

**JK SHAH CLASSES FINAL CA AUDIT- AMENDMENTS AND RTP FOR MAY 17 attempt-
Simplified Notes**

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SA 610 (REVISED) USING THE WORK OF INTERNAL AUDITOR (APPLICABLE FROM 1ST APRIL 2016)

PM QUESTION

In the course of the statutory audit of Z Ltd, its statutory auditors, having determined that the work of internal auditor is likely to be adequate for the purpose of statutory audit, wanted to use the work of internal auditor in respect of physical verification of fixed assets. How an evaluation of this specific work done by the internal auditor can be done?

CA. Amboj, a practicing chartered accountant has been appointed as an internal auditor of Textile Ltd. He conducted the physical verification of the inventory at the year-end and handed over the report of such verification to CA. Kishor, the statutory auditor of the Company, for his view and reporting. Can CA. Kishor rely on such report?

- This Standard on Auditing (SA) deals with the external auditor's responsibilities if using the work of internal auditors. This includes (a) using the work of the internal audit function in obtaining audit evidence and (b) using internal auditors to provide direct assistance under the direction, supervision and review of the external auditor.
- The external auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the external auditor's use of the work of the internal audit function or internal auditors to provide direct assistance on the engagement.
- While using the work of internal auditor, external auditor shall determine whether
 - Internal auditor is objective in performing his procedures
 - Internal audit function is reasonably independent
 - Internal auditor has taken due professional care while performing his procedures
 - Scope of internal audit is not limited by the management
 - Internal auditor has obtained reasonable evidence supporting his judgment
- USING DIRECT ASSISTANCE if not prohibited by law and regulation:

Prior to using internal auditors to provide direct assistance for purposes of the audit, the external auditor shall:

(a) Obtain written agreement from an authorized representative of the entity that the internal auditors will be allowed to follow the external auditor's instructions, and that the entity will not intervene in the work the internal auditor performs for the external auditor; and

(b) Obtain written agreement from the internal auditors that they will keep confidential specific matters as instructed by the external auditor and inform the external auditor of any threat to their objectivity.

The external auditor shall direct, supervise and review the work performed by internal auditors on the engagement in accordance with SA 220.

The direction, supervision and review by the external auditor of the work performed by the internal auditors shall be sufficient in order for the external auditor to be satisfied that the internal auditors have obtained sufficient appropriate audit evidence to support the conclusions based on that work.

SRE 2400: Engagements to Review Historical Financial Information

1) A practitioner, who is not the auditor of an entity, undertakes an engagement to review financial statements and on the form and content of the report that the practitioner issues in connection with such a review.

2) A review engagement provides a moderate level of assurance that the information subject to review is free of material misstatement, this is expressed in the form of negative assurance

3) The objective is to check whether anything has come to the practitioner's attention that causes the practitioner to believe that the financial statements are not prepared, in all material respects, in accordance with the applicable financial reporting framework (negative/limited assurance)

4) The agreed terms of engagement shall be recorded in an engagement letter or other suitable form of written agreement, and shall include:

(a) The intended use and distribution of the financial statements, and any restrictions on use or distribution where applicable;

(b) Identification of the applicable financial reporting framework;

(c) The objective and scope of the review engagement;

(d) The responsibilities of the practitioner;

(e) The responsibilities of management

(f) A statement that the engagement is not an audit, and that the practitioner will not express an audit opinion on the financial statements; and

(g) Reference to the expected form and content of the report to be issued by the practitioner, and a statement that there may be circumstances in which the report may differ from its expected form and content.

5) Procedures for the review of financial statements

- Obtaining an understanding of the entity's business and the industry in which it operates.
- Inquiries concerning the entity's accounting principles and practices.

- Inquiries concerning the entity's procedures for recording, classifying and summarising transactions, accumulating information for disclosure in the financial statements and preparing financial statements.
- Inquiries concerning all material assertions in the financial statements.
- Analytical procedures designed to identify relationships and individual items that appear unusual. Such procedures would include:
 - Comparison of the financial statements with statements for prior periods.
 - Comparison of the financial statements with anticipated results and financial position.
 - Study of the relationships of the elements of the financial statements that would be expected to conform to a predictable pattern based on the entity's experience or industry norm.

FORMAT OF REPORT:

INDEPENDENT PRACTITIONER'S REPORT

Dear Management,

Intro para

Management Responsibility

Practitioner's Responsibility

Conclusion

Basis of accounting and Restriction on distribution and use

SAE 3420: Assurance Engagements to Report on Compilation of Pro forma financial information included in a prospectus

This SAE deals with reasonable assurance engagements undertaken by a practitioner to report on the responsible party's (management) compilation of pro forma financial information included in a prospectus.

In accounting, pro forma refers to a statement of a company's financial doings, that excludes unusual or nonrecurring transactions, when reporting the company's earnings. Excluded expenses typically include declining investment values, restructuring costs and adjustments made on the company's balance sheet that fix faulty accounting practices from other years.

The objectives of the practitioner are:

- (a) To obtain reasonable assurance about whether the pro forma financial information has been compiled, in all material respects, by the responsible party on the basis of the applicable criteria; and
- (b) To report in accordance with the practitioner's findings.

The SAE applies where:

Such reporting is required by securities law or the regulation of the securities exchange (“relevant law or regulation”) in the jurisdiction in which the prospectus is to be issued; or This reporting is generally accepted practice in such jurisdiction.

The practitioner has no responsibility to compile the pro forma financial information for the entity; such responsibility rests with the responsible party.

The practitioner’s sole responsibility is to report on whether the pro forma financial information has been compiled, in all material respects, by the responsible party on the basis of the applicable criteria.

