

COMPANIES ACT 2013

Provisions as applicable for Audit & Accounts

Intensive Study Course on Companies Act,2013

Organised by WIRC of ICAI

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ACCOUNTS OF COMPANIES

- Chapter IX - Section 128 to 138

SECTION 128 - BOOKS OF ACCOUNTS ETC. TO BE KEPT BY COMPANY

- The Act recognizes the fact that books of accounts and other records may be kept in **electronic form** also in such manner as may be prescribed.
- To keep books of accounts & other relevant documents for every financial year at the **registered office**. May be kept at such other place in India as the Board may decide.
- Open for inspection **by any Director** at registered office or such other place during business hours.
- A director can inspect the book of accounts of the subsidiary, only with the authority of the Board of Directors.
- Preservation of books of accounts for at least **8 years** except in case of Investigation through Court Order.
- Penalty In case of non compliance of this section MD / WTD in charge of finance / CFO / Any other Person in charge is punishable with imprisonment up to 1 year **or** with fine of min 50,000/- and max 5,00,000/- **or** with both.

SECTION 129 - FINANCIAL STATEMENTS

- The term Balance sheet & Profit and Loss Account, has been defined collectively as “financial statement” under the Act. **Cash flow statement** and **Statement showing changes in equity**, if any, of the Company also included.
- Financial statement, with respect to **One Person Company, small company and dormant company**, may not include the cash flow statement.
- The financial statement shall be in the form or forms as may be provided for different class or classes of Companies in **Schedule III**.
- If one or more subsidiaries /associates /JVs than Consolidated Financial Statements (**CFS**) mandatory except those .
- CFS of all subsidiaries and the company shall be prepared and laid before the **AGM**.
- For the purpose of “financial statements”, “Subsidiary” shall include “Associate Company” and “Joint venture” applies only to holding company.

SECTION 129 - FINANCIAL STATEMENTS

- In case of **non compliance** of this section MD / WTD in charge of finance / CFO / Any other Person in charge is punishable with imprisonment up to 1 year **or** with fine of minimum 50,000/- and maximum 5,00,000/- **or** with both.
- **Company to attach a separate statement containing the salient features of the financial statements of its Subsidiaries in Form AOC-1 shall be certified same as balance sheet.**
- The requirement of attaching the Financial Statements and other reports as was required by **section 212** of the Companies Act 1956 has been dispensed with.
- In case of Companies covered under **section 135**, amount of expenditure incurred on corporate social responsibility activities needs to be disclosed in notes to accounts.
- **Exclusion** for insurance, banking and electricity companies which are governed by different statutes.
- **Rules 12** : AOC 4 within 30 days of AGM with ROC, Class or classes of companies as may be notified by the **CG** from time to time shall file their financial statements in **XBRL form**

SEC 129(3)- CONSOLIDATED FINANCIAL STATEMENTS

Where a company has one or more subsidiaries, it shall prepare a consolidated financial statement of the company and of all the subsidiaries in the same form and manner as that of its own which shall also be laid before the annual general meeting of the company along with the laying of its financial statement.

Provided that the company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries in such form as may be prescribed.

Provided further that the Central Government may provide for the consolidation of accounts of companies in such manner as may be prescribed.

Explanation.—For the purposes of this sub-section, the word “subsidiary” shall include associate company and joint venture.

SUBSIDIARY COMPANY [SECTION 2(87)]

- “Subsidiary company” or “Subsidiary”, in relation to any other company (that is to say the holding company), means a company in which the holding company—
 - (i) controls the composition of the Board of Directors; or
 - (ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:
- Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.
- Explanation.—For the purposes of this clause,—
 - (a) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;
 - (b) the composition of a company’s Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;
 - (c) the expression “company” includes any body corporate;
 - (d) “layer” in relation to a holding company means its subsidiary or subsidiaries;

ASSOCIATE COMPANY & CONTROL

Associate Company [Section 2(6)]

- 2(6) defines “Associate company”, in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.
- Explanation.—For the purposes of this clause, “significant influence” means control of at least twenty per cent. of total share capital, or of business decisions under an agreement;

Control [Section 2(27)]

- Control shall include the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting arrangements or in any other manner.

JOINT VENTURE

- Joint venture not defined.
- A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.
- Joint control is the contractually agreed sharing of control over an economic activity.
- Central Government empowered to exempt any company or class of companies from compliance of requirements of Section 129 in public interest

MANNER OF CONSOLIDATION – RULE 6 – COMPANY (ACCOUNTS) RULES, 2014

- The consolidation of financial statements of the company shall be made in accordance with provisions of Schedule III of the Act and the applicable accounting standards.
- Provided that in case of a company covered under sub-section (3) of Section 129 which is not required to prepare consolidated financial statements under the Accounting Standards, it shall be sufficient if the company complies with provisions on consolidated financial statements provided in Schedule III of the Act.
- *[Provided further that nothing in this rule shall in respect of preparation of consolidated financial statement by an intermediate wholly-owned subsidiary, other than wholly-owned subsidiary whose immediate parent is a company incorporated outside India.]*
- *[Provided also that nothing contained in this rule shall, subject to any other law or regulation, apply for the financial year commencing from the 1st day of April, 2014 and ending on the 31st day of March, 2015, in case of a company which does not have a subsidiary or subsidiaries but has one or more associate companies or joint ventures or both, for the consolidation of financial statement in respect of associate companies or joint ventures or both, as the case may be.] {14th October 2014}*
- *[Provided also that nothing contained in this rule shall apply in respect of consolidation of financial statement by a company having subsidiary or subsidiaries incorporated outside India only for the financial year commencing on or after 1st April, 2014.] {16th January 2015}*

CONSOLIDATED FINANCIAL STATEMENT (CFS)

Earlier :

- * Clause 32 of the Listing Agreement mandates Listed Companies to prepare CFS
- * Neither AS 21 nor Companies Act 1956 requires other company to prepare CFS

Companies Act 2013 :

- * Mandatory for all Companies to prepare CFS in respect of the Subsidiary, Associate, JV Co.
- * CFS will have to be done in addition to SFS
- * CFS should be prepared in same form and manner as Standalone Financial Statement (SFS) of holding company.

Impact :

- * All companies including private companies need to prepare CFS. They need to gear up their financial reporting process for the same.
- * CFS should comply with notified AS
- * Reopen and revision of accounts mandatory to CFS also

CONSOLIDATED FINANCIAL STATEMENTS

- **Consolidated financial statements now mandatory for all classes of companies**

- Increase the cost of compliance
- Duplication of information*: requirement to give *summary statement for all subsidiaries / associates / joint ventures continues*

[General Circular No. 39/2014 dated 14th October, 2014 states that in the CFS, the company would need to give all disclosures relevant for CFS only.]*

EXAMPLE

- A Ltd. has subsidiary as on 01 April 2014
- The subsidiary disposed off on 31 August 2014
- Is consolidation required on 31 March 2015?

