

**COMPANIES (AUDITOR'S REPORT)  
ORDER, 2016 (CARO 2016) –  
PRACTICAL UNDERSTANDING AND SOLVING OF  
VARIOUS INTRICACIES INVOLVED THEREIN**

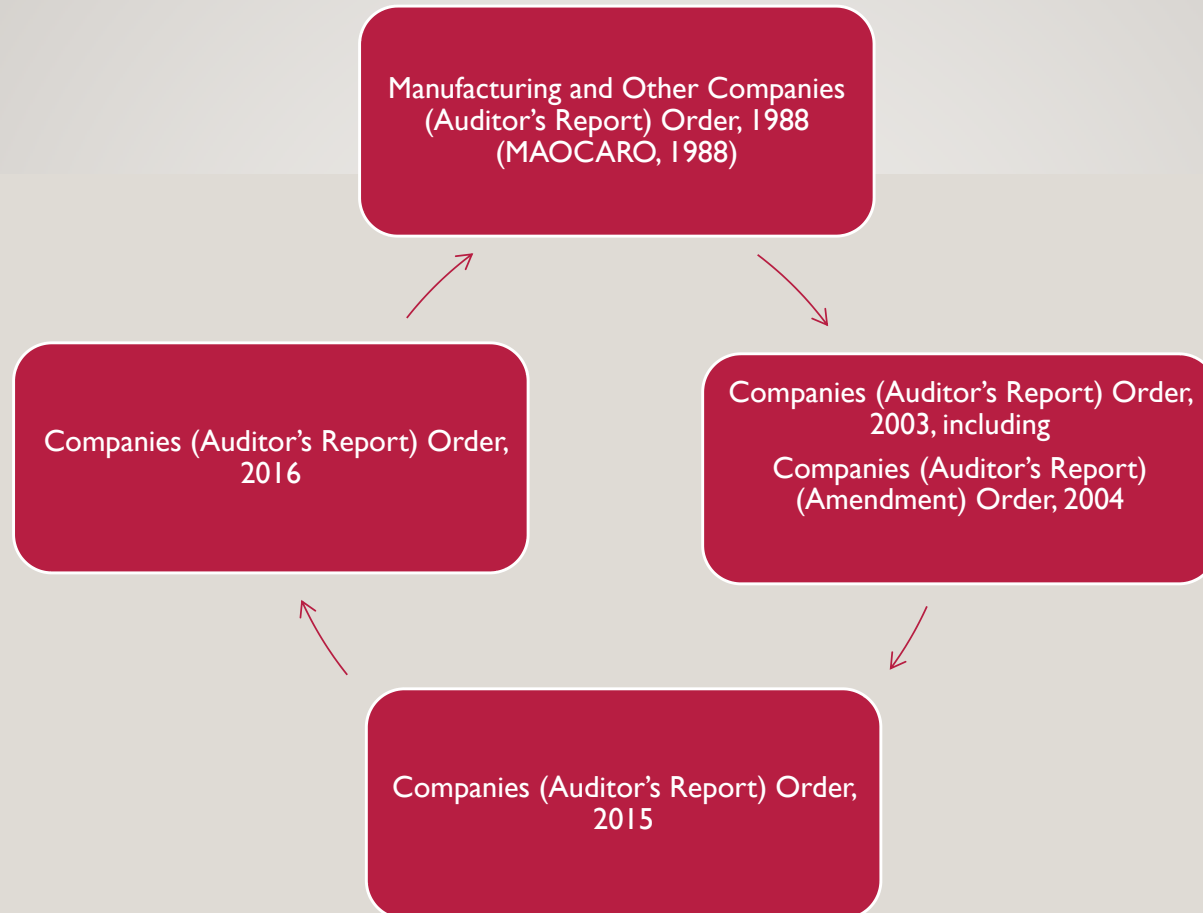
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- CA Manoj H. Dama