Before agreeing to accept an engagement, the practitioner shall:

- (a) Determine that the practitioner has the capabilities and competence to perform the engagement;
- (b) Determine that the applicable criteria are suitable and that it is unlikely that the pro forma financial information will be misleading for the purpose for which it is intended;
- (c) Evaluate the wording of the opinion prescribed by the relevant law or regulation, if any, to determine that the practitioner will likely be able to express the opinion so prescribed based on performing the procedures specified in this SAE;
- (d) Where the sources from which the unadjusted financial information have been extracted, have been audited or reviewed and a modified audit opinion or review conclusion has been expressed, or the report contains an EOM paragraph, consider whether or not the relevant law or regulation permits the use of, or reference in the practitioner’s report to, the modified audit opinion or review conclusion or the report containing the EOM paragraph with respect to such sources;
- (e) If the entity’s historical financial information has never been audited or reviewed, consider whether the practitioner can obtain a sufficient understanding of the entity and its accounting and financial reporting practices to perform the engagement;
- (f) Obtain the agreement of the responsible party that it acknowledges and understands its responsibility for:
 - (i) Adequately disclosing and describing the applicable criteria to the intended users;
 - (ii) Compiling the pro forma financial information on the basis of the applicable criteria

Audit Procedures

Assessing the Suitability of the Applicable Criteria

Obtaining an Understanding of how the Responsible Party has Compiled the Pro Forma Financial Information and Other Engagement Circumstances

Obtaining Evidence about the Appropriateness of the Source from Which the Unadjusted financial Information Has Been Extracted

Obtaining evidence of the appropriateness of the Pro Forma Adjustments

Evaluating the Presentation of the Pro Forma Financial Information

Obtain Written representations

REPORT FORMAT AND CONSIDERATIONS

The practitioner's report shall include the following basic elements:

- (a) A title that clearly indicates that the report is an independent assurance report;
- (b) An addressee(s), as agreed in the terms of engagement;
- (c) Introductory paragraphs that identify:
 - (i) The pro forma financial information;
 - (ii) The source from which the unadjusted financial information has been extracted,;
 - (iii) The period covered by, or the date of, the pro forma financial information; and
 - (iv) A reference to the applicable criteria on the basis of which the responsible party has performed the compilation of the pro forma financial information, and the source of the criteria;
- (d) A statement that the responsible party is responsible for compiling the pro forma financial information on the basis of the applicable criteria;
- (e) A description of the practitioner's responsibilities,
- (f) A statement that the engagement was performed in accordance with SAE 3420
- (h) Unless otherwise required by law or regulation, the practitioner's opinion using one of the following phrases, which are regarded as being equivalent:
 - (i) The pro forma financial information has been compiled, in all material respects, on the basis of the (applicable criteria); or
 - (iii) The pro forma financial information has been properly compiled on the basis stated;

SRS 4410- Engagements to Compile financial information

- This SRS addresses engagements where the practitioner assists management in the preparation and presentation of historical financial information. The SRS may, however, also be applied, adapted as necessary, when the practitioner is engaged to assist management in preparing and presenting other financial information. Examples include:
 - Pro forma financial information.
 - Prospective financial information, including financial budgets or forecasts.
- Contents of letter of engagement
 - neither an audit nor a review will be carried out and that accordingly no assurance will be expressed.
 - engagement cannot be relied upon to disclose fraud or defalcations
 - Nature of the information to be supplied by the client.
 - Intended use and distribution of the information, once compiled.
 - Basis of accounting on which financial information is to be compiled
 - management is responsible to the users for the information to be compiled by the accountant.
- Practitioners may also undertake engagements to assist management in the preparation and presentation of non-financial information, for example, greenhouse gas statements, corporate social responsibility reporting, environmental reporting, sustainability reporting, integrated reporting, statistical returns or other information returns. In those circumstances, the practitioner may apply this SRS, adapted as necessary, as relevant to those types of engagements.

- If the accountant becomes aware that the information is incorrect or unsatisfactory, the accountant should consider performing additional procedures
- The identified financial reporting framework and any known departures, should be disclosed within the financial information
- If the accountant becomes aware of material misstatements, he should persuade the management to carry out necessary amendments. If it is not done and the financial statements are still considered to be misleading, the accountant should withdraw from the engagement.
- The practitioner shall obtain an acknowledgement from management or those charged with governance, as appropriate, that they have taken responsibility for the final version of the compiled financial information.
- The financial statements or other financial information compiled by the accountant should contain a reference such as “Unaudited,” “Compiled without Audit or Review” and also “Refer to Compilation Report” on each page of the financial information or on the front of the complete set of financial statements.

Guidance note on Audit of Internal Financial Controls over Financial Reporting

Sec 143(3)(i) The auditor needs to obtain reasonable assurance to state whether an adequate internal financial controls system was maintained and whether such internal financial controls system operated effectively in the company in all material respects

1) What is IFC-FR?

A process designed, implemented and maintained by management for providing reasonable assurance on reliability of financial reporting and the preparation of financial statements.

It means IFC-FR includes review and testing of such controls which can affect the process of financial reporting E.g. Authority over payments, delegation of financial authority etc.

2) Controls for Which period covered?

When forming its audit opinion on ICFR, the auditor will surely test transactions during the financial year ending 31 March 2016 and not just as at the balance sheet date, though the extent of testing at or near the balance sheet date may be higher.

3) IFC APPLIES TO:

All companies including One person company and Small company

Auditors of foreign component having an Indian Parent company are not required to report upon IFC-FR

Reporting on IFC will not be applicable with respect to interim financial statements, such as quarterly or half-yearly financial statements, unless such reporting is required under any other law or regulation.

4) Regulatory framework

| | |
|--------------------------------|--|
| Sec 134 | In case of listed Company, the DRS shall comment upon adequacy and operating effectiveness of IFC |
| Sec 143 | The auditor needs to obtain reasonable assurance to state whether an adequate internal financial controls system was maintained and whether such internal financial controls system operated effectively in the company in all material respects with respect to financial reporting only. |
| Sec 177 | Audit committee may call for comments of auditors about internal control systems before their submission to the Board and may also discuss any related issues with the internal and statutory auditors and the management of the company. |
| Schedule IV | The independent directors should satisfy themselves on the integrity of financial information and ensure that financial controls and systems of risk management are robust and defensible. |
| Company (accounts) Rules, 2014 | The director's report should contain details in respect of adequacy of internal financial controls with reference to the financial reporting. |

5) Stages for auditing IFC- FR

Step – 1 Planning: Under the planning stage, the auditor is required to establish an overall audit strategy that sets the scope, timing and direction of the audit, and that guides the development of the audit plan. The planning stage involves identification of significant account balances/disclosure items, identification and understanding significant flow of transactions, identification of Risk of Material Misstatements (RoMM), identification of controls which will address RoMM including applications, associated IT environment and general IT controls.

