

7. “Reporting”

PART- I DESCRIPTIVE QUESTIONS

7.1 - SA 700 “Forming an Opinion and Reporting on Financial Statements”

Q.1. KPI Ltd. is a company on which International Standards on Auditing are applicable along with Standard on Auditing issued by the ICAI. The company appointed new auditors for the audit of the financial statements for the year ended on 31st March 2024 after doing all appointment formalities. In the auditor’s report, auditor referred the International Standard on Auditing in addition to the Standard on Auditing issued by the ICAI.

As an expert, you are required to advise the auditor regarding auditor’s report for audits conducted in accordance with both the Standards. [RTP-Nov. 19]

Ans: Auditor’s Report for Audits Conducted in Accordance with Both Standards on Auditing Issued by ICAI and International Standards on Auditing:

As per SA 700, “Forming an Opinion and Reporting on Financial Statements”, an auditor may be required to conduct an audit in accordance with the International Standards on Auditing, in addition to the SAs issued by ICAI. If this is the case, the auditor’s report may refer to SAs in addition to the International Standards on Auditing, but the auditor shall do so only if:

- (a) There is no conflict between the requirements in the International Auditing Standards and those in SAs that would lead the auditor:
 - to form a different opinion, or
 - not to include an Emphasis of Matter paragraph or Other Matter paragraph that, in the particular circumstances, is required by SAs; and
- (b) The auditor’s report includes, at a minimum, each of the elements set out in Auditor’s Report Prescribed by Law or Regulation discussed above when the auditor uses the layout or wording specified by the Standards on Auditing.

When the auditor’s report refers to both the ISAs and the Standards on Auditing issued by ICAI, the auditor’s report shall clearly identify the same including the jurisdiction of origin of the other auditing standards.

Q.2. CA Sameer is statutory auditor of Tram Fram Ltd. for FY 2023-24. While concluding audit, CA Sameer decided to issue an unmodified opinion, though he also concluded that a material uncertainty exists with respect to company’s ability to continue as a going concern on account of a pending litigation related to labour laws. He is of the view that the company has made appropriate disclosures with respect to such pending litigation in the notes to accounts annexed to the financial statements of Tram Fram Ltd. for the FY 2023-24. Explain how CA Sameer will deal with the above situation in his auditor’s report (draft the relevant portion of the auditor’s report.)

Ans: **Material Uncertainty Related to Going Concern:**

In given situation, auditor is required to include in audit report an additional para titled as “Material Uncertainty Related to Going Concern” so as to state the fact related to going concern in that para.

Material Uncertainty Related to Going Concern

We draw attention to Note 10 in the financial statements, which indicates that the outcome of

a litigation on account of labour laws is pending in case of the company during the year 31st March, 2024. As stated in Note 11, this event or condition, indicate that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Q.3. CA S has been appointed as Statutory Auditor of SRT Ltd. for the financial year 2023-24. The Company while preparing financial statements for the year under audit prepared one additional profit and loss account that disclosed specific items of expenditure and included the same as an appendix to the financial statements. CA S has not been able to understand this as the additional profit and loss account is not covered under applicable financial reporting framework. Guide him as to how he should deal with this issue while reporting on the financial statements of SRT Ltd. [July 21 (5 Marks); RTP-May 23]

Ans: Supplementary Information Presented with the Financial Statements:

SA 700 "Forming an Opinion and Reporting on Financial Statements" deals with the supplementary information presented with the financial statements. Accordingly,

- If supplementary information that is not required by applicable FRF is presented with the audited F.S., the auditor shall evaluate whether, in the auditor's professional judgment, supplementary information is nevertheless an integral part of the F.S. due to its nature or how it is presented.
- When it is an integral part of the F.S., the supplementary information shall be covered by the auditor's opinion.
- If supplementary information that is not required by the applicable FRF is not considered an integral part of audited F.S., the auditor shall evaluate whether such supplementary information is presented in a way that sufficiently and clearly differentiates it from the audited F.S. If not, then the auditor shall ask management to change the presentation of supplementary information. If management refuses to do so, the auditor shall identify the unaudited supplementary information and explain in the auditor's report that such supplementary information has not been audited.
- When an additional profit and loss account that discloses specific items of expenditure is disclosed as a separate schedule, included as an appendix to the financial statements, the auditor may consider this to be supplementary information that can be clearly differentiated from the financial statements.
- Thus, additional profit and loss account is not considered an integral part of the audited financial statements and the auditor shall evaluate that supplementary information is presented in a way that sufficiently and clearly differentiates it from the audited financial statements.