December 16, 2017

# THE JOURNEY

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# THE JOURNEY

Order Reference	Particulars
Manufacturing and Other Companies (Auditor's Report) Order, 1988 (MAOCARO)	Came into force on the 1st day of November, 1988. No exemption to Private Limited Company Not applicable to consolidated financial statements
Companies (Auditor's Report) Order, 2003	Applicable to financial year ending after 12th June, 2003 Exemptions given to Private Limited Companies fulfilling certain criteria Not applicable to reporting on consolidated financial statements
Companies (Auditor's Report) Order, 2015	Applicable to financial years commencing on or after 1st April, 2014 Exemptions given to Private Limited Companies retained Applicable to reporting on consolidated financial statements as well
Companies (Auditor's Report) Order, 2016	Applicable to financial years commencing on or after 1st April, 2015 Exemptions given to Private Limited Companies liberalised Not applicable to reporting on consolidated financial statements

# COMPANIES (AUDITOR'S REPORT) ORDER, 2016

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- CARO 2016 applicable for audits of financial statements for periods beginning on or after April 1, 2015. Does not apply to consolidated financial statements.
- Applies to every company (exceptions provided) including a foreign company as defined in Section 2(42) of the Companies Act, 2013 (and would therefore apply to Branches and Liaison Offices of foreign companies established in India).
- Applicability based on the status of the Company as at the balance sheet date.
- Specific exemption given to companies licensed under section 8 of the Companies Act 2013. However, it appears that the exemption would also extend to companies licensed to operate under section 25 of the Companies Act 1956.

# COMPANIES (AUDITOR'S REPORT) ORDER, 2016

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- Applicability to private limited company, not being a subsidiary or holding of a public company:
  - paid up capital and reserves (capital and revenue, including revaluation reserve) and surplus (debit balance to be reduced) more than one crore rupees as on the balance sheet date
  - total borrowings (long term or short term, including interest accrued & due, and outstanding dues in respect of credit cards) exceeding rupees one crore from any bank or financial institution at any point of time during the financial year
  - total revenue (aggregate of revenue from operations and other income) as disclosed in Schedule III to the Companies Act, 2013 (including revenue from discontinuing operations) exceeding rupees ten crores during the financial year as per the financial statements.



# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the company is maintaining proper records showing full particulars, including quantitative details and situation of fixed assets. [Paragraph 3(i)(a)]</p>	<ul style="list-style-type: none"><li>• Covers all fixed assets whether tangible or intangible, self-financed or acquired through finance lease</li><li>• Covers fixed assets fully depreciated or amortized or have been retired from active use and held for disposal or impaired</li><li>• The aggregate original cost, depreciation or amortisation to date, and impairment loss, if any, as per FA records under individual heads should reconcile with the figures shown in the books of account</li><li>• Challenges in case of fixed assets whose situation keeps changing, for example, construction equipment which has to be moved to sites.<ul style="list-style-type: none"><li>➤ In such circumstances, it should be sufficient if record of movement/custody of the equipment is maintained.</li></ul></li><li>• Assets located in the residential premises of members of the staff<ul style="list-style-type: none"><li>➤ Register should indicate the name &amp; designation of the person who has custody of the asset for the time being.</li></ul></li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether these fixed assets have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account; [Paragraph 3(i)(b)]</p>	<ul style="list-style-type: none"><li>• Physical verification is a responsibility of the management. The auditor may prefer to observe the verification. It is necessary that the auditor satisfies himself that such verification was done and that there is adequate evidence.</li><li>• Challenges in case of certain process industries where verification by direct physical check may not be possible; say for assets in continuous use or which are concealed within larger units.<ul style="list-style-type: none"><li>➤ indirect evidence of the existence of the assets may suffice – e.g. the very fact that an oil refinery is producing at normal levels of efficiency may be sufficient to indicate the existence of the various process units even where each such unit cannot be verified by physical or visual inspection.</li></ul></li><li>• Assets like building<ul style="list-style-type: none"><li>➤ not be necessary to verify by measurement except where there is evidence of alteration/demolition.</li></ul></li><li>• Assets like open land<ul style="list-style-type: none"><li>➤ in view of the possibility of encroachment, adverse possession, etc., it may be necessary for a survey to be made periodically.</li></ul></li></ul>

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<p>Whether these fixed assets have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account; [Paragraph 3(i)(b)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Assets be marked with “distinctive numbers” especially where assets are movable in nature and where verification of all assets is not being conducted at the same time.</li><li>• “reasonable intervals” depends on circumstances of each case<ul style="list-style-type: none"><li>➤ verification programme should be such that all assets are verified at least once in every three years.</li></ul></li></ul>



# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the title deeds of immovable properties are held in the name of the company. If not, provide the details thereof; [Paragraph 3(i)(c)]</p>	<ul style="list-style-type: none"><li>• Include items in Capital Wok in Progress.<ul style="list-style-type: none"><li>➤ TDRs (Transfer Development Rights), Plant and Machinery embedded in land etc., are not considered as an immovable property.</li></ul></li><li>• “Title deeds” means legal deed or document constituting evidence of a right, especially to the legal ownership of the immovable property.<ul style="list-style-type: none"><li>➤ Registered sale deed / transfer deed / conveyance deed, etc. of land, land &amp; building together, etc. In case of leasehold land and land &amp; buildings together, the lease agreement duly registered with the appropriate authority</li></ul></li><li>• Immovable property mortgaged with the Banks/Financial Institutions, etc.<ul style="list-style-type: none"><li>➤ Confirmation should be sought from the respective institution. Consider verifying this information from the online records, if available.</li></ul></li><li>• Title deeds lost accidentally or otherwise.<ul style="list-style-type: none"><li>➤ Certified copies of the documents, as available with the company, and details about the FIR filed needs to be obtained and documented. Seek written representations.</li></ul></li></ul>

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<p>Whether the title deeds of immovable properties are held in the name of the company. If not, provide the details thereof; [Paragraph 3(i)(c)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Existence of pending / disputed court cases relating to ownership.<ul style="list-style-type: none"><li>➤ Consider communicating with the legal counsel, whether in-house or external. Also consider disclosing the dispute while reporting under this Clause</li></ul></li><li>• Title deeds in different languages<ul style="list-style-type: none"><li>➤ Have the company obtain a translated version. Seek written representations.</li></ul></li><li>• Title deeds in the name of erstwhile entities which merged with the company or there has been a change in the name of the Company<ul style="list-style-type: none"><li>➤ Consider reporting the fact, including giving reference to the approved scheme.</li></ul></li><li>• Title deeds in the process of being transferred in the name of the Company to be reported as an exception.</li><li>• Title deeds available should be reconciled with the fixed assets register.<ul style="list-style-type: none"><li>➤ Possibility of reconciliation being in progress or discrepancies noticed between the details in the fixed assets register and the details available in the title deeds. Auditor to consider implications on opinion on the financial statements as well as on the Internal Financial Controls Over Financial Reporting of the Company.</li></ul></li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether physical verification of inventory has been conducted at reasonable intervals by the management and whether any material discrepancies were noticed and if so, whether they have been properly dealt with in the books of account; [Paragraph 3(ii)]</p>	<ul style="list-style-type: none"><li>• Responsibility of the management and, therefore, has to be carried out by the management itself and not by the auditor. The auditor may prefer to observe the verification. It is necessary that the auditor satisfies himself that such verification was done and that there is adequate evidence.</li><li>• Reporting applicable even if there is only one transaction during the reporting period and irrespective of the fact whether any inventory is held as at the period end or not.</li><li>• Physical verification of inventories lying with third parties and/ or goods-in-transit<ul style="list-style-type: none"><li>➤ If performed by performing alternate procedures such as obtaining confirmations, the fact of such procedures needs to be reported.</li></ul></li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the company has granted any loans, secured or unsecured to companies, firms, Limited Liability Partnerships or other parties covered in the register maintained under section 189 of the Companies Act, 2013. If so,</p> <p>a) Whether the terms and conditions of the grant of such loans are not prejudicial to the company's interest;</p>	<ul style="list-style-type: none"><li>• If a party is covered by section 188 or section 184, even if the loan given to these parties are not entered in the Register specified under section 189, reporting must be made in this Clause.</li><li>• Reporting under clause (iii)(a) applies only at the point of “grant” (i.e., inception or the date of renewal or modification of the significant terms). Reporting under the remaining sub-clauses applies to all loans given during the year and also to loans outstanding at any point in time during the year.</li><li>• Interest free loans granted for which repayment terms/schedule is not specified.<ul style="list-style-type: none"><li>➤ A disclaimer of an opinion on these sub-clauses would impact our responsibility under Section 143(1)(a) in respect of loans made by the company on the basis of security.</li></ul></li><li>• Loan may be given in cash or in kind or may be long term or short term.</li><li>• Also take into consideration the loan transactions that have been squared-up during the year.</li><li>• “terms and conditions” would primarily include rate of interest, security, terms and period of repayment and restrictive covenants, if any.</li></ul>