Step – 2 Design and implementation: The auditor should test the design effectiveness of controls by determining whether the company's controls, if they are operated as prescribed by persons possessing the necessary authority and competence to perform the control effectively, satisfy the company's control objectives and can effectively prevent or detect errors or fraud that could result in material misstatements in the financial statements.

Step – 3 Operating effectiveness: Operating effectiveness of a control is tested by determining whether the control is operating as designed and whether the person performing the control possesses the necessary authority and competence to perform the

control effectively. Testing of operating effectiveness involves planning the nature, timing and extent of procedures to be performed, assessing findings and concluding on operating effectiveness.

Step – 4 Reporting: Where there are deficiencies that, individually or in combination, result in one or more material weaknesses, the auditor should evaluate the need to express a modified opinion i.e. qualified or adverse on the company's IFC – FR, unless there is a restriction on the scope of the engagement in which case the auditors should either disclaim the opinion or withdraw from the engagement. The auditor should determine the effect of the modified opinion on IFC – FR has on his opinion on the financial statements. Additionally, the auditor should disclose whether his opinion on the financial statements was affected by the modified opinion on IFC – FR

Guidance note on Fraud Reporting

1 Q: Who are all covered under 143(12) of the Companies Act 2013 to report the Fraud?

A: Reporting obligation to statutory auditor; cost auditor and secretarial auditor

2 Q: Whether auditors appointed under other regulations are covered under 143(12)?

A: No, the fraud reporting is not applicable to internal auditor, tax auditor, VAT auditor, Sales tax Auditor.

3 Q: What are the procedures to be followed, if the Fraud is Rs.1 crore or more?

A: If identified any fraud and the amount involved INR 1 crore or more:

- a) Report within two days to Audit Committee / Board
- b) Wait upto 45 days for reply from Board / Audit Committee
- c) Within 15 days of receipt of above replies – forward to Central Government – Details to be included specified in Form ADT – 4
- d) If no reply from Directors – forward to Central Government, the note send to Board / Audit Committee.
- e) The report / note to be submitted by Registered Post with Acknowledgement due / Speed post

4 Q: What are the procedures to be followed, if the Fraud below Rs.1 crore?

A: If identified any fraud and the amount involved is less than INR 1 crore:

- a) Report within two days to Audit Committee / Board
- b) Adequate disclosures in Board report including remedial action taken

5 Is there a difference between definitions of fraud under standards on auditing and companies Act?

A: Yes, there are differences in definition of Fraud as per Standards on Auditing (SA 240) and Companies Act (s.447)

Under Section 447, fraud includes 'acts with an intent to injure the interests of the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss.

However, an auditor may not be able to detect acts that have intent to injure the interests of the company or cause wrongful gain or wrongful loss, unless the financial effects of such acts are reflected in the books of account.

For example: an auditor may not be able to detect if an employee is receiving pay-offs for favoring a specific vendor, which is a fraudulent act, since such pay-offs would not be recorded in the books of account.

SA 240: An intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage.

Therefore, the auditor shall consider the requirements of the SAs, insofar as it relates to the risk of fraud, including the definition of fraud as stated in SA 240.

6 Q: Whether fraud identified during other engagements including Limited Review / tax audit to be reported?

A: If an offence of fraud in the company, that is identified by the auditor in the course of providing attest or non-attest services, which the auditor uses or intends to use the information, when performing the statutory audit, then the matter may become reportable.

7 Q: An already identified fraud either by Management / other auditors, whether to be reported by the Auditor?

A: Auditors need to report on fraud, only if he is the first person to identify/note such instance in the course of performance of his duties as an auditor.

Accordingly, in case a fraud has already been reported or has been identified by the management or through the company's vigil/whistle blower mechanism and has been being remediated with by them and such case is informed to the auditor, he will not be required to report the same.

8 Q: Whether frauds taken place in any of subsidiaries, joint-ventures and associates to be reported by the parent company auditor?

A: Reporting under Section 143(12) arises only if a suspected offence of fraud is being or has been committed in the company by its officers or employees. Accordingly, the auditor of the parent company is not required to report on frauds, if they are not being or have not been committed in the parent company by the officers or employees of the parent company.

However, if the suspected offence of fraud in the component is being or has been committed by employees or officers of the parent company and if such suspected offence

involving fraud in the component is against the parent company, then the parent auditor to report.

9 Q: What is the trigger to report the fraud – suspicion / reason to believe / knowledge?

A: Based on a harmonious reading of Section 143(12), Rule 13 of the Companies (Audit and Auditors) Amendment Rules, 2015 and Form ADT - 4, reporting on fraud in the course of performance of duties as auditor, is applicable only when the auditor has reason to believe and has knowledge that a fraud has occurred or is occurring i.e., when the auditor has evidence that a fraud exists.

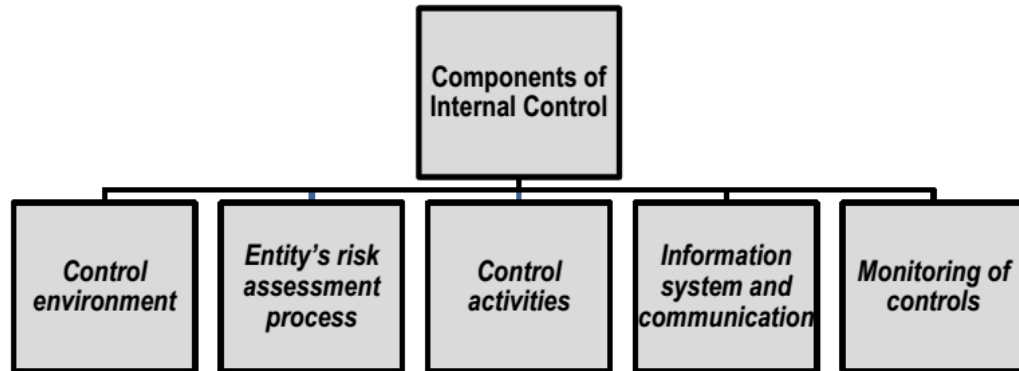
10 Q: Whether concept of materiality applicable to fraud reporting?