Q.4. The auditors of a listed company have affirmed in their audit report communication of significant audit findings including significant deficiencies in internal control of the company identified to those charged with governance. Where are such matters included in audit report of a listed company? Also dwell upon importance of such communication.

Ans: Auditor's Responsibilities:

- Matters as stated in the question are in nature of auditor's responsibilities and are stated in "The Auditor's Responsibilities for the Audit of the Financial Statements" section of the auditor's report in accordance with SA 700.

- Communication of significant audit findings and deficiencies identified in internal control to TCWG is one of important responsibilities of auditor. Such communication assists TCWG in fulfilling their responsibility to oversee financial reporting process and in fulfilling their oversight responsibilities.

Q.5. MN & Associates, Chartered Accountants have been appointed as statutory Auditors of Cotton Ltd. for the FY 2023-24. The Company is into the business of yarn manufacturing. For this purpose, cotton ginning is also done within the factory premises. Raw cotton is purchased from local market and processed in-house. The Company received a notice from the State Government to deposit market development fee for the last 5 years to the tune of ₹ 10.00 Crores. The Company and all other organisations in the same business has not deposited the market development fee, taking shelter of an old circular issued by the Government. The trade association met with the government officials to resolve the matter and agreed to deposit the same prospectively. However, the matter relating to payment of development fee for the last 5 years is pending before the Government as at the end of the financial year. The Company, however, disclosed the same in notes to accounts, as contingent liability, without quantifying the effect and proper explanation. If the liability is provided in the books of account, entire reserves will be wiped off. Auditor seeks your guidance as to how this disclosure affects them while forming an opinion on financial statements. [July 21 (5 Marks)]

Ans: Forming an opinion and reporting on financial statements:

- As per Ind AS 37, “Provisions, Contingent Liabilities and Contingent Assets”, an entity should disclose for each class of contingent liability at the end of the reporting period a brief description of the nature of the contingent liability and, where practicable:
 - (a) an estimate of its financial effect, measured in the standard;
 - (b) an indication of the uncertainties relating to the amount or timing of any outflow; &
 - (c) the possibility of any reimbursement.
- A 700 “Forming an opinion and reporting on financial statements”, requires the auditor to evaluate whether in view of the requirements of the applicable FRF
 - (i) The F.S. adequately disclose the significant accounting policies selected and applied;
 - (ii) The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;
 - (iii) The accounting estimates made by the management are reasonable;
 - (iv) The information presented in the financial statements is relevant, reliable, comparable and understandable;
 - (v) The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements.
- If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor shall discuss the matter with management and, depending on the requirements of the applicable FRF and how the matter is resolved, shall determine whether it is necessary to modify the opinion in the auditor’s report in accordance with SA 705.
- In the present case, the matter relating to payment of development fee for the last 5 years is pending before the Government as at the end of the financial year. The Company, however, disclosed the same in notes to accounts, as contingent liability, without

quantifying the effect and proper explanation. If the liability is provided in the books of account, entire reserves will be wiped off.

Conclusion: Considering the requirements of Ind-AS 37 as stated above, auditor must ensure that disclosure as per Ind-AS 37 to be given in financial statements. If appropriate disclosures not given in the financial statements, auditor need to modify the report as per the requirements of SA 705.

1.2 - SA 701 “ Communicating Key Audit Matters in the Independent Auditor’s Report”

Q.6. “The auditor shall determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the key factors”. You are required to define key audit matters and briefly discuss the factors determining the key audit matters. [MTP-April 18]

Ans: Considerations to determine Key Audit Matters:

As per SA 701 “Communicating Key Audit matters in the Independent Auditor’s Report” Key Audit Matters are those matters that, in the auditor’s professional judgment, were of most significance in the audit of the F.S. of the current period. Key audit matters are selected from matters communicated with TCWG.

Auditor shall determine, from the matters communicated with TCWG, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall consider the following:

- (a) Areas of higher assessed RMM, or significant risks identified in accordance with SA 315;
- (b) Significant auditor judgments relating to areas in the F.S. that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- (c) The effect on the audit of significant events or transactions that occurred during the period.
- (d) The auditor shall determine which of the matters so determined above were of most significance in the audit of the F.S. of the current period and therefore are the key audit matters.