EXAMPLE

- M Company holds a 70% interest in H Company. At the current year end M holds inventory purchased from H for Rs. 270,000 at cost plus 20%.
- The group's consolidated balance sheet has been drafted without any adjustments in relation to this holding of inventory.
- What adjustments should be made to the draft consolidated balance sheet figures for minority interest and retained earnings?

MI

Retained Earnings

- | | |
|------------------------|----------------------|
| • No change | Reduce by Rs. 54,000 |
| • Reduce by Rs. 13,500 | Reduce by Rs. 31,500 |
| • Reduce by Rs. 16,200 | Reduce by Rs. 37,800 |
| • No change | Reduce by Rs. 45,000 |

EXAMPLE

- H Ltd has acquired 95% stake in S Ltd. Resultant goodwill is Rs. 50 lacs
- Subsequently, S Ltd issues further equity that is being acquired by A Ltd.
- Hence, H Ltd's holding reduces to 85%.
- Should the goodwill be reduced?

DEPRECIATION

SCHEDULE II

OVERVIEW OF KEY CHANGES

- Overview of some of the key changes in the Schedule II to the Companies Act, 2013 as compared to erstwhile Schedule XIV to the Companies Act, 1956 are as follows:
 1. Schedule II prescribes indicative useful lives of various assets instead of Straight Line Method (SLM)/ Written Down Value (WDV) rates for calculating depreciation
 2. Useful lives prescribed for tangible assets only
 3. No life prescribed for intangible assets. Notified accounting standard to govern the same
 4. Depreciation is systematic allocation of the depreciable amount of an asset over its useful life.
 5. The depreciable amount of an assets is the cost of an asset or other amount substituted for cost, less its residual value

OVERVIEW OF KEY CHANGES

1. Useful life is the period over which an asset is expected to be available for use by an entity, or the number of production or similar units expected to be obtained from the asset by the entity. Schedule XIV of Companies Act, 1956 did not include such requirement.
2. Companies are allowed to follow different useful lives/residual value if an appropriate justification is given supported by technical advice.
3. Component accounting and useful life of a significant part of an asset to be determined separately
4. No separate rate for double/ triple shift; depreciation to be increased based on the double shift/triple shift use of the assets
5. Useful lives of fixed assets prescribed under schedule II are Act different from those envisaged under Schedule XIV of the Companies Act, 1956.
6. No reference to depreciation on low value assets

CONTINUOUS PROCESS PLANT

- “Continuous process plant” means a plant which is required and designed to operate for 24 hours a day.
- Companies can continue to follow the guidance note issued by the ICAI with regard to continuous process plant – “Guidance note on some important issues arising from the amendments to Schedule XIV to the Companies Act, 1956.”
- Concept of component accounting as stated in para 21 will be applicable for continuous process plants also.

DOUBLE/ TRIPLE SHIFT WORKING

- ❖ Under Schedule II, no separate rates/lives are prescribed for extra shift working

- ❖ It states :
 - Double shift = increase depreciation by 50%
 - Triple shift = increase depreciation by 100%

- ❖ The useful life as given in Schedule II is to be treated as based on single shift operations

- ❖ If a company uses its assets for single, double or triple shifts in a financial year/accounting period, the depreciation charge for no. of days operated for double/triple shift has to be increased by 50%/100%, as the case may be.

ILLUSTRATION: SHIFT BASED DEPRECIATION

- Cost of Asset=5,00,000/-
- Useful life=40 years
- Salvage Value (5%)=25,000/-

Particulars	Schedule II	Schedule XIV	Difference in Depreciation
Single Shift	$(5\text{lac}-25,000) / 40 = 11875$	$5 \text{ lac} \times 4.75\% = 23,750$	11,875
Double Shift	$11,875 + 5,938 = 17,813$	$5\text{lac} \times 7.42\% = 37,100$	19,287
Triple Shift	$11,875 + 11,875 = 23,750$	$5 \text{ lac} \times 10.34\% = 51,700$	27,950

ILLUSTRATION-SHIFT BASED DEPRECIATION (2/2)

Option 2:

9 years (15 years – 6 years)

[considering the plant was used on a triple shift basis on all days in the previous three years]

- Therefore, the carrying amount to be depreciated as -
 - Single Shift – 9 years
 - Double Shift – Depreciation as per single shift to be increased by 50%
 - Triple shift - Depreciation as per single shift to be increased by 100%

Option 3:

6 years (15 years – 9 years)

[considering the plant was used on a triple shift basis on all days in previous three years and each shift is considered to depreciate the asset equally]

- Therefore, the carrying amount to be depreciated as -
 - Single Shift – 6 years
 - Double Shift – Depreciation as per single shift to be increased by 50%
 - Triple shift - Depreciation as per single shift to be increased by 100%

ILLUSTRATION-SHIFT BASED DEPRECIATION (1/2)

- A Company purchased machinery 3 years prior to the commencement of the 2013 Act
- For all 3 years, machinery worked on triple shift and accordingly, asset is depreciated at 31.02% (as per old rate)
- Residual value – Nil
- On transition, balance useful life is -
- **Option 1:**
- **12 years (15 years – 3 years)**
- Therefore, the carrying amount to be depreciated as -
 - Single Shift - 12 years
 - Double Shift – Depreciation as per single shift to be increased by 50%
 - Triple shift - Depreciation as per single shift to be increased by 100%

TRANSITIONAL PROVISION UNDER SCHEDULE II

- The most important and challenging aspect of Schedule II is the effect to be given in the books of account on the date of transition, i.e. 1st April, 2014. Reproduced below is Note 7 to Part C of Schedule II,
- From the date this Schedule comes into effect, the carrying amount of the asset as on that date-
 - (a) shall be depreciated over the remaining useful life of the asset as per this Schedule;
 - (b) after retaining the residual value, shall be recognized in the opening balance of retained earnings where the remaining useful life of an asset is nil.”

TRANSITIONAL PROVISION-ACCOUNTING TREATMENT

Option 1: Debit to Retained Earnings

General Reserve Account	Dr	xx	
	To Provision for Depreciation Account		xx

Deferred Tax Liability Account	Dr	xx	
	To General Reserve Account		xx

Option 2: Debit to Statement of Profit and loss

Depreciation Account	Dr	xx	
	To Provision for Depreciation Account		xx

Profit And Loss Account	Dr	xx	
	To Depreciation		xx

Deferred tax Liability(or asset, as the case may be) for the year automatically gets adjusted