A: The auditor should apply the concept of materiality in performing the audit. On reporting, materiality is applicable wherever the amount is quantifiable. Where the amount is not quantifiable, the auditor should apply professional judgment to estimate the likelihood of the amount.

The answers of the questions are primarily based on Guidance note issued by ICAI. Also refer the ICAI Guidance note on detailed guidance on each of the above.

Internal Controls- important points added

1) Components of Internal Control



a) Control Environment (WORK CULTURE):

Communication and enforcement of integrity and ethical values

Commitment to competence(Knowledge)

Participation by those charged with governance

b) Risk Assessment Process (as per SA 315 notes)

c) Control Activities:

-Performance Reviews- performing analytical procedure (ratios and comparisons)

-Information processing- verifying Information technology controls. They are mainly- application based controls and 2) verifying general policies established by management.

-Physical Controls e.g. security of assets

-Segregation of duties (internal check through work distribution)

d) Information Systems and communication- We need to verify systems for financial reporting to check whether systems correctly record on timely basis- A-amount, C-Classification, P-Presentation, D-disclosures

e) Monitoring of controls- Supervision and reviews. Establishing timelines and MIS reports for compliance with the procedure

2) Inherent Limitations of Internal Control

Human Error & System break down

Judgement

Cost

Collusion

Management override/bias

Misuse of authority

3) Risks can arise or change due to circumstances such as the following:

- (a) Changes in operating environment
- (b) New personnel.
- (c) New or revamped information systems
- (d) Rapid growth.
- (e) New technology.
- (f) New business models, products, or activities.
- (g) Corporate restructurings.
- (h) Expanded foreign operations.
- (i) New accounting pronouncements.

Company Audit

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| Rotation of auditor- Difference in Requirements SQC 1 vs Companies Act, 2013 | As per SQC-1- rotation should be done after 7 years SQC- 1 became applicable from April 1, 2009 (FY 09-10) So rotation should be done after FY 15-16. As per the Co Act, 2013, transitional period of 3 years is given which ends on FY 16-17. Hence, no rotation required as per SQC-1 because Law will supersede Standard i.e. Rotation will be done from FY 17-18. |
| Auditor's Representation in reply to notice u/s 140(4) | If the Tribunal is satisfied on an application either of the company or of any other aggrieved person that the rights conferred by section 140(4) of the Companies Act, 2013 are being abused by the auditor, then, the copy of the representation may not be sent and the representation need not be read out at the meeting. (FURTHER CA CAN BE HELD GUILTY UNDER CLAUSE 6 PART I First Schedule of CA ACT, 1949) |
| Sec 130 | Company Shall not re-open accounts unless an application in this regard is made by CG, Tax Authorities, SEBI or any other regulatory body or by a court order. |
| Sec 131 | Voluntary Revision of FS or Board's report. BOD shall make an application to the Tribunal IF tribunal order is received then revision can be done for any of the three preceding FY |
| Sec 140 (5) | Removal of auditor by the tribunal if application has been made by CG or any concerned person (stake holder) Auditor cannot be reappointed for another 5 years and he shall be liable for action u/s 447. |

Revised Schedule III from FY 16-17

Background

The Schedule III to the Companies Act, 2013 (2013 Act) provides general instructions for preparation of the balance sheet and the statement of profit and loss of a company.

The Ministry of Corporate Affairs (MCA) issued a road map for implementation of the Indian Accounting Standards (Ind AS) converged with the International Financial Reporting Standards (IFRS):

- On 16 February 2015 by companies other than insurance companies, banking companies and Non-Banking Financial Companies (NBFCs) (corporate road map) in a phased manner commencing from accounting periods beginning on or after 1 April 2016
- On 30 March 2016 by banking companies, insurance companies and NBFCs in a phased manner commencing from accounting periods beginning on or after 1 April 2018.

New development

The MCA on 6 April 2016, amended Schedule III to include general instructions for preparation of financial statements of a company whose financial statements are required to comply with Ind AS. The amendment divides Schedule III into two parts i.e. Division I and II

Division I is applicable to a company whose financial statements are required to comply with the current accounting standards

Division II is applicable to a company whose financial statements are drawn up in compliance with Ind AS.

Overview of the revised Schedule III – Division II

Division II of the Schedule III provides instructions for preparation of financial statements and additional disclosure requirements for companies required to comply with Ind AS.

Applicability

It is applicable to every company to which Ind AS apply in preparation of its financial statements.

The provisions of Schedule III also apply when a company is required to prepare consolidated financial statements, in addition to the disclosure requirements specified under Ind AS.

Part I contains the form in which the Balance Sheet of a company required to comply with Ind AS and states the general instructions as regard to preparation of Balance Sheet.

Part II contains the form and states the general instructions as regard to preparation of Statement of Profit and Loss.

PART III contain general instructions for preparation of Consolidated Financial Statements.

CARO 2016: ALREADY COVERED IN CLASSROOM DISCUSSION

MANNER OF SIGNING THE CERTIFICATES (as per COUNCIL of the INSTITUTE):

- Name of the CA firm
- Firm Registration Number (FRN)
- Name of the member
- Designation (Partner/Proprietor)
- Membership Number

ANY OTHER DETAIL AS REQUIRED BY APPLICABLE LAW.

GUIDANCE NOTE ON Reporting u/s 143(3) (f) and (h) of Companies Act, 2013.

Sec 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 word “observations” or “comments” have the same meaning as the matters leading to emphasis of matter paragraph (matters not affecting auditor’s opinion). There is no change in objective or scope of audit.

Reporting depends upon auditor’s professional Judgment

Examples of emphasis of matter which may have an adverse effect on the functioning of the company include situations where:

- ◆ The going concern assumption is appropriate but there are several factors leading to a material uncertainty that may cast a significant doubt about the Company’s ability to continue as a going concern; or
- ◆ a material uncertainty regarding the outcome of a litigation wherein an unfavourable decision could result in a significant outflow of resources for the company, etc.