Q.7. AKY Ltd. is a listed company engaged in the business of software and is one of the largest companies operating in this sector in India. The company’s annual turnover is 40,000 crores with profits of 5,000 crores. Due to the nature of the business and the size of the company, the operations of the company are spread out in India as well as outside India. The company’s contracts with its various customers are quite complicated & different. During the course of the audit, the audit team spends significant time on audit of revenue - be it planning, execution or conclusion. This matter was also discussed with management at various stages of audit. The efforts towards audit of revenue also involve significant involvement of senior members of the audit team including the audit partner. After completion of audit for the year ended on 31st March 2024, the audit partner was discussing significant matters with the management wherein they also communicated to the management that he plans to include revenue recognition as key audit matter in his audit report. The management did not agree with revenue recognition to be shown as key audit matter in the audit report, Comment. [MTP - Oct. 19]

Ans: Determining Key Audit Matters:

SA 701, “Communicating Key Audit Matters in the Independent Auditor’s Report”, deals with the auditor’s responsibility to communicate key audit matters in the auditor’s report. As per SA 701, the auditor shall determine, from the matters communicated with TCWG, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following:

- (i) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment.
- (ii) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- (iii) The effect on the audit of significant events or transactions that occurred during the period.

The auditor shall determine which of the matters determined in accordance with above were of most significance in the audit of the financial statements of the current period and therefore are the key audit matters.

In the instant case, AKY Ltd., a listed company engaged in the business of software and its contracts with its various customers are also quite complicated and different. Further, the audit team spends significant time on audit of revenue and efforts towards audit of revenue also involve significant involvement of senior members of the audit team including audit partner during audit. This matter was also discussed with management at various stages. After completion of audit, the audit partner communicated the management regarding inclusion of paragraph on revenue recognition as key audit matter in his audit report.

Conclusion: Assessment of the auditor is valid as concerned matter qualifies to be a key audit matter; hence, it should be reported accordingly by the auditor in his audit report.

Q.8. What is the auditor’s responsibility to report a key audit matter for which there are no relevant disclosures in the financial statements? [RTP-May 22]

Ans: Auditor’s responsibility to report KAM for which there are no relevant disclosures in the F.S.:

- When communicating key audit matters, the fact that there are no disclosures in the financial statements related to a matter determined to be a key audit matter does not relieve the auditor from the requirement to communicate it. An auditor may determine a key audit matter related to the audit for which relevant disclosure requirements do not exist in the applicable FRF.
- For example, the implementation of a new IT system (or significant changes to an existing IT system) during the period may be an area of significant auditor attention, in particular, if such a change had a significant effect on the auditor’s overall audit strategy or related to significant risk (e.g., changes to a system affecting revenue recognition)
- Also, if an auditor determines that it is necessary to include information about the entity in order to effectively describe a key audit matter that has not been disclosed by management and management does not agree to disclose that information, the auditor should reconsider the adequacy of the disclosures in accordance with applicable financial reporting framework.

- The auditor should communicate the matter as a key audit matter unless law or regulation precludes public disclosure about the matter or in extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Q.9. Below is draft extract of audit report of a listed company. Para (A) below reflects certain matter stated in audit report communicated with CFO of company and Para (B) is in nature of auditor's response to said matter.

(A) The Company recognizes revenues when the control of goods is transferred to the customer at the net consideration which the Company expects to receive for those goods from customers in accordance with contracts terms and conditions. The terms of sales arrangements based on the terms and conditions of relevant contract and nature of discount and rebates create complexities that require judgment in determining revenues.

(B) We read the Company's revenue recognition policy and assessed its compliance in terms of Ind AS 115 "Revenue from contracts with customers".

We assessed design and tested the operating effectiveness of internal controls related to sales and rebates/discounts.

We tested on a sample basis that revenue has been recognized in the proper period with reference to the supporting documents including confirmations from customers.

From description given above, identify what auditors are trying to report and under what heading such matter should be reflected in audit report of the company?