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Reportable Clause	Points to consider
<p>a) Whether the terms and conditions of the grant of such loans are not prejudicial to the company's interest;</p> <p>b) Whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;</p>	<ul style="list-style-type: none"><li>• Providing loans at concessional rates of interest to a relative of the director who is also an employee of the company.<ul style="list-style-type: none"><li>➤ Cannot be said to be prejudicial to the interest of the company if other employees of the company also receive the loan on the same terms.</li></ul></li><li>• Waiver of principal amount and/or interest on the loans given by the Company,<ul style="list-style-type: none"><li>➤ Need to be assessed and concluded for reporting as to why such waiver is not prejudicial to the interest of the Company. Provision does not tantamount to a waiver.</li></ul></li><li>• The word 'regular' should be taken to mean that the principal and interest should normally be received whenever they fall due, respectively.</li><li>• In case of NBFC, the auditor, for reporting under this clause, would also need to refer various directions issued by Reserve Bank of India.</li></ul>

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Reportable Clause	Points to consider
<p>b) Whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;</p> <p>c) If the amount is overdue, state the total amount overdue for more than 90 days, and whether reasonable steps have been taken by the company for recovery of the principal and interest. [Paragraph 3(iii)]</p> <p>... Contd.</p>	<ul style="list-style-type: none"><li>• In case of non-stipulation of schedule of repayment of principal &amp; payment of Interest, the auditor should state the fact and may report that he is unable to make specific comment on the regularity of repayment of principal &amp; payment of interest, in such cases.</li><li>• Depending upon the circumstances, the degree of delay in recovery and other similar factors, issue of reminders or the sending of an advocate's or solicitor's notice, may amount to "reasonable steps" even though no legal action is taken</li><li>➤ Negative reporting with respect to reasonable steps taken by management for recovery may impact the audit opinion on the financial statements, since it affects the "valuation" assertion.</li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>In respect of loans, investments, guarantees, and security whether provisions of section 185 and 186 of the Companies Act, 2013 have been complied with. If not, provide the details thereof. [Paragraph 3(iv)]</p>	<ul style="list-style-type: none"><li>• Section 185 prohibits advance of any loan to directors, etc., directly or indirectly. What is an indirect loan is not defined in section 185 or elsewhere in the Act. Indirect is interpreted to mean a loan to a director through the agency of one or more intermediaries.</li><li>• If the company is in default in the repayment of any deposits accepted or in payment of interest thereon, then the company is not allowed to give any loan or guarantee or any security or an acquisition till such default is subsisting.</li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>In case the company has accepted deposits, whether the directives issued by the Reserve Bank of India and the provisions of sections 73 to 76 or any other relevant provisions of the Companies Act, 2013 and the rules framed thereunder, where applicable, have been complied with? If not, the nature of such contraventions be stated; if an order has been passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any Court or any other Tribunal, whether the same has been complied with or not? [Paragraph 3(v)]</p>	<ul style="list-style-type: none"><li>• Section 73 of the Act, prohibits a company (other than a banking company, non-banking financial company (NBFC) and such other company as may be specified by the central government in consultation with the Reserve Bank of India), to invite, accept or renew deposits from the public except in the manner provided in this section and the Companies (Acceptance of Deposits) Rules, 2014</li></ul>



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Reportable Clause	Points to consider
<p>Whether maintenance of cost records has been specified by the Central Government under sub-section (1) of Section 148 of the Companies Act, 2013 and whether such accounts and records have been so made and maintained. [Paragraph 3(vi)]</p>	<ul style="list-style-type: none"><li>• The Order does not require a detailed examination of such records. The auditor should, therefore, conduct a general review of the cost records to ensure that the records as prescribed are made and maintained.</li><li>• Where the auditor finds that the records have not been written or are not prima facie complete, it will be necessary for the auditor to make a suitable comment in his report.</li></ul>