Examples of emphasis of matter which may not have an adverse effect on the functioning of the company include a situation where there is an emphasis of matter:

- ◆ on managerial remuneration which is subject to the approval of the Central Government;
- ◆ relating to accrual of a contractually receivable claim based on management estimate where the ultimate realisation could be different from the amount accrued;
- ◆ on frauds that have been dealt with in the financial statements of the company and would not have any continuing effect on the financial statements

Sec 143 (3) (h) : “any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith”

According to Guidance Note, the words “qualification”, “adverse remark” and “reservation” used in clause (h) of section 143(3) should be considered to be similar to the terms “qualified opinion”, “adverse opinion” and “disclaimer of opinion”.

Accounts will not include cost accounts because auditor is duty bound to report opinion only upon financial statements

SEBI LODR- (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS), 2015 with amendments passed in 2016

Overview

Total Chapters- XII

LODR is divided into two parts

A) Regulations

B) Schedules

RTP contains Regulations from Chapter IV especially in relation with corporate governance and code of conduct supported with Schedule II and V.

Applicable to all Listed Companies.

| Reg No. | Deals With | Summary |
|---|---|---|
| 18 (1) | Qualified and Independent Audit Committee | - min 3 directors as members - 2/3 of members- independent - financial literate members - chairperson- indep director - CS- secretary to the committee |
| 18 (2) | Meeting & Powers of Audit Committee | - atleast 4 times in a year with max gap of 120 days between two meetings - powers- Same as Company Law |
| Schedule II | Role of Audit Committee | - oversight functions - co-ordinate with auditors - increase transparency |
| 17 | Composition of Board | -Atleast one woman director - minimum 50%- non-executive directors -1/3 rd independent directors - chairperson- non executive director - if chairperson is promoter or relative of promoter then ½ of BOD should be independent directors |
| Schedule V | Remuneration of Directors | -Disclosure requirements in corporate governance report (disclose complete package, stock option details) |
| 17 (6) | Approval of Remuneration | - fixed by BOD - previous approval of shareholders except for sitting fees to non-executive directors - independent director cannot be given stock option |
| 17 (2, 4) 25 (5, 6) 26 (1, 2, 4, 5) | Obligations of Director and Senior Management | - Atleast 4 times in a year with max gap of 120 days between 2 meetings - director can be member in max 10 committees and chairperson in max 5 committees - review compliance report of applicable laws - independent director if removed, needs to be replace by another independent director max by the next board |

| | | |
|---------------------------------------|---|---|
| | | meeting |
| 17 (5), 26 (3), 46 (2) Sch V | Provisions Regarding Code of Conduct (COC) | - BOD shall lay down a code of conduct - COC should incorporate duties of independent director - COC should be posted on website - declaration of compliance with COC to be included in annual report and certified by CEO |
| 22 & 46 Sch V | Vigil Mechanism | - mechanism for directors and employees to report genuine concerns - adequate safeguards against victimization - details to be posted on website of the company and in board's report |
| 16 (c), 24 & 46 Sch V | Subsidiary of Listed Entity | - one Indep Director of parent co shall be on the board of subsidiary - Audit committee of parent co shall review FS of subsidiary - policy for determining material subsidiary - material subsidiary → 20% of total networth/total income |
| 32 and Sch II | Statement of deviation | - deviation in utilisation of funds - whether funds were applied for the specified purposes (CONSIDER CLAUSE (IX) OF CARO , 2016) - statement to be submitted annually to SEBI |
| Sch V | Management Discussion and Analysis | - form part of annual report - include discussion on – SWOT analysis, Industry developments, Segement wise performance, risks, internal controls etc) |
| 36 | Information to Shareholders | -appointment or reappointment of director- company shall submit- following info to shareholders ----- brief resume, expertise, relationship with other directors, details of other directorships |
| 20 and Sch II | Stakeholders Relationship Committee | -Grievance redressal mechanism for investors - chairperson- non executive director -BOD shall decide other members of this committee |
| 40 | Transfer/ Transposition/ Transmission of Sec | - BOD shall delegate the power of transfer to committee/compliance officer/registrar to the issue - BOD shall review the transfer atleast once in a fortnight - auditor should verify from the minute books regarding delegation of the power |
| Sch II | Compliance Certificate | Certification from CEO and CFO that they have reviewed FS and Cash flow statement, maintaining internal control, |
| 4 | Disclosure and Transparency | Timely disclosure of material matters including financial situation, performance and ownership |
| 27, 46 and Sch V | Related Party Disclosures | - quarterly compliance report - details of all related party transactions should be given - signed by CEO/compliance officer |
| Sch V | Disclosure of Accounting Treatment | - IF treatment other than AS has been given, then disclosure required along with management's explanation |

| | | |
|-----------------------|---------------------------------------|---|
| 21 | Risk Management Committee | <ul style="list-style-type: none"> - majority of members shall be from BOD - chairperson shall be a member of BOD - applicable to top 100 listed entities based on market CAP |
| 19 and Sch II | Nomination and Remuneration Committee | <ul style="list-style-type: none"> - at least three directors- non-executive directors -at least half shall be independent. -Chairperson - independent director. - recommend to the Board of Directors a policy, relating to the remuneration of the directors, key managerial personnel and other employees - Identifying persons who are qualified to become directors and who may be appointed in senior management |
| 27 and Sch II | Report on Corporate Governance | <ul style="list-style-type: none"> -The listed entity shall submit a quarterly compliance report on corporate governance in the format as specified by the SEBI within 15 days from the close of quarter. -signed either by the Compliance Officer or the Chief Executive Officer of the listed entity. |
| Auditor's Certificate | | As per Schedule V, a listed entity shall obtain a compliance certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance and shall annex it to the Directors' Report. |

Chapter 10- Audit of Consolidated Financial Statements

1) Auditing the Consolidation

Before commencing an audit of consolidated financial statements, the auditor should plan his work to enable him to conduct an effective audit in an efficient and timely manner. The auditor should make plans, among other things, for the following:

- (a) Understanding of the group structure and group-wide controls including assessment of Information Technology (IT) system and related general and applications IT related controls (manual and automated) for consolidation process;
- (b) understanding of accounting policies of the parent and its components as well as of the consolidation process including the process of translation of financial statements of foreign components;
- (c) determining and programming the nature, timing, and extent of the audit procedures to be performed based on the assessment of the risk of material misstatement in the consolidation process;
- (d) determining the extent of use of other auditor's work in the audit (SA 600); and
- (e) coordinating the work to be performed.

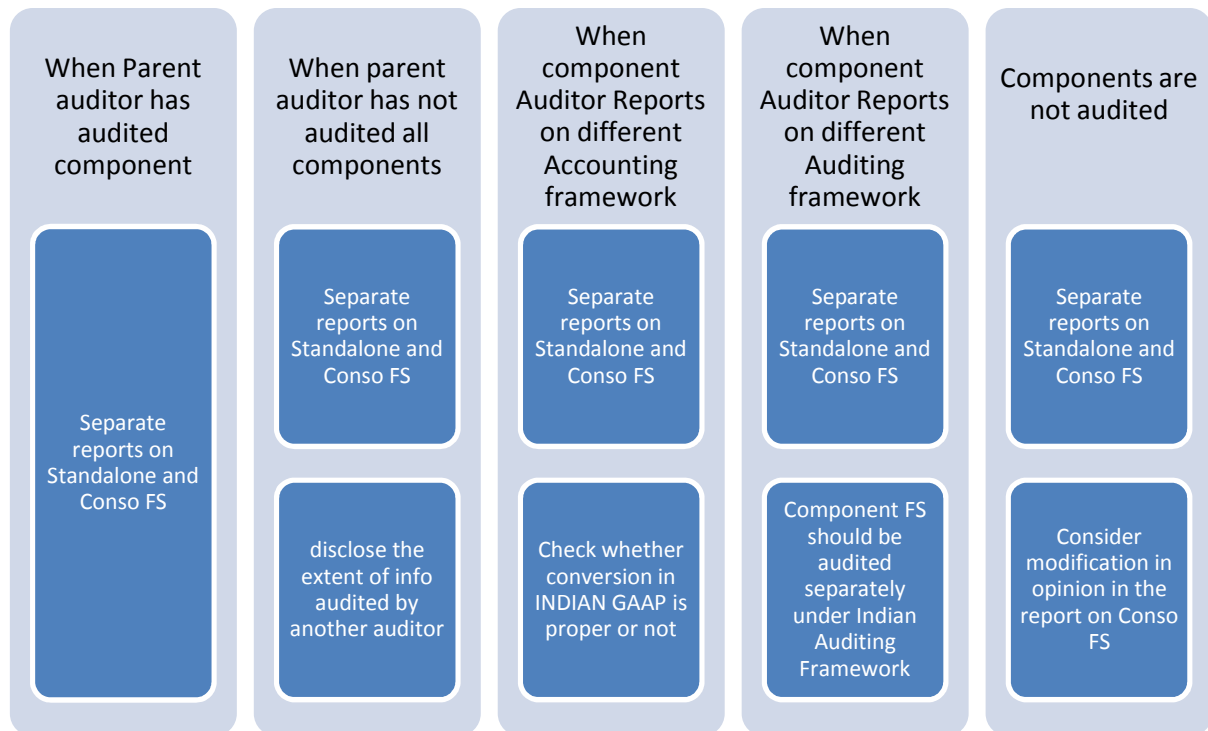
2) Permanent Consolidation Adjustments:

Determining the Goodwill/Capital Reserve

Determination of amount of equity attributable to minority/non-controlling interests

3) Current Period Consolidation Adjustments:

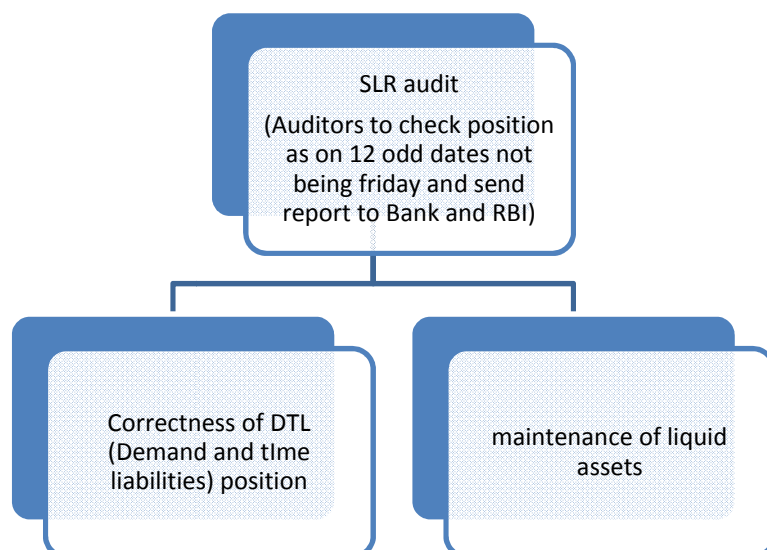
Current period adjustments are those adjustments that are made in the accounting period for which the consolidation of financial statements is done. Current period consolidation adjustments primarily relate to elimination of intra-group transactions and account balances



Expect Questions from Sec 129 and Accounting Standards for Consolidation

Chapter 10- Audit of Banks

CRR is a cash reserve ratio ,Under **CRR** a certain percentage of the total bank deposits has to be kept in the current account with RBI which means banks do not have access to that much amount for any economic activity or commercial activity. Statutory liquidity ratio (**SLR**) is the Indian government term for reserve requirement that the commercial banks in India require to maintain in the form of gold, government approved securities before providing credit to the customers.



Chapter 14 AUDIT OF NBFC

CARO 2016 Reporting

1) As per Clause (xvi) of Paragraph 3 of CARO, 2016, the auditor is required to report that “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.”

Discussion:

(a) The auditor is required to examine whether the company is engaged in the business which attract the requirements of the registration. The registration is required where the financing activity is a principal business of the company.

(b) The Reserve Bank of India restrict companies from carrying on the business of a nonbanking financial institution without obtaining the certificate of registration.

(c) NBFCs are doing functions similar to banks, however there exist difference between banks & NBFCs. NBFCs lend and make investments and hence their activities are akin to that of banks; however there are a few differences as given below:

(i) NBFC cannot accept demand deposits; (ii) NBFCs do not form part of the payment and settlement system and cannot issue cheques drawn on itself.