Ans: Communicating Key Audit Matters:

- Matter stated in question is in nature of Key audit matter and should be stated under heading "Key audit matters" in audit report. Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. Key audit matters are selected from matters communicated with TCWG.
- SA 701 states that auditor shall determine, from the matters communicated with TCWG, those matters that required significant auditor attention in performing the audit. In making this determination, significant auditor judgments relating to areas in the financial statements that involved significant management judgment including accounting estimates that have been identified as having high estimation uncertainty be taken into account.
- Matter stated in the question relates to revenue recognition and creation of complexities requiring judgment in revenues. Further, description also describes how matter was addressed by auditors by performing various audit procedures in accordance with SA 701.

Q.10. The property, plant and equipment of ABC Ltd. Included & 25.75 Crores of earth removing machines of outdated technology which had been retired from active use and had been kept for disposal after knock down. These assets appeared at residual value and had been last inspected ten years back. As an auditor, what may be your reporting concern as regards matters specified above? [May 18 (5 Marks)]

Ans: Reporting Concerns in relation to significant events:

Auditor is required to report under the various requirements of Standards of Auditing, legal and Regulatory provisions. In the present situation, major reporting requirements will be:

- (a) As per the requirement of SA 260 “Communication with Those Charged with Governance” auditor should communicate significant matters arising during the audit that were discussed, or subject to correspondence, with management.
- (b) The situation as given in the question appears to be a Key Audit Matter and hence auditor is required to report the situation in the audit report as Key Audit Matter.
- (c) Further as per requirement of Para 3(1) of CARO, 2020, auditor is required to comment
 - (i) Whether the company is maintaining proper records showing full particulars, including quantitative details and situation of Property, Plant and Equipment;
 - (ii) Whether these Property, Plant and Equipment have been physically verified by the management at reasonable intervals.

In the present case, physical verification of assets held under disposal was done ten years back.

Conclusion: In the present case, auditor reporting concerns will be as per the requirement of SA 260, SA 701 and Para 3(1) of CARO, 2020.

Alternative Answer: Answer of this question may also be based on the reporting issues like Valuation, Accounting and Disclosures as per the requirements of applicable FRF. In that case, if auditor is not satisfied with the valuation, accounting and disclosures, he may qualify the report as per the requirements of SA 705.

Q.11. While auditing the complete set of consolidated financial statements of] Ltd., a listed company, using a fair presentation framework, PQR & Co, a Chartered Accountant firm, discovered that the consolidated financial statements are materially misstated due to the non-consolidation of one of the subsidiaries. The material misstatement is deemed to be pervasive to the consolidated financial statements. The effects of the misstatement on the consolidated financial statements could not be determined because it was not practicable to do so. Thus, PQR & Co. decided to provide an adverse opinion for the same and further determined that, there are no key audit matters other than the matter to be described in the Basis for Adverse Opinion section. Comment whether PQR & Co. need to report under SA 701 “Communicating Key Audit Matters in the Independent Auditor’s Report”? [Dec. 21 (5 Marks); MTP-Sep. 22]

Ans: Relationship between Key Audit Matters, the Auditor’s Opinion and Other Elements of the Auditor’s Report:

- SA 700 establishes requirements and provides guidance on forming an opinion on the F.S. Communicating KAM is not a substitute for disclosures in the F.S. that the applicable FRF requires management to make, or that are otherwise necessary to achieve fair presentation.
- SA 705, “Modifications to the Opinion in the Independent Auditor’s Report”, addresses circumstances in which the auditor concludes that there is a material misstatement relating to the appropriateness or adequacy of disclosures in the financial statements.
- When auditor expresses a qualified or adverse opinion in accordance with SA 705, presenting the description of a matter giving rise to a modified opinion in Basis for Qualified (Adverse) Opinion section helps to promote intended users’ understanding and

to identify such circumstances when they occur. Separating the communication of this matter from other KAMs described in the Key Audit Matters section, therefore, gives it the appropriate prominence in the auditor's report.