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Reportable Clause	Points to consider
<p>Whether the company is regular in depositing undisputed statutory dues including Provident Fund, employees' State Insurance, Income-tax, Sales-tax, Service Tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated; [Paragraph 3(vii)(a)]</p>	<ul style="list-style-type: none"><li>• Obligation to pay a statutory due is created or arises out of a statute, rather than being based on an independent contractual or legal relationship.<ul style="list-style-type: none"><li>➤ Thus, would include municipal taxes, TDS, fees payable to the licensing authority.</li><li>➤ Sum payable to an electricity company as electricity bill would not constitute a statutory due because the due has arisen on account of contract of supply of goods or services between the parties.</li><li>➤ Any dues recoverable as arrears of land revenue by the concerned authority, shall be treated as a statutory due.</li></ul></li><li>• Payment of import duty where the goods were placed in the bonded warehouse:<ul style="list-style-type: none"><li>➤ Payment of import duty is to be made when the goods are removed from the bonded warehouse. Accordingly, the question of regularity does not arise in respect of custom duty in this case.</li><li>➤ Interest and rent that are required to be incurred under section 61 of the Customs Act, 1962 would be covered under "other statutory dues" and the auditor would have to examine and comment upon the regularity of the company in depositing such interest and rent.</li></ul></li></ul>

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Reportable Clause	Points to consider
<p>Where dues of income Tax or sales Tax or service Tax or duty of customs or duty of excise or value added tax have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned [Paragraph 3(vii)(b)]</p>	<ul style="list-style-type: none"><li>• Mere representation shall not be treated as a dispute.</li><li>• Show-cause or similar notice<ul style="list-style-type: none"><li>➤ Generally contains the requirements/queries of the assessing officer and should not be construed to be a demand payable by the company. However, in some cases, a show cause notice and demand may be combined in one document. Hence, it would be necessary to evaluate each situation individually.</li></ul></li><li>• Tax demands that have been set aside are clearly not 'dues'.</li><li>• Demand referred for reassessment resulting in cancellation of the earlier demand, would not constitute an amount due.</li><li>• Demands that have been stayed should be regarded as disputed dues.</li><li>• Department preferring an appeal to a higher authority:<ul style="list-style-type: none"><li>➤ Considered to be no dispute until the time the Department makes an appeal to the relevant appellate authority.</li></ul></li></ul>

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<p>Where dues of income Tax or sales Tax or service Tax or duty of customs or duty of excise or value added tax have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned [Paragraph 3(vii)(b)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Amount under dispute has not been paid before filing the appeal and no appeal is filed within the time allowed - would become a statutory due.</li><li>• Disputed amounts not been deposited but on consideration of the likely outcome of the dispute, a provision has been made in the accounts.<ul style="list-style-type: none"><li>➤ Amount will need to be reported, notwithstanding provision thereof.</li></ul></li><li>• Amount deposited under protest in respect of disputed dues, whether disclosed as recoverable or otherwise, should be brought out by the auditor in his report under the clause.</li><li>• Consideration needs to be given to the balance shown as Provision for tax (net of advance tax) and its classification in the Balance Sheet. If Provision for tax is disclosed as a Short-term Provision, careful evaluation is required to determine if any part of the balance could be considered as undisputed dues remaining unpaid for more than 6 months at the Balance Sheet date.</li><li>• A reconciliation should be maintained with respect to disclosures under contingent liabilities and disclosure under this clause.</li></ul>

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Reportable Clause	Points to consider
<p>Whether the company has defaulted in repayment of loans or borrowing to a financial institution, bank, government or dues to debenture holders? If yes, the period and the amount of default to be reported (in case of defaults to banks, financial institutions, and government, lender wise details to be provided). [Paragraph 3(viii)]</p>	<ul style="list-style-type: none"><li>• Report the period and amount of all defaults existing at the balance sheet date irrespective of when those defaults have occurred.</li><li>• The term “Government” does not include Government Company/ Public Sector Undertaking/ Boards/ Authority/ Corporation and Foreign Government.</li><li>• Submission of application for reschedulement/restructuring does not mean that no default has occurred.</li><li>• Deferred sales tax liability granted by the government to be included in this clause for reporting.</li><li>• A subsidy given by the government that is refundable subject to non-fulfillment of certain conditions is not be considered as a borrowing.</li><li>• Auditor may give a brief nature of the dispute, if any, between the Company and the lender while reporting under this clause.</li></ul>