2) As per Clause (xii) of Paragraph 3 of CARO, 2016, the auditor is required to report that 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.

Discussion:

Every Nidhi shall, within a period of one year from the commencement of these rules, ensure that it has—

- (i) not less than two hundred members;
- (ii) net owned funds of ten lakh rupees or more;
- (iii) unencumbered term deposits of not less than ten per cent of the outstanding deposits;
- (iv) ratio of net owned funds to deposits of not more than 1:20.

Auditor Shall report shortfalls, if any as per CARO 2016 clause (xii)

Chapter 15- Audit Under FISCAL LAWS

ICDS- Income Computation and disclosure standards as per INCOME TAX ACT, 1961
(INCOME TAX LAW- ITL)

Overview

ICDS shall apply effective from current tax year 2015-16 itself (i.e. Assessment Year 2016-17 and onwards).

Section 145 of the ITL provides that the taxable income of a taxpayer falling under the heads “profits and gains of business or profession” (Business) or “income from other sources” (Other Sources), shall be computed in accordance with either cash or mercantile system of accounting which is regularly employed by the taxpayer. It further provides that the CG may notify, from time to time, ICDS to be followed by assesses following mercantile system of accounting.

In FORM 3CD- Clause 13 (d) Whether any adjustment is required to be made to the profits or loss for complying with the provisions of income computation and disclosure standards notified under section 145(2)

Summary

ICDS I relating to accounting policies (corresponding to ICAI AS-1)

- ▶ Expected losses or mark-to-market losses shall not be recognized unless permitted by any other ICDS.
- ▶ Concept of materiality for selection of accounting policies is omitted based on Committee’s recommendation that the concept is not recognized by the ITL for the purpose of computation of taxable income.
 - ▶ Accounting policies shall not be changed without a reasonable cause[7] .

ICDS II relating to valuation of inventories (corresponding to ICAI AS-2)

- ▶ ICDS requires valuation of inventory of services at cost or net realizable value, whichever is lower. Cost of services shall consist of labour and other costs of personnel directly engaged in providing the service including supervisory personnel and attributable overheads.
 - ▶ Use of standard cost method, as a technique for measurement of cost, is not permitted based on Committee’s recommendation to reduce accounting alternative.
 - ▶ To reduce litigation, ICDS specifically incorporates the well-established principle that the value of inventory of a business as on the beginning of a tax year shall be the same as the value of inventory at the end of the immediately preceding tax year. Similarly, cost of inventory, if any, on the day of commencement of business will be opening inventory where business has commenced during the relevant tax year.
 - ▶ Method of valuation of inventory once adopted by a taxpayer in any tax year shall not be changed without a reasonable cause[8] .
 - ▶ Inventory on the date of dissolution of a partnership firm, association of persons and body of individuals shall be valued at net realizable value regardless of whether business is discontinued or not.

ICDS III relating to construction contracts (corresponding to ICAI AS-7)

- ▶ Retention money shall be recognized for computing revenue based on percentage of completion method.
- ▶ Pre-construction income in the nature of interest, dividend and capital gains shall not be reduced from the cost of construction. As per Committee, they shall be taxed as income in accordance with the applicable provisions of the ITL.
- ▶ ICAI AS requires that contract costs relating to future activity shall be recognized as an asset when it is probable that such costs are recoverable. ICDS provides for recognizing such costs as an asset. As per Committee, if such costs are not realizable then the same may be allowed under the provisions of ITL.
- ▶ Condition of non-recognition of contract revenues, if it is not possible to reliably measure the outcome of a contract, is not incorporated in ICDS based on Committee's recommendation that it is subjective in nature and has resulted in litigation and postponement of tax liability.
- ▶ Losses incurred on a contract shall be allowed only in proportion to the stage of completion. As per Committee, future or anticipated losses shall not be allowed, unless such losses are actually incurred.
- ▶ Once a contract crosses 25% of the completion stage, the revenue in respect of such contract shall be required to be recognized.

ICDS IV relating to revenue recognition (corresponding to ICAI AS-9)

- ▶ Revenue from service transactions shall be recognized by following "percentage completion method" alone[9] .

ICDS V relating to tangible fixed assets (corresponding to ICAI AS-10)

- ▶ In case of acquisition of an asset in exchange for another asset, shares or other securities, fair value of tangible fixed asset acquired shall be recorded as actual cost of the asset[10] .
- ▶ Income arising on transfer of a tangible fixed asset shall be computed in accordance with the provisions of the ITL.
- ▶ Also provisions relating to revaluation of assets are not incorporated in ICDS since, as per Committee, the ITL does not recognize the concept of revaluation of assets.

ICDS VI relating to the effects of changes in foreign exchange rates (corresponding to ICAI AS-11)

- ▶ Initial and subsequent recognition of foreign currency transactions and resultant exchange differences will be subject to specific provisions of the ITL and Income Tax Rules, 1962.
- ▶ Since mark-to-market gains or losses are unrealized in nature as per Committee, all gains or losses on forward exchange or similar contracts entered into for trading or speculation contracts shall be recognized only on settlement.
- ▶ Since the ITL does not distinguish between integral and non-integral foreign operations as per Committee, exchange differences on non-integral foreign operations shall also be recognized for the purpose of computation of income[11] .

ICDS VII relating to government grants (corresponding to ICAI AS-12)

- ▶ Government grants should either be treated as revenue receipt or should be reduced from the cost of fixed assets based on the purpose for which such grant or subsidy is given.
- ▶ Recognition of Government grants shall not be postponed beyond the date of actual receipt.

ICDS VIII relating to securities (Broadly corresponding to ICAI AS-13)

- ▶ Since ICDS deals with computation of income under Business or Other Sources heads, ICDS only deals with securities held as stock-in-trade.
- ▶ Securities should be valued at lower of cost or net realizable value (NRV). Comparison of cost and NRV shall be done category-wise (and not for each individual security), for which securities shall be classified into the following categories: (a.) Shares (b.) Debt securities (c.) Convertible securities (d.) Any other securities not covered above.
- ▶ Unlisted or thinly traded securities shall be valued at cost.
- ▶ Cost which cannot be ascertained by specific identification shall be determined on the basis of first-in-first-out (FIFO) method.
- ▶ In case of acquisition of securities in exchange for issue of shares or other securities, fair value of shares or securities acquired shall be recorded as actual cost of the securities[12] .
- ▶ In case of acquisition of securities in exchange for another asset, fair value of securities acquired shall be recorded as actual cost of the securities[13] .