- Further, when auditor expresses a qualified or adverse opinion, communicating other KAMS would still be relevant to enhancing intended users' understanding of the audit, and therefore the requirements to determine KAMs apply. If adverse opinion is expressed in circumstances when auditor has concluded that misstatements, individually or in the aggregate, are both material and pervasive to the F.S. depending on the significance of the matter(s) giving rise to an adverse opinion, the auditor may determine that no other matters are key audit matters.
- In the given situation J Ltd., a listed company, has not consolidated one of its subsidiaries. Further, Consolidated Financial Statements of Ltd. Are materially misstated due to such non- consolidation. The material misstatement is also deemed to be material and pervasive and effect of the failure to consolidate have not been determined. In the given situation it is appropriate to give Adverse Opinion by PQR & Co., a Chartered Accountant Firm.
- Since, in the given case, Adverse Opinion is being expressed thus PQR & Co. can communicate Key Audit Matter in given below manner:
“**Key Audit Matters:** Except for the matter described in the Basis for Adverse Opinion section, we have determined that there are no other key audit matters to communicate in our report”

Q.12. Mr. Hemant Ramsey was appointed as the engagement partner for conducting the audit of Kshetra Lap Ltd. for F.Y. 2023-24, on behalf of Ramsey & Associates. Mr. Vishay Tyagi was appointed as the engagement quality control reviewer by the firm for the said audit. During F.Y. 2023-24, there was an implementation of ERP system in a phased manner, in Kshetra Lap Ltd. due to which some of its business processes got automated. As a result of the implementation of such a system, there was a significant effect on the auditor's overall audit strategy. Mr. Hemant discussed the implementation of such a system with Mr. Vishay and also told him that such a matter may be a key audit matter to be reported in the audit report. Mr. Vishay considered the significance of such matter but however he was of the opinion that such a matter did not appear to link with the matters disclosed in the financial statements and so there was no need to disclose such matter as a key audit matter. Whether the contention of Mr. Vishay is proper with respect to the matters to be communicated as a key audit matter? [RTP-Nov. 21]

Ans: Determining Key Audit Matters:

SA 701, “Communicating Key Audit Matters in the Independent Auditor's Report”, deals with the auditor's responsibility to communicate key audit matters in the auditor's report. As per SA 701, the auditor shall determine, from the matters communicated with TCWG, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following:

- (i) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315 Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment.

- (ii) Significant auditor judgments relating to areas in the financial statements that involved significant auditor judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- (iii) The effect on the audit of significant events or transactions that occurred during the period.

Auditor shall determine which of the matters determined in accordance with above were of most significance in the audit of the F.S. of the current period and therefore are the key audit matters.

Such matters are often linked to matters disclosed in the F.S. and are intended to reflect areas of the audit of the financial statements that may be of particular interest to intended users.

In addition to matters that relate to the specific required considerations, there may be other matters communicated with TCWG that required significant auditor attention and that therefore may be determined to be key audit matters. Such matters may include, for example, matters relevant to the audit that was performed that may not be required to be disclosed in the financial statements. For example, the implementation of a new IT system (or significant changes to an existing IT system) during the period may be an area of significant auditor attention, in particular if such a change had a significant effect on the auditor's overall audit strategy or related to a significant risk (e.g., changes to a system affecting revenue recognition).

In the given case, there was implementation of ERP system in the company due to which some of its business processes got automated and which had a significant effect on the auditor's overall audit strategy during the period.

Accordingly, such a matter can be considered as a key audit matter if according to Mr. Hemant, such a matter required significant attention that had affected his overall audit strategy.

Conclusion: Contention of Mr. Vishay is not proper as matters that do not link with the matters disclosed in the financial statements can also be considered as a key audit matter if it required significant attention of the auditor which had an impact on its audit.

Q.13. CA. Amar has come across certain key matters while auditing the accounts of PR Ltd. for the financial year 2023-24. He, being the associate of your firm, seeks your advice on "Communicating Key Audit Matters" in the Auditor's report. Guide him.

Ans: Communicating Key Audit Matters:

- As per SA 701 "Communicating Key Audit matters in the Independent Auditor's Report" Key Audit Matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of F.S. of current period.
- The auditor shall describe each key audit matter, using an appropriate sub-heading, in a separate section of the auditor's report under the heading "Key Audit Matters,"
- The introductory language in this section of the auditor's report shall state that:
 - (a) Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period; and
 - (b) These matters were addressed in the context of the audit of the F.S. as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

- The description of each key audit matter in the Key Audit Matters section of the auditor's report shall include a reference to the related disclosure(s), if any, in the F.S. & shall address:
 - (a) Why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter, and
 - (b) How the matter was addressed in the audit.
- The auditor shall describe each key audit matter in the auditor's report unless:
 - (i) Law or regulation precludes public disclosure about the matter; or
 - (ii) In extremely rare circumstances, the auditor determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. This shall not apply if the entity has publicly disclosed information about the matter.