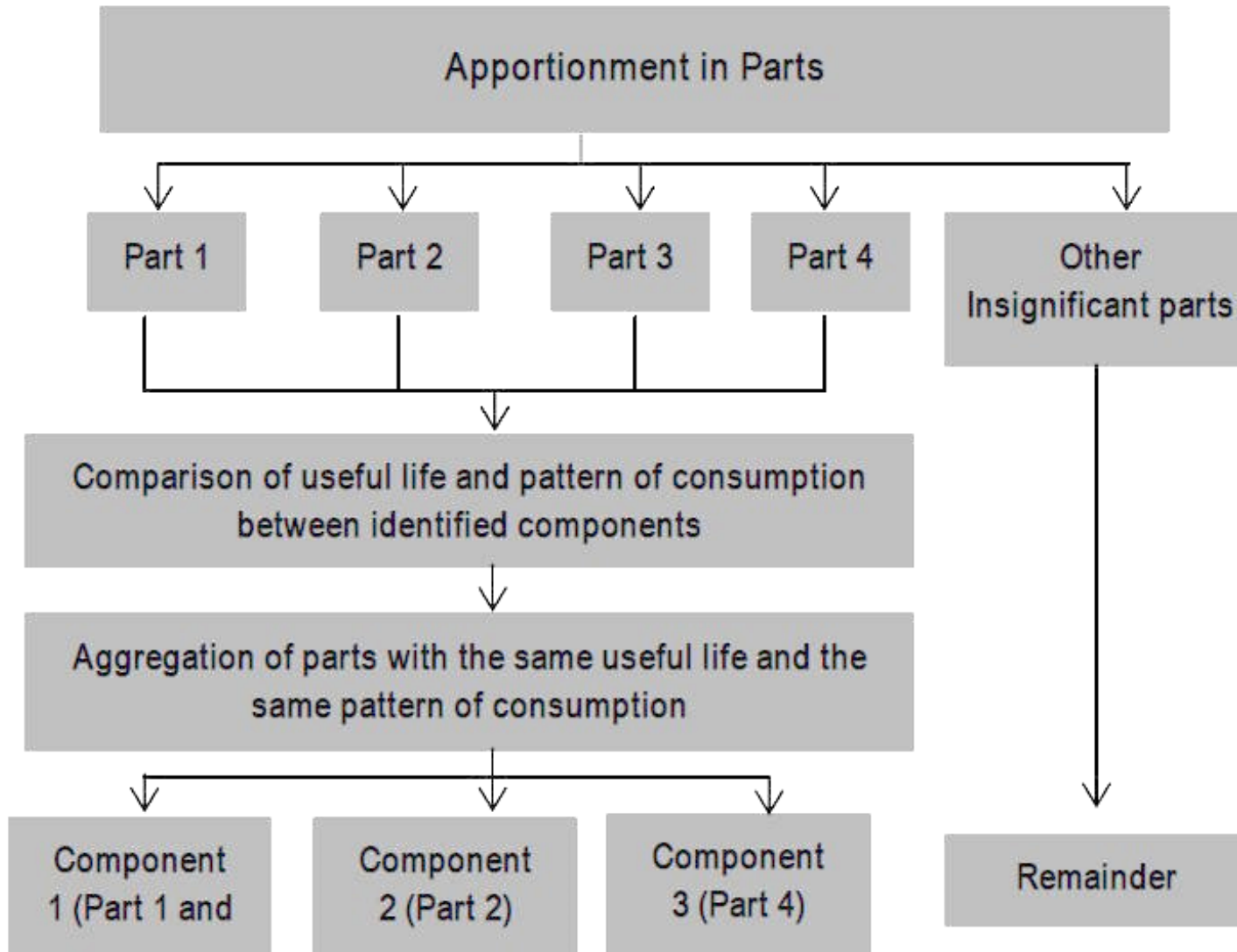
COMPONENT ACCOUNTING: OVERVIEW

- The Component Approach was already allowed under AS-10 but was optional. Schedule II requires application of component accounting mandatorily when relevant and material from 1.4.2015
- Useful life specified in Part C of the Schedule is for whole of the asset.
- Useful life of significant part shall be determined separately:
 - I. Where cost of a part of the asset is significant to total cost of the asset and;
 - II. Useful life of that part is different from the useful life of the remaining asset

COMPONENT ACCOUNTING: MATERIALITY

- A company needs to identify only material / significant components separately for depreciation
- Materiality is a matter of management / audit judgment and needs to be decided on the facts of each case
- Also consider impact on retained earnings, current year profit or loss and future profit or loss (say, when part will be replaced) to decide materiality
- If a component may have material impact from either perspective, the said component will be material and require separate identification

COMPONENT ACCOUNTING: ILLUSTRATION



COMPONENT ACCOUNTING .. CONTD.

- First split the fixed asset into various identifiable parts to the extent possible
- The identified parts are then grouped together if they have the same or similar useful life. No need to identify and depreciate insignificant parts as separate components; rather, they can be combined together in the remainder of the asset or with the principal asset.
- Identification of significant parts is a matter of judgment and to be decided on case-to-case basis. Identification of separate parts of an asset and determination of their useful life is not merely an accounting exercise; rather, it involves technical expertise. Hence, involve technical experts to determine the parts of an asset
- In case if useful life of component is lower than the useful life of the principal asset as per Schedule II such lower life should be used.
- If however the useful life of component is higher than the useful life of the principal asset as per Schedule II ,the company has a choice of using either the higher or lower useful life. However higher useful life can be used by management only if the intention to use the component exists even after expiry of the useful life for the principal asset.

ILLUSTRATIONS

Useful Life of Principal Asset Under Schedule II - 10 years

Management estimation of principal asset - 10 years

AS-6- Component Useful life - 8 years

Life of Component - 12 years

In this case the company can choose 10 years life as prescribed by Schedule II

For Some industries the determination is simple while for some industry it is complex process

- An IT company, which has only computers as fixed assets, may be able to determine with little analysis that there are no significant components requiring separate depreciation.
- However, for an airline company, it may be clear that engine has different useful life vis-à-vis remainder of the aircraft

COMPONENT ACCOUNTING: REPLACEMENT COSTS & MAJOR INSPECTION / OVERHAUL

- The application of component accounting will cause significant change in measurement of depreciation and accounting for replacement costs
- Presently, companies need to expense replacement costs in the year of incurrence. Under component accounting, companies will capitalize these costs as a separate component of the asset, with consequent expensing of net carrying value of the replaced component
- If it is not practicable for a company to determine carrying amount of the replaced component, it may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or constructed
- Even under the component accounting, a company does not recognize in the carrying amount of an item of fixed asset the costs of the day-to-day servicing of the item. These costs are expensed in the statement of profit and loss as incurred
- Major inspection/overhaul costs can be capitalized in certain cases and depreciated over the period during which the benefits of such costs are utilized e.g. 3 years or 5 years as the case may be

DEPRECIATION (SCHEDULE II)

- Can a company follow a longer useful life and higher residual value than that specified in Schedule II ?
- What are the requirement of componentization?

DEPRECIATION (SCHEDULE II)

- How do we as auditors ensure that “Componentisation” of assets is done correctly?
- Financial year end of a company is December 31, 2014, would the provisions of schedule II be applicable?

DEPRECIATION (SCHEDULE II)

- When the estimated useful life of an asset is changed, should the depreciation be charged prospectively or retrospectively?
- What are the provisions relating to assets working on double shift or triple shift basis?