ICDS IX relating to borrowing costs (corresponding to ICAI AS-16)

- ▶ Borrowing cost will not include exchange differences arising from foreign currency borrowings[14] .
- ▶ As against the criterion of substantial period of time for classifying any asset (whether fixed asset or inventory) as qualifying asset under ICAI AS-16, ICDS retains substantial period condition (i.e. 12 months) only for qualifying assets in the nature of inventory. Thus, ICDS requires capitalisation of borrowing costs for other tangible and intangible assets even if they do not require substantial period for completion.
- ▶ Capitalisation of specific borrowing cost shall commence from date of borrowing[15] .
- ▶ A normative pro-rata formula is provided for capitalizing borrowing costs relating to general borrowings. ICDS also provides specific rules for capitalisation in respect of : (a.) Assets acquired and put to use during same tax year and (b.) Assets awaiting capitalization brought forward from earlier year and put to use during the relevant tax year.
- ▶ Unlike ICAI AS, income on temporary investments of borrowed funds cannot be reduced from borrowing costs eligible for capitalization in ICDS.
- ▶ Unlike ICAI AS, condition of suspension of capitalization during interruption of active development is removed in ICDS.

ICDS X relating to provisions, contingent liabilities and contingent assets (corresponding to ICAI AS-29)

- ▶ A provision can be recognized when it is "reasonably certain" that an outflow of economic resources will be required to settle an obligation [16] .
- ▶ A contingent asset can be recognized when the realization of related income is "reasonably certain"[17] .

Working notes

[7] ICAI AS permits change if it is required by statute or for compliance of ICAI AS or if the change would result in a more appropriate presentation. [8] ICAI AS permits change if it is required by statute or for compliance of ICAI AS or if the change would result in a more appropriate presentation. [9] ICAI AS permits adoption of either 'completed service contract method' or 'percentage completion method'.

[10] ICAI AS provides that where fixed asset is acquired in exchange for another asset, shares or other securities issued, cost of asset acquired should be recorded either at fair market value of asset given up/shares or securities issued or fair market value of asset acquired, whichever is more clearly evident. [11] As against accumulation in foreign currency translation reserve in Balance Sheet as prescribed under ICAI AS. [12] ICAI AS requires recognition of cost of securities acquired in exchange for issue of shares or other securities at fair value of securities issued. [13] ICAI AS requires recognition of cost of securities acquired in exchange for another asset at fair value of securities issued or fair value of asset given up, whichever value is more clearly evident.

[14] ICAI AS includes such differences to the extent that they are regarded as an adjustment to interest costs. [15] ICAI AS requires cumulative fulfillment of three conditions viz. incurrence of capital expenditure, incurrence of borrowing costs and preparatory activities being in progress. [16] As against condition of "probable" under ICAI AS. [17] As against condition of "virtual certainty" under ICAI AS

Chapter 16 COST AUDIT

As Explained in the classroom discussion (refer company audit notes)

List of Regulated Sectors

- Telecommunication Services
- Generation, transmission distribution and supply of Electricity
- Petroleum products
- Drugs and pharmaceuticals
- Fertilizers
- Sugar and industrial alcohol

List of Non Regulated Sectors

- Machinery used for defence space atomic research
- Turbo jets and Turbo propellers
- Arms and ammunition
- Aeronautical Services
- Steel and Cement
- Rubber and allied products
- Roads and other infrastructure project
- Ores and mineral products
- Edible oil
- Jute and Jute products

Chapter 22 Professional Ethics

| Reference | Amendments in | Content |
|------------------------------------|--|--|
| Clause 6 Part I First Schedule | Responding to Tenders | As per the guideline issued by the Council of the Institute of Chartered Accountants of India, a member of the Institute in practice shall not respond to any tender issued by an organization or user of professional services in areas of services which are exclusively reserved for chartered accountants, such as audit and attestation services. However, such restriction shall not be applicable where minimum fee of the assignment is prescribed in the tender document itself or where the areas are open to other professionals along with the Chartered Accountants. |
| Clause 6 Part I First Schedule | Website | Client names can be displayed if required by Law The Website may provide a link to the Website of ICAI, its Regional Councils and Branches and also the Website of Govt./Govt. Departments/Regulatory authorities/other Professional Bodies, such as, American Institute of Certified Public Accountants (AICPA), the Institute of Chartered Accountants of England & Wales (ICAEW) and The Canadian Institute of Chartered Accountants (CICA). |
| Clause 10 Part I First Schedule | Charging on Fees on % or Performance | Exceptions- Liquidator Auditor of Co-op Society Valuer Fund Raising Services (IPO/FPO) Debt recovery Cost optimisation Any other service as decided by the council |
| Clause 11 Part I First Schedule | General resolution of the Council | Members of the Institute in practice be generally permitted to act as recovery consultant in the banking sector, for which no specific permission from the Council would be necessary. |

Annexure

Important phrases in Auditing paper

| | | | |
|----------------------------------|--|--|--|
| Materiality | Auditor's Professional Judgment and Experience | Preparation and Presentation of FS | Responsibility of management |
| Audit Risk | Risk of Material Misstatement | Independence | Integrity and objectivity |
| Misstatement | Reasonable justification | Limitation on scope | Objective of auditor |
| Audit Engagement | Engagement Team | Audit Documentation (Records) | Risk Assessment Procedures |
| Compliance Procedures | Substantive Procedures | Management and Where Appropriate TCWG | Sufficient Appropriate Audit Evidence |
| Planning and Performing Audit | Management Representation | Reliability and Integrity of management | Questioning Mind |
| Maintain Alertness | Planned Audit Procedures | Alternate Audit Procedures | Additional Audit Procedures |
| Consider impact on audit opinion | Persuasive Audit Evidence | Applicable Financial Reporting Framework | Nature Timing and Extent of Audit Procedures |
| Inconsistency | Internal Control System | Fraud Risk Factors | Terms of Engagement |