The auditor shall not communicate a matter in the Key Audit Matters section of the auditor's report when the auditor would be required to modify the opinion in accordance with SA 705 (Revised) as a result of the matter.

7.3 - SA 705 "Modifications to the Opinion in the Independent Auditor's Report"

Q.14. MNO Ltd. is a power generating company having its plants in the north eastern states of the country. For the FY 2023-24. M/s PRT & Associates are the statutory auditors of the company. During the course of audit, the audit team was unable to obtain sufficient appropriate audit evidence about a single element of the consolidated financial statements. That is, the auditor was also unable to obtain audit evidence about the financial information of a joint venture investment (In XYZ Ltd.) that represents over 90% of the entity's net assets. What kind of opinion should the statutory and that issue in such case?

Ans: **Type of opinion to be expressed:**

M/s PRT & Associates are unable to obtain sufficient appropriate audit evidence about the financial information of a joint venture investment that represents over 90% of the entity's net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are both material and pervasive to the consolidated financial statements.

Therefore, the statutory auditor should issue a disclaimer of opinion. Relevant extract of Disclaimer of Opinion Paragraph and Basis for Disclaimer of Opinion paragraph is as under:

Disclaimer of Opinion

We do not express an opinion on the accompanying F.S. of MNO Ltd. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these F.S.

Basis for Disclaimer of Opinion

The Group's investment in its joint venture XYZ Company is carried at 95 crores on the Group's consolidated balance sheet, which represents over 90% of the Group's net assets as on March 31, 2024. We were not allowed access to the management and the auditors of XYZ Company, including XYZ Company's auditors' audit documentation. As a result, we were unable to determine whether any adjustments were necessary in respect of the Group's proportional share of XYZ Company's assets that it controls jointly, its proportional share of XYZ Company's liabilities for which it is jointly responsible, its proportional share of XYZ's

income and expenses for the year, (and the elements making up the consolidated statement of changes in equity) and the consolidated cash flow statement.

Q.15. “When the auditor modifies the audit opinion, the auditor shall use the heading “Qualified Opinion”, “Adverse Opinion”, or “Disclaimer of Opinion”, as appropriate, for the Opinion section.” As an expert you are required to brief the special considerations required for expressing:

- (a) Qualified Opinion;
- (b) Adverse Opinion and
- (c) Disclaimer of Opinion.

[RTP-Nov. 18, May 20]

Ans: Special Considerations required for modified opinion:

(a) **Special consideration required for expressing Qualified Opinion:**

When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state that, in the auditor’s opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion section:

- (i) **When reporting in accordance with a fair presentation framework**, the accompanying financial statements present fairly, in all material respects (or give a true and fair view of) [...] in accordance with [the applicable FRF]; or
- (ii) **When reporting in accordance with a compliance framework**, the accompanying financial statements have been prepared, in all material respects, in accordance with [the applicable FRF].

When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase “except for the possible effects of the matter(s)..” for the modified opinion.

(b) **Special consideration needed for expressing Adverse Opinion:**

When the auditor expresses an adverse opinion, the auditor shall state that, in the auditor’s opinion, because of the significance of the matter(s) described in the Basis for Adverse Opinion section:

- (i) **When reporting in accordance with a fair presentation framework**, the accompanying financial statements do not present fairly (or give a true and fair view of) [...] in accordance with [the applicable FRF]; or
- (ii) **When reporting in accordance with a compliance framework**, the accompanying financial statements have not been prepared, in all material respects, in accordance with [the applicable FRF].

(c) **Special consideration is required for expressing Disclaimer of Opinion:** When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall:

- (i) State that the auditor does not express an opinion on the accompanying financial statements;
- (ii) State that, because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and
- (iii) Amend statement required in SA 700 (Revised), which indicates that financial statements have been audited, to state that the auditor was engaged to audit the

financial statements.

Unless required by law or regulation, when the auditor disclaims an opinion on the F.S., the auditor's report shall not include a Key Audit Matters section in accordance with SA 701.

Q.16. As an auditor of a company registered under section 8 of the Companies Act, 2013 you find that as per the notification of the Ministry of Corporate Affairs regarding applicability of Indian Accounting Standