31st March, 2022 was ₹ 75 crores, ₹ 145 crores and ₹ 260 crores respectively. As an auditor of the company for the year ended 31st March, 2022 how would you deal with the above? (RTP-May-2015, Nov-2017, MTP-May-2018)

Ans.



(i) **Provision:-** As per **section 138** of the Companies Act, 2013, **read with Rule 13** of Companies (Audit and Auditors) Rules, 2014 **every private company** shall be required to appoint an internal auditor or a firm of internal auditors or Body Corporate, having –

- Turnover of **two hundred crore rupees or more** during the preceding financial year; or
- Outstanding loans or borrowings from banks or public financial institutions **exceeding one hundred crore rupees or more at any point of time** during the preceding financial year:

(ii) **In the instant case:- JKH Pvt. Ltd.** is having **turnover of ₹ 260 crores** during the preceding financial year which is more than two hundred crore rupees.

(iii) **Conclusion:-** Hence, the **company has the statutory liability to appoint an Internal Auditor** and mandatorily conduct internal audit.

102.

**Internal Audit: Applicability**

Incentivize Pvt. Ltd. has paid up capital of ₹ 50 lakh during the previous financial year which rose to ₹ 60 lakh in current financial year. The company had turnover of ₹ 210 crore during the previous financial year which declined to ₹ 151 crore in current financial year. Discuss whether the company is required to appoint an internal auditor to conduct internal audit of the functions and activities of the company. (MTP-May-2016)

Ans.

**Applicability of Provisions of Internal Audit:**

- (i) **Provision:-** As per **section 138** of the Companies Act, 2013, **read with Rule 13** of Companies (Audit and Auditors) Rules, 2014 **every private company** shall be required to appoint an internal auditor or a firm of internal auditors or Body Corporate, having –
- Turnover of **two hundred crore rupees or more** during the preceding financial year; or
  - Outstanding loans or borrowings from banks or public financial institutions **exceeding one hundred crore rupees or more at any point of time** during the preceding financial year:
- (ii) **In the instant case:-** Incentivize Pvt. Ltd. has **paid up capital of ₹ 50 lakh** during the previous financial year which rose to **₹ 60 lakh in current financial year**. The company had **turnover of ₹ 210 crore** during the previous financial year which **declined to ₹ 151 crore** in current financial year.
- (iii) **Conclusion:-** Although the **turnover of the current financial year has been decreased** the turnover of the preceding financial year was **more than ₹ 200 crore which is the requirement** of the section as mentioned above. **Hence Incentivize Pvt. Ltd. has the statutory liability to appoint an internal auditor and mandatorily conduct internal audit.**

103.

**Independence of Internal Auditor**

Write a short note on - Independence of Internal Auditor.

Ans.



- (i) **Provision:-** As per **section 138** of the Companies Act, 2013, the internal auditor, who shall either be:
- A **chartered accountant** whether engaged in practice or not or
  - A **cost accountant**, or
  - Such **other professional** as may be decided by the Board to conduct internal audit of the functions and activities of the companies
  - Auditor **may or may not be an employee** of the company.
- (ii) **Audit Planning:-**
- The **Audit Committee** of the company or the **Board** shall, in **consultation with the Internal Auditor**, formulate the **scope, functioning, periodicity and methodology** for conducting the internal audit.
  - It may also be noted that the **Central Government** may, by rules, **prescribe the manner and the intervals** in which the internal audit shall be **conducted and reported** to the Board.
- (iii) **Concept of Independence:-**
- The concept of independence is **equally relevant for internal auditor also**.
  - Internal auditing is an **independent, objective assurance and consulting activity** designed to add value and improve an organisation's operations.
  - As mentioned above**, the internal auditor may be **part of the management**, but he evaluates the **functioning of the management** at different levels.
- (iv) **Conclusion:-** Therefore, to be **efficient and effective**, the **internal auditor must have adequate independence**.

104.

**Internal Audit System**

PQR Ltd, an unlisted company and having average annual turnover of less than ₹ 200 crores has no internal audit system. Give your views.

Ans.



- (i) **Provision:-** As per **Section 138** of Companies Act 2013, companies required to have **internal audit system** that fall under the limits prescribed under **Rule 13 of Companies (Audit and Auditors) Rules 2014"**
- (ii) **Applicability (Rule 13):** Companies required to appoint **internal auditor / firm of internal auditors:**
- Every listed company;**
  - Every **UNLISTED PUBLIC COMPANY** having-
    - >= 25 Crores** - **Outstanding deposits** at any point of time during the preceding financial year; or