DEPRECIATION (SCHEDULE II)

- ABC Limited had considered the minimum rates mentioned in the Schedule XIV of the Companies Act, 1956 for the depreciating all its fixed assets till March 31, 2014. Based on the rates mentioned for SLM and WDV in the Schedule XIV, ABC Limited has derived the useful life for the assets and considered the same useful life for its assets.

Schedule II of the Companies Act, 2013 is now applicable to ABC Limited w.e.f. April 1, 2014. Whether ABC Limited needs to follow the useful lives mentioned in the Schedule II or derived useful lives considered till March 31, 2013 can be considered?

SECTION 130 - REOPENING OF ACCOUNTS ON COURT'S OR TRIBUNAL'S ORDER (NEW PROVISION)

- Company shall neither reopen nor recast its accounts unless application made by CG / Income Tax / SEBI / Any other Regulatory Body; **and**
- An Order is passed by Court / Tribunal to the effect that accounts were prepared in fraudulent manner or affairs of the company were mismanaged.
- The accounts so revised or re-cast shall be final.

SECTION 131 - VOLUNTARY REVISION OF FINANCIAL STATEMENTS OR BOARD'S REPORT (NEW PROVISION)

- If financial statements or Board's report do not comply with provisions of the Act, the Board may prepare revised set for any of 3 preceding financial years after obtaining approval from Tribunal.
- **Revision not permitted more than once in a financial year.**
- Detailed reasons for such revision to be disclosed in Board's report.
- Copy of Tribunal's order shall be filed with ROC.

SECTION 134 - FINANCIAL STATEMENT, BOARD'S REPORT ETC.

- To be **signed by** either Chairperson or by 2 Directors (1 should be MD) **and** CEO, CFO and Company Secretary.
- Option available under the Companies Act, 1956 of signing by only one Director with explanations and reasons is dispensed with.
- In case of **One Person Company (OPC)**, Director Report should be signed by One Director only.
- **Additional Information to be included in Directors Report:**
 - a) The extract of **Annual Return** as prescribed under section 92.
 - b) In case of a company which are required to constitute **Nomination and Remuneration Committee**, Company's policy on Directors appointment and remuneration including criteria for determining qualification, positive attributes, independence of a Director etc.
 - c) Explanations or Comments by the Board on every qualification, reservation or adverse remark or disclaimer made by Practicing Company Secretary (PCS) in it's **Secretarial Audit Report.**

SECTION 134 - FINANCIAL STATEMENT, BOARD'S REPORT ETC.

- d) Particulars of **Loans, guarantees or Investments** under section 186.
- e) Particulars of contracts or arrangements with **related parties**.
- f) **Material changes and commitments post balance sheet date**, if any, affecting the financial position of the company.
- g) *A statement indicating development & implementation of a risk management policy for the company.*
- h) The details about policy developed and implemented on **CSR** initiatives taken during the year.
- i) Listed company and every other public company having a paid up share capital of 25 crores rupees or more to include **statement on formal annual evaluation** of the performance of Board, its committees and individual directors.

SECTION 135 CORPORATE SOCIAL RESPONSIBILITY (NEW PROVISION)

- Section 135 and Schedule VII shall come into force from 1st April 2014.
- CSR mandatory for every company having Net worth of \geq Rs. 500 cr., or Turnover of \geq Rs. 100 cr. or a Net Profit of \geq Rs. 5 cr. during any financial year
- **CSR Committee** to monitor & recommend company's activities & spending.
- To spend in every financial year, at least 2% of the average net profits of last 3 FYs.
- To **display CSR policy** on company's **website**.
- CSR activities specified in **Schedule VII**.
- Preference on spending for local & surrounding areas.
- In case of default, Board to disclose reasons in its report.
- If company ceases to be covered under section 135 for 3 consecutive financial years, it is neither required to constitute CSR committee nor shall it comply with provisions of this section till such time it meets the criteria defined in the section.
- CSR activities through registered trust or a registered society or a company established by the company or its holding or subsidiary or associate company under section 8.

SECTION 137 – COPY OF FINANCIAL STATEMENTS TO BE FILED WITH REGISTRAR

- FS duly adopted in AGM to be filed with ROC **within 30 days** of AGM.
- If FS not adopted in AGM, **provisional FS** can be filed within 30 days till the time FS are approved and filed with ROC.
- To attach FS of **foreign subsidiaries** which have not established place of business in India.
- **One Person Company** to file FS duly adopted by its members **within 180 days** from close of FY.

SECTION 138 - INTERNAL AUDIT (NEW PROVISION)

- Internal Audit of the functions and activities of the company.
- Applicable to listed and prescribed class of companies
- IA can be done by CA / CWA / Other professional decided by the Board.
- 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
- Every listed company
- Every public company having paid up share capital of rupees **50 crore or more**
- Turnover of **200 crores or more**
- every other public company which has any outstanding loans or borrowings from banks or public financial institutions exceeding **100 crore** rupees or which has accepted deposits of **twenty five crore** rupees or more at any point of time during the last financial year
- Every Private limited company only first criteria of share capital and deposits limits not to consider from above others limits same as above.

AUDIT AND AUDITORS

- Chapter X - Section 139 to 148

SECTION 139 – APPOINTMENT OF AUDITORS

- First auditor to be appointed by Board within 30 days from incorporation. Upon failure members to appoint in EGM within 90 days.
- Subsequent appointment at first AGM.
- Auditor to hold office till conclusion of 6th AGM.
- **Ratification** by members at every AGM.
- **The company has to intimate both Auditor and Registrar within 15 days of the appointment.**
- The Auditor is also required to give a certificate that he is duly qualified to be appointed as the Auditor of the Company.
- In case of Government Companies, the First Auditor shall be appointed by the Comptroller and Auditor General (**CAG**) within 60 days from the date of incorporation and on failure to do so, the Board shall appoint auditor within next 30 days, and on failure to do, the members will appoint the Auditor within 60 days who shall hold office till conclusion of first AGM.
- 2 or more joint auditors, the rotation of auditors in such a manner that all of the joint auditors do not complete their term in the same year
- In case of existing Government companies, the CAG shall appoint the Auditor within the period of 180 days from the commencement of the financial year and the auditor so appointed shall hold it position till the conclusion of the Annual general Meeting.
- *The provisions for rotation of Auditors in the listed Company & Certain other class of Companies, as may be prescribed, have been provided for.*
- **Maximum 5 years for individual CA and 10 years for CA firm.**
- **Cooling period of continuous duration of 5 years.**
- No firm to be appointed having common partner / partners.
- **Transition period:** 3 years from the commencement of the Act has been prescribed for the companies existing on or before the commencement of the Act, to comply with the provision of the rotation of Auditor.
- Members can resolve to change audit partner and audit team.
- Casual vacancy to be filled by Board within 30 days except in case of resignation of an auditor.
- In case the Company has an audit committee, then all appointment of Auditors including filling of casual vacancy, shall be made after taking into account the recommendation of the committee.