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<p>Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported; [Paragraph 3(ix)]</p>	<ul style="list-style-type: none"><li>• Currently, no legal requirement under the Act to disclose the end use of money in the financial statements.<ul style="list-style-type: none"><li>➤ Schedule III requires only unutilized amount to be disclosed in the FS.</li><li>➤ it appears that the clause envisages that the companies should disclose the end use of money raised in the financial statements by way of notes and the auditor should verify the same.</li><li>➤ SEBI (Listing Obligations &amp; Disclosure Requirements) Regulations, 2015 contain a number of disclosure requirements with respect to utilization of proceeds as also in respect of unutilized monies.</li></ul></li><li>• Auditor not able to verify the end-use of money raised<ul style="list-style-type: none"><li>➤ Should state that he is not able to comment upon the disclosure of end-use of money by the company since he could not verify the same.</li><li>➤ Should also mention the reasons which resulted in the inability to verify the disclosure.</li></ul></li></ul>

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<p>Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported; [Paragraph 3(ix)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Offer for sale of specified securities (i.e. equity shares and convertible securities) to the public by any existing holder<ul style="list-style-type: none"><li>➤ Outside the purview of reporting as does not result in any moneys raised in a company.</li></ul></li><li>• Moneys raised from foreign capital markets and by way of issuance of Global Depository Receipts and American Depository.<ul style="list-style-type: none"><li>➤ Strictly in terms of the definitions of public offer, initial public offer and further public offer, receipts may not fall within the scope of reporting under this clause.</li></ul></li><li>• Term loans normally have a fixed or pre-determined maturity period or a repayment schedule.<ul style="list-style-type: none"><li>➤ Banking industry, for example, loans with repayment period beyond 36 months are usually known as “term loans”.</li><li>➤ Cash credit, overdraft and call money accounts/deposits, not covered by the expression “term loans”.</li></ul></li></ul>



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<p>Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported; [Paragraph 3(ix)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Not necessary to establish a one-to-one relationship with the amount of term loan and its utilisation.<ul style="list-style-type: none"><li>➤ Loan disbursed by the bank may be deposited in the common account of the company from which subsequently the utilisation is made.</li><li>➤ Should not be construed that the amount has not been utilised for the purpose it was raised.</li></ul></li><li>• Company acquiring improved version/model of assets<ul style="list-style-type: none"><li>➤ For example, loan sanctioned for purchase of machinery to be used for manufacture of shoe upper is instead used to purchase a machine, which apart from manufacturing shoe uppers has certain additional manufacturing facilities.</li><li>➤ Should not be construed that the loan has not been applied for the purpose for which it was raised.</li></ul></li></ul>

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<p>Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported; [Paragraph 3(ix)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Term loans taken during the year might not have been applied for the stated purpose during the year,<ul style="list-style-type: none"><li>➤ For example, the loan was disbursed at the fag end of the year. Auditor should mention in his audit report that the term loan obtained during the year has not been utilised.</li><li>➤ Should also consider the term loans which although were taken in the previous accounting period but have been actually utilised during the current accounting period.</li></ul></li><li>• Term loans, where the lender is not concerned with the purpose of the loan.<ul style="list-style-type: none"><li>➤ Auditor should clearly mention that he is unable to comment.</li></ul></li><li>• Term loans, where specific purpose is not stated and loans given for general business purposes.<ul style="list-style-type: none"><li>➤ Auditor should verify whether the company has invested or utilized the money for purposes other than objects of the company.</li></ul></li></ul>