SECTION 140 – REMOVAL, RESIGNATION OF AUDITOR AND GIVING OF SPECIAL NOTICE

- When the Auditor of a Company **other than Government Company**, resigns from the Company, then is required to **file** a statement in prescribed **form** within **30 days** with the Company and the Registrar and also **approval at GM** to be called in **3month**.
- In case of **Government Company**, such statement shall be *filed with* the CAG. The statement shall indicate the reasons and other facts as may be relevant with regards to his resignation.
- Penalty has also been prescribed where Auditor fails to file such statement.
- A new provisions has been introduced whereby the Tribunal suo-moto or on an application from CG / person concerned, can direct the company to change the Auditor if it is satisfied that the Auditor 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.
- In case of a firm liability will be of firm and partner(s) who acted in fraudulent manner.
- **Removal of Auditor by special resolution AND CG approval.**
- Auditor shall be given reasonable opportunity of being heard.
- Special notice required for appointing auditor other than retiring auditor.

SECTION 141 – ELIGIBILITY, QUALIFICATIONS AND DISQUALIFICATIONS OF AUDITORS

- A firm in which majority of partners are practicing CA 's can also be appointed; i.e. the **multi-disciplinary firms** having professionals from variety of fields like CA, CWA, PCS or Lawyers etc.)

New disqualifications introduced for appointment:

- If a person by himself or his relative or partner is holding security of company/subsidiary/its holding/associate company/subsidiary of such holding company of **above rs one lac**
- If he is **indebted** to the company / subsidiary / holding / associate company / fellow subsidiary in excess of such amount as may be prescribed. (**above rs. Five lacs**)
- Has given a **guarantee** or provided any security in connection with indebtedness of any third person to the company / subsidiary / holding / associate company / fellow subsidiary for such amount as may be prescribed. (**above rs one lac**)
- If a person or a firm **directly or indirectly has business relationship** with the company or its subsidiary or of its holding or associate company or subsidiary of such holding company.
- A person whose **relative** is a Director or is in **employment** of the company as a Director or KMP.

SECTION 141 – ELIGIBILITY, QUALIFICATIONS AND DISQUALIFICATIONS OF AUDITORS

- A person **whose relative is a Director** or is in employment of the company as a Director or KMP.
- A person who has been convicted by a **Court** of an offence involving fraud and a period of **10 years** has not elapsed from date of such conviction.
- If any person whose subsidiary or associate company or any other form of entity is engaged in any of the consulting and specialized services as provided under section 144 shall not be eligible for appointment.
- **Maximum number of audits 20 for each individual / partner. However OPC, DORMANT, SMALL AND PVT CO HAVING PAID UP CAPITAL OF <100 CR NOT INCLUDED.**

AUDIT REPORT UNDER NEW LAW

- Companies Act, 2013
 - Section 143 (1)
 - Section 143(2)
 - Section 143(3)
 - Section 143(5)
 - Section 143(11)
 - Section 145
- Standards of Auditing – Section 143(9) and 143(10)
- Indian Accounting Standards – Section 129 read with Section 133
- Company (Audit & Auditors) Rules, 2014
- Auditing pronouncements by ICAI
- Section 45 MA of the Reserve Bank of India Act, 1934

FORM OF STANDARD AUDITOR'S REPORT

1. Title
2. Addressee
3. Report on the Consolidated or Standalone Financial Statements
4. Introductory Paragraph
5. Management's Responsibility for the Standalone Financial Statement
6. Auditor's Responsibility
7. Auditor's Opinion
8. Report on Other Legal and Regulatory Requirements
9. Signature of the Auditor
10. Date of the Auditor's Report
11. Place of Signature

* Silent about Letter head of the Auditor

SECTION 143 – POWERS AND DUTIES OF AUDITORS AND AUDITING STANDARDS

- Comply with auditing standards.

The Auditors Report shall now also be required to provide for the following

- **Qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;**
- **Whether the Company has adequate internal financial controls system in place and the operating effectiveness of such controls;**
- Auditor is required to provide the reasons, where any of the matters required to be included in the Audit Report under this section is answered in negative or with a qualification, which was not required under the old law.
- The Auditor shall now also inquire in case of Company not being an Investment Company or Banking Company, whether the assets of the Company consisting of shares, debentures and other securities have been sold at a price less than at which they are purchased by the Company.

SECTION 143 (3)

- The auditor's report shall also state—
 - (a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;
 - (b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;
 - (c) whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

SECTION 143 (3)(CONTD.)

- (d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;
- (e) whether, in his opinion, the financial statements comply with the accounting standards;
- (f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;
- (g) whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;
- (h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;
- (i) whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls;
- Note; Auditor reporting on existence and operation of internal financial controls made optional for the year ending March 31, 2015. However, Directors reporting obligations to continue
- (j) such other matters as may be prescribed

SECTION 143(3)(f)

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

- “the expression ‘adverse effect of the functioning of the company’ should not be interpreted to mean that any event affecting the functioning of the company, observed by the auditor, should be reported upon, even though it does not affect the financial statements”
- Concept of materiality is to be applied. – SA 200
- Ordinarily matters that are pervasive in nature such as going concern or matters that will significantly impact the operations of the company due to its size and nature will need to be reported under this clause.
- There is no change in the objective and scope of an audit of financial statements due to the inclusion of this clause.
- Matters to be reported under this clause even if such observation did not result in a modification to the audit opinion on the financial statements of the company.

SECTION 143(3)(h)

Any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

- The words - qualification, adverse remark, or reservation shall be construed as qualified opinion, adverse opinion and disclaimer of opinion as referred to SA 705.
- Reporting under this clause will not be required if there are no modifications i.e. no qualified, adverse or disclaimer of opinion and there are no such observations under Section 143(3)(b) of the said Act, regarding books of accounts kept by the company.
- An emphasis of matter is not in the nature of a qualification, reservation or adverse remark.

FRAUD REPORTING

FRAUD REPORTING UNDER SECTION 143(12)

- Statutory auditors including branch auditors [Cost Auditor and Secretarial Auditor] to report to the Central Government [within 60 days] about the fraud/suspected fraud committed against the company by the officers or employees of the company
 - Does not include fraud by third parties such as vendors and customers.
 - Internal auditor, VAT auditors, Tax Auditors etc. are not covered
 - Reporting of fraud by auditors under Form ADT -4 [Rule 13 of the Companies (Audit and Auditors) Rules, 2014]
 - GN issued on fraud reporting
 - SA 240 The Auditor's Responsibilities relating to Frauds in An Audit of FS
 - Clarity on applicability of section 143(12) for limited reviews is given in GN
- Companies (Amendment) Act 2015 passed on 26th May 2015 deals with:
 - Materiality levels (threshold limit) for reporting to CG. [limits not notified]
 - Below threshold limits, Auditor has to report to ACM or Board
 - Cases not reported to CG, should be disclosed in Board Report

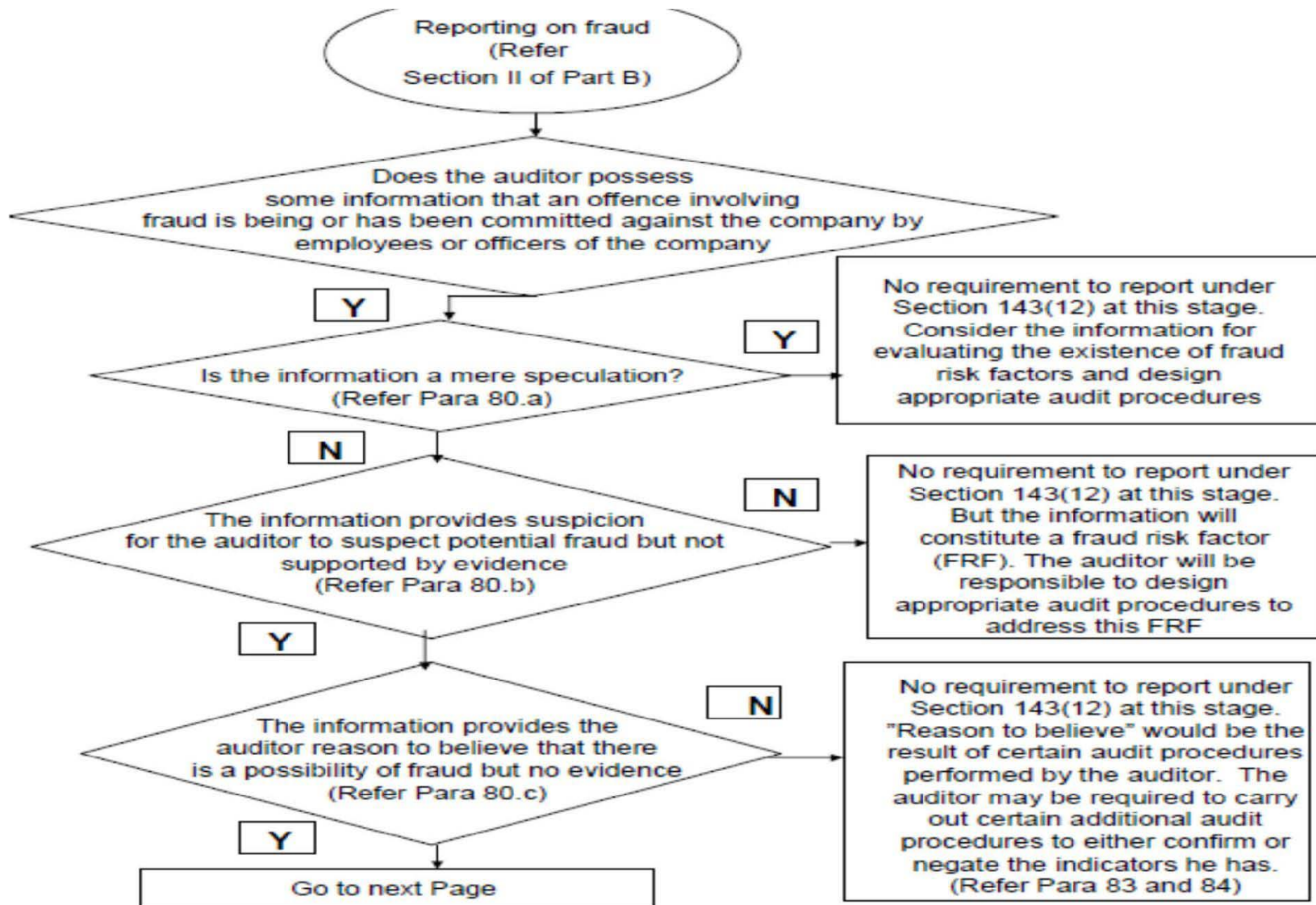
FRAUD REPORTING UNDER SECTION 143(12)

- Fraud as defined in the Explanation to Section 447 of Companies Act, 2013 – “Fraud” in relation to affairs or any body corporate, includes
 - any act, omission, concealment of any fact or abuse of position
 - committed by any person or any other person with the connivance in any manner,
 - with intent to deceive, to gain undue advantage from, or to injure the interests of, the Company or its shareholder or its creditors or any other person,
 - whether or not there is any wrongful gain wrongful loss.
- “wrongful gain” means the gain by unlawful means of property to which the person gaining is not legally entitled.
- “wrongful loss” means the loss by unlawful means of property to which the person losing is legally entitled .

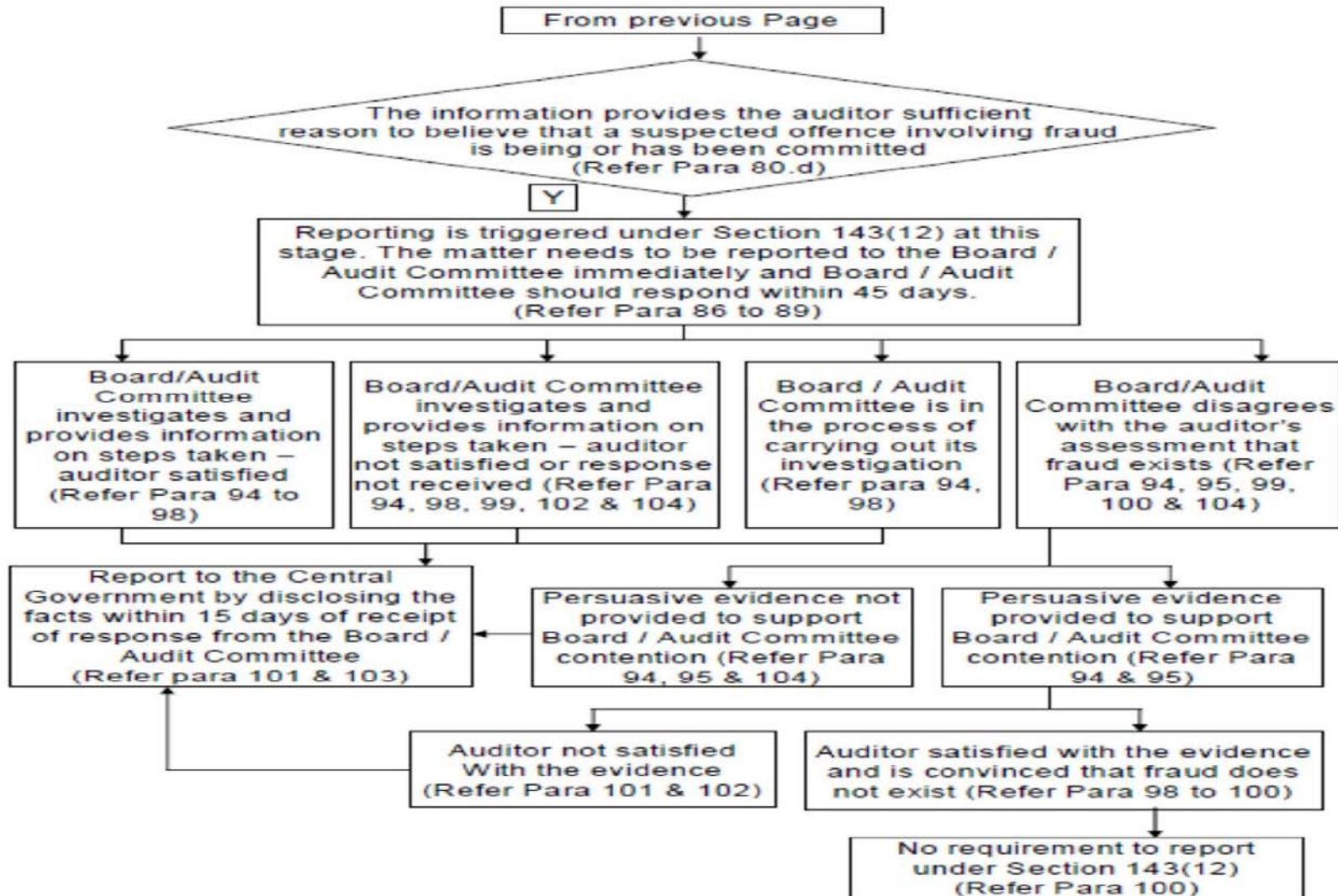
FRAUD REPORTING UNDER SECTION 143(12)

- The Guidance Note provides an overview of reporting requirement u/s 143(12). It also provides detailed guidance w.r.t various aspects of this reporting requirement like requirements for reporting u/s 143(12), responsibility of management, responsibility of auditor, Issues for consideration by the auditors, Applicability of Standards on Auditing, Audit procedures Technical guidance, Appendices etc.
- Review Steps taken by management, if not taken within 45days auditor to Report under ADT-4.
- **Non compliance of provisions attracts penalty ranging from Rs. 1 lakh to Rs. 25 lakhs.**
- *The Companies (Amendment) Bill, 2014 that was passed by the Lok Sabha, envisaged bringing in, by way of Rules, certain materiality thresholds in respect of reporting under section 143(12) As and when the aforesaid Bill is passed by the Rajya Sabha, it will be reviewed if and where required.*

FLOW CHART AS GIVEN IN GN



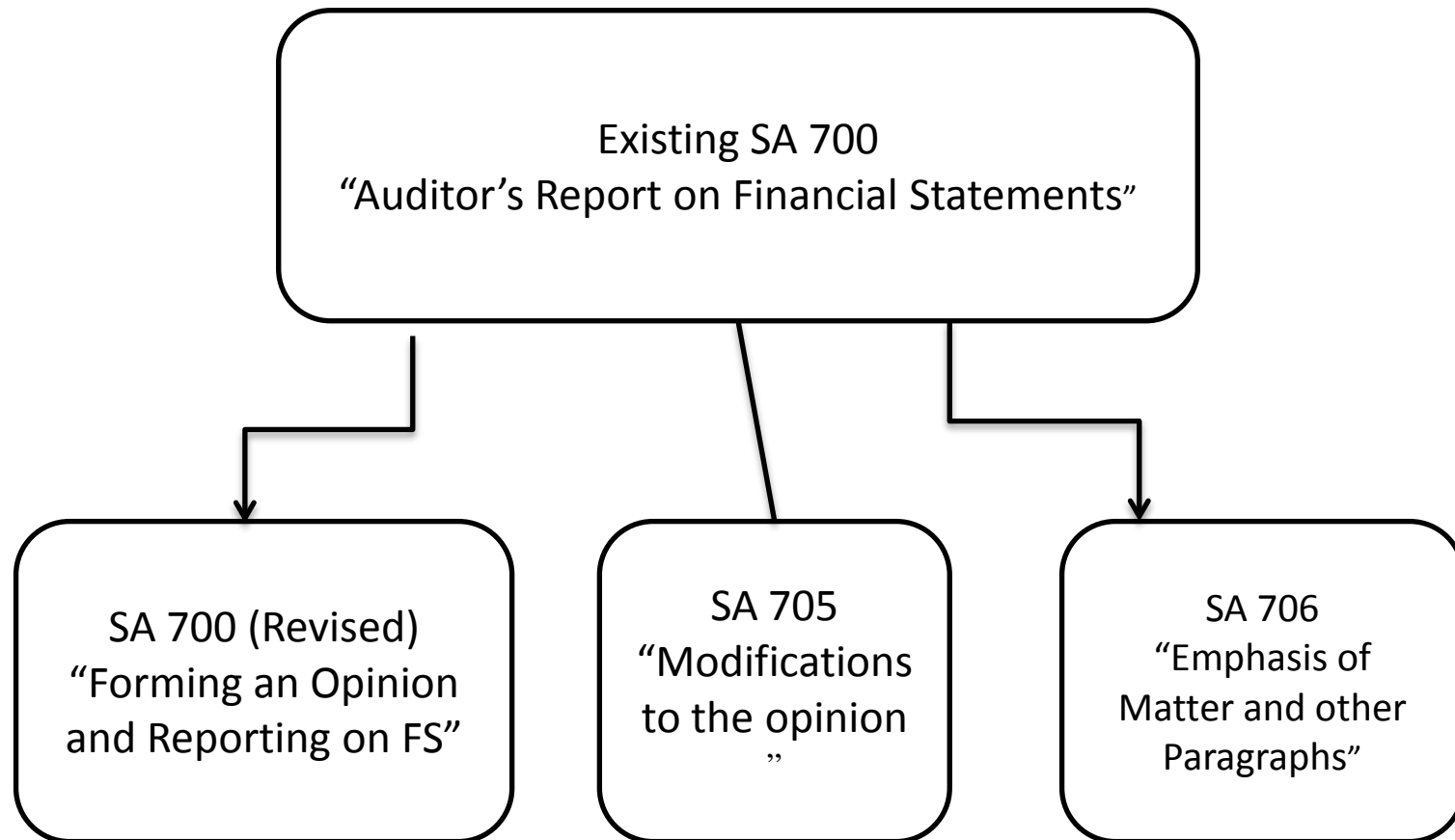
(CONTINUED) FLOW CHART AS GIVEN IN GN



RULE 11 : OTHER MATTERS TO BE INCLUDED IN AUDITORS REPORT.

- The auditor's report shall also include their views and comments on the following matters, namely:-
 - (a) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;
 - (b) whether the company has made provision, as required under any 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 company.

STANDARDS OF AUDITING – SECTION 143(9) AND 143(10)



CARO 2015

- **Applicability Of CARO 2015** :- Every company including a *foreign company* u/s 2(42) of CA, 2013.
- **Non-Applicability of CARO 2015** :-
 - (a) A Banking Company as defined in Section 5(c) of the Banking Regulation Act, 1949;
 - (b) An Insurance Company as defined under the Insurance Act, 1938;
 - (c) A company licensed to operate under Section 8 of the Companies Act;
 - (d) A One Person Company as defined u/s 2(62) of the Companies Act and a small company as defined u/s 2(85) of the Companies Act; and
 - (e) A Private Limited Company with a Paid up Capital and Reserves up to Rs. 50 Lakhs Loan Outstanding up to Rs. 25 Lakhs from any bank or financial institution and Turnover up to Rs. 5 crores at any point of time during the financial year.