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<p>Whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans were applied for the purposes for which those are raised. If not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported; [Paragraph 3(ix)] .... Contd.</p>	<ul style="list-style-type: none"><li>• Temporary investment of the surplus funds during construction phase.<ul style="list-style-type: none"><li>➤ Auditor should mention the fact that pending utilisation of the funds raised through Initial Public Offer or Further Public Offer (including debt instruments) or term loans for the stated purpose, the funds were temporarily used for the purpose other than for which they were raised but were ultimately utilised for the stated end-use.</li></ul></li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether any fraud by the company or any fraud on the company by its officers or employees has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated. [Paragraph 3(x)]</p>	<ul style="list-style-type: none"><li>• Does not require the auditor to discover such frauds.<ul style="list-style-type: none"><li>➤ Scope restricted to frauds '<u>noticed or reported</u>' during the year by the Management.</li><li>➤ Does not relieve the auditor from his responsibility to consider fraud and error in an audit of financial statements.</li></ul></li><li>• Clause will include only the reported frauds and not suspected fraud.</li><li>• Restricts reporting of fraud on the Company to frauds perpetrated by its officers/employee.<ul style="list-style-type: none"><li>➤ Therefore fraud by any external persons/party on the Company should not be considered for reporting under this clause.</li></ul></li><li>• Fraud noticed or reported even after the Balance Sheet date but any time before the signing of the audit report, should be considered for reporting, if the fraud pertains to a period on or prior to the balance sheet date.</li><li>• Likely sources of information other than inquiries of Management include:<ul style="list-style-type: none"><li>➤ Reports of the internal auditor, minutes of the board/audit/other committees, CEO and CFO certificate in terms of SEBI (LODR) Regulations, 2015.</li></ul></li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether Managerial remuneration has been paid or provided in accordance with the requisite approvals mandated by the provisions of section 197 read with schedule V to the Companies Act? If not, state the amount involved and steps taken by the Company for securing refund of the same [Paragraph 3(xi)]</p>	<ul style="list-style-type: none"> <li>• Section 197 applies only to a public company.</li> <li>• Remuneration would not include sitting fees paid to directors in accordance with the provisions of the Act or remuneration payable to directors for services rendered by him of a professional nature</li> <li>• Order does not clarify what constitutes “amounts involved” <ul style="list-style-type: none"> <li>➤ May be construed as such amount of remuneration that has been paid or provided in excess of the limits prescribed under section 197 read with Schedule V of the Act.</li> <li>➤ Amount that may have recovered or partially recovered by the company during the year would not be reduced from the “amount involved”.</li> </ul> </li> <li>• Non-compliance with section 197 will require evaluation as per requirements of SA 250 – Compliance with Laws and Regulations, to determine impact on the auditor’s report on financial statements and the company’s internal financial control over financial reporting.</li> </ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the Nidhi Company has complied with the Net Owned Funds to Deposits in the ratio of 1:20 to meet out the liability and whether the Nidhi Company is maintaining ten per cent unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability [Paragraph 3(xii)]</p>	<ul style="list-style-type: none"><li>• Section 406 (1) of the Act defines “Nidhi” to mean a company which has been incorporated as a Nidhi with the object of cultivating the habit of thrift and savings amongst its members, receiving deposits from, and lending to, its members only, for their mutual benefit, and which complies with such rules as are prescribed by the Central Government for regulation of such class of companies.</li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether all transactions with the related parties are in compliance with section 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards [Paragraph 3(xiii)]</p>	<ul style="list-style-type: none"><li>• Section 188 of the Act is applicable to all classes of companies</li><li>• Related Party, with reference to a company is defined in section 2(76) of the Act.</li><li>• ‘ordinary course of business’ not defined under the Act.<ul style="list-style-type: none"><li>➤ SA 550 Related Parties has listed certain examples of transactions outside the entity’s normal course of business:</li></ul></li><li>• Some indicators based on which to evaluate ‘ordinary course of business’:<ul style="list-style-type: none"><li>➤ transaction is covered in the objects of the company,</li><li>➤ transaction is usual or unusual, both from the company &amp; its line of business,</li><li>➤ More frequent, more likely treated as an ordinary course of business. Inverse does not necessarily hold true,</li><li>➤ transaction is taking place at arm’s length &amp; Business purpose thereof</li><li>➤ transaction is done on similar basis with other third parties</li><li>➤ Size and volume of transaction</li></ul></li><li>• For the purpose of this Clause the auditor may test the transaction of arm’s length basis based on the transfer pricing mechanism in use for the purposes of Income Tax Act, 1961.</li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the company has made any preferential allotment or private placement of shares or fully or partly convertible debentures during the year under review and if so, as to whether the requirement of Section 42 of the Companies Act, 2013 have been complied with and the amount raised have been used for the purposes for which the funds were raised. If not, provide the details in respect of the amount involved and nature of non-compliance; [Paragraph 3(xiv)]</p>	<ul style="list-style-type: none"><li>• The term “preferential allotment” is not defined under the Act.<ul style="list-style-type: none"><li>➤ For the purpose of this clause, preferential allotment would mean an allotment to parties in preference to others.</li><li>➤ Preference can be with regard to the price or other terms and conditions associated with the allotment.</li><li>➤ In the case of a listed company, preferential allotment of securities is governed by the SEBI (Disclosure and Investor Protection) Guidelines, 2000.</li></ul></li><li>• Guidance provided in respect of Paragraph 3(ix), to the extent relevant, should be considered by the auditors while reporting under this clause.</li><li>• In cases where the issue has taken place before the Balance Sheet date but allotment is done after the Balance Sheet date but before the date of signing, the report should be suitably worded.</li></ul>



# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether the provisions of section 192 of Companies Act, 2013 have been complied with. [Paragraph 3(xv)]</p>	<ul style="list-style-type: none"><li>• The term “person connected with the director” has not been defined in the Act, or the Rules thereunder.<ul style="list-style-type: none"><li>➤ The term “to any other person in whom the director is interested” as defined in the explanation to section 185(1) of the Act may be used as the reference point for reporting under this clause.</li></ul></li><li>• Transactions involving change in the assets or liabilities of a company but not involving “cash” or cash equivalents” as defined under Accounting Standard (AS) 3, “Cash Flow Statement” may be construed as non-cash transactions.</li><li>• Transactions not considered as non-cash transaction<ul style="list-style-type: none"><li>➤ Acquisition of the asset takes place in one year and the corresponding liability is created in the financial statements, the corresponding settlement in the following year.</li><li>➤ Mergers under Court schemes would be entered into subject to requisite approvals of Court etc.</li></ul></li></ul>

# MATTERS TO BE INCLUDED IN THE AUDITOR'S REPORT AS SPECIFIED IN PARAGRAPH 3 OF THE ORDER.

Reportable Clause	Points to consider
<p>Whether the company is required to be registered under section 45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained. [Paragraph 3(xvi)]</p>	<ul style="list-style-type: none"><li>• The registration is required where the financing activity is a principal business of the company.<ul style="list-style-type: none"><li>➤ Financial activity as principal business is when a company's financial assets constitute more than 50 per cent of the total assets and income from financial assets constitute more than 50 per cent of the gross income.</li></ul></li><li>• The Reserve Bank of India restrict companies from carrying on the business of a non-banking financial institution without obtaining the certificate of registration.</li></ul>

# OTHER GENERAL MATTERS

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The auditor is required to give reasons for any unfavourable or qualified answer. Further, where the auditor is unable to express an opinion on any such matter which is applicable to the company, he is also required to indicate in his report such fact together with the reasons as to why he is unable to express any opinion.

Whether it is necessary for the auditor to include in his report the management's explanation for any matter on which he makes an unfavorable comment?

- Normally, such an explanation need not be included but there may be circumstances where the auditor feels such inclusion is necessary. Examples of such circumstances would be:
  - to make the comment itself more meaningful and complete. For example, physical verification of inventories, though planned, may not have been carried out because of a strike or a lockout. An unfavorable comment without this explanation would be misleading;
  - to explain the fact why in spite of an unfavorable comment, the true and fair view of the financial statements is not vitiated. For example, physical verification of a part of the inventories at the year-end may not have been carried out, but there is sufficient other evidence produced by the management which satisfies the auditor regarding the existence, condition and value of the inventories.

# OTHER GENERAL MATTERS

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- If any of the comments on matters specified in the Order are adverse, the auditor should consider whether his comments have a bearing on the true and fair view presented by the financial statements and, therefore, might warrant a modification in the report under sub-sections (2), (3) and (4) of section 143.
- It should not, however, be assumed that every unfavorable comment under the Order would necessarily result in a qualification in the report under sub-sections (2) and (3) of section 143
  - Unfavorable comment may be regarding a matter which has no relevance to a true and fair view presented by the financial statements. Example, failure to deposit provident fund dues in time.
  - While the non-compliance may be material enough to warrant an unfavorable comment under the Order, it may not be material enough to affect the true and fair view presented by the financial statements.
  - Non-compliance may be in an area which calls for remedial action on the part of the management, and may be important for that reason but may not be sufficiently important in the context of the report under sub-sections (2) and (3) of section 143.

# QUESTIONS AND KNOWLEDGE SHARE