CARO 2015 (CONTD.)

- **Matters to be included in the auditor's report – CARO 2015**

- **Fixed Assets –**

Maintenance + Physical Verification + Discrepancy Maintenance of proper records showing full particulars, including quantitative details and situation of fixed assets;

Physically verified by the management at reasonable intervals;

If any material discrepancies on verification then, properly dealt with in the books of account;

- **Inventory –**

Maintenance + Physical Verification + Procedures + Discrepancy Maintenance of proper records showing full particulars, including quantitative details; Physical verification of inventory at reasonable intervals by the management; Procedures of physical verification followed by the management reasonable and adequate in relation to the size of the company and the nature of its business. If procedure inadequate it should be reported; If any material discrepancies on verification then, properly dealt with in the books of account;

CARO 2015 (CONTD.)

- **Loans Given –**

Granted + Repayment + Recovery Granted any loans, secured or unsecured to companies, firms or other parties covered in the register maintained u/s 189 of the Companies Act; Receipt of the Principal amount and Interest are also regular; and If overdue amount is more than rupees one lakh, whether reasonable steps have been taken by the company for recovery of the principal and interest;

- **Internal Control System –**

Adequate ICS + Weakness in ICS Adequate internal control system(ICS) commensurate with the size of the company and the nature of its business, ICS for the purchase of inventory and fixed assets and for the sale of goods and services. Report on continuing failure to correct major weaknesses in ICS.

CARO 2015 (CONTD.)

- **Accept Deposits –**

RBI Directions Compliances + Order of CLB/NCTL/RBI/Court Compliances Accepted Deposits as per direction by RBI and u/s 73 to 76 or any other relevant provisions of the Companies Act and the rules complied with; If not complied, the nature of contraventions should be stated; If an order has been passed by CLB or NCLT or RBI or any court or any other tribunal, whether the same has been complied with or not?

- **Cost Records –**

Maintenance as specified by CG Maintenance of cost records has been specified by the Central Government u/s 148(1) of the Companies Act; Whether such accounts and records have been made and maintained;

CARO 2015 (CONTD.)

○ Statutory Dues –

Depositing Regularly + O/s 6 months reported + Amount & Forum mentioned + Transfer to IEPF Regular in depositing undisputed statutory dues including PF, ESI, income-tax, sales-tax, wealth tax, service tax, duty of customs, duty of excise, **value added tax**, cess and any other statutory dues with the appropriate authorities; If the arrears of O/s statutory dues as at the last day of the FY concerned for a period of more than six months from the date they became payable, shall be indicated; In case dues of taxes or cess have not been deposited on account of any dispute – Amount involved and the forum where dispute is pending shall be mentioned; (A mere representation to the concerned Department shall not constitute a dispute) Amount transferred to investor education and protection fund in accordance with the relevant provisions of the Companies Act, and rules within time.

CARO 2015 (CONTD.)

- **Accumulated Losses –**

Reg. 5 yrs Co. + Acc. Losses min. 50% of Net Worth + Cash Losses in FY and Preceding FY Company which has been registered for a period not less than five years – its accumulated losses at the end of the FY are not less than 50% of its net worth; and Whether it has incurred cash losses in such FY and in the immediately preceding FY;

- **Repayment Defaults –**

To Bank/FI/Debenture holders + Report-Period & Amount Defaulted in repayment of dues to a financial institution or bank or debenture holders; The period and amount of default to be reported.

- **Guarantee Given –**

Loan taken by others + T&C are not prejudicial Given any guarantee for loans taken by others from bank or financial institutions; Terms and conditions are prejudicial to the interest of the company.

CARO 2015 (CONTD.)

- **Term Loans –**

Applied for Purpose Term loans were applied for the purpose for which the loans were obtained;

- **Fraud –**

On/By Company + Report-Nature & Amount Whether any fraud on or by the company has been noticed or reported during the year; The nature and amount involved is to be indicated.

SECTION 144 – AUDITOR NOT TO RENDER CERTAIN SERVICES

- Auditor not to render **directly or indirectly** following services to company / holding company / subsidiary company:
 - 1) Accounting & book keeping services,
 - 2) internal audit,
 - 3) design and implementation of any financial information system,
 - 4) actuarial services,
 - 5) investment advisory services,
 - 6) investment banking services,
 - 7) rendering of outsourced financial services,
 - 8) management services and
 - 9) any other kind of services as may be prescribed.
- “**Directly or indirectly**” shall include:
 - **Individual Auditor:** either by himself or through his relative or any other person connected or associated with such individual or through any other entity, whosoever, in which such individual has significant influence or control, or whose name or trademark or brand is used by such individual.
 - **Audit Firm:** Rendering of services either by itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever in which the firm or any partner of the firm has significant influence or control or whose name or trademark or brand is used by the firm or any of its partners.
 - **Transition Period:**
Auditors or audit firms providing non-audit services before the commencement of the new Act shall have to comply with provisions of this section before the closure of the first financial year after the commencement of this Act

SECTION 147 – PUNISHMENT FOR CONTRAVENTION

Specific penalty has been prescribed for contravention of provisions related to appointment of Auditors.

- In case of contravention related to this Chapter the company shall be punishable with fine ranging from **25,000/- to 5,00,000/-** **AND** any officer who is in default shall be punishable **with imprisonment** for a term up **to 1 year or with fine ranging from 10,000/- to 1,00,000/- or with both.**
- If auditor contravenes provisions of section 139 / 143 / 144 / 145, he shall be punishable with fine ranging **from 25,000/- to 25,00,000/-.**
- Where auditor has wilfully or knowingly contravened the provisions with the intention to deceive the company / shareholders / creditors / tax authorities then he shall be punishable with imprisonment up to 1 year or fine ranging from **1,00,000/- to 25,00,000/-** or with both.

SECTION 147 – PUNISHMENT FOR CONTRAVENTION

- If auditor contravenes the provisions related to his powers and duties (143), Services that he cannot render (144) and attendance of general meeting (146) he shall be further liable to:
- refund the remuneration received by him to the company; and
- pay for damages to the company, statutory bodies or authorities or to any other persons for loss arising out of incorrect or misleading statements of particulars made in his audit report.
- If it is proved that partner or partners of audit firms has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, or by the company or its Directors or officers, then partner or concerned partners of the audit firm and the firm shall be jointly and severally responsible for the liability, whether civil or criminal as provided in this Act or in any other law for the time being in force.

**“when we are no longer
able to change a situation,**

**we are challenged to change
ourselves!”**

Victor Frank

THANK YOU.....

CA DURGESH KABRA

FOUNDER PARTNER

DMKH & Co.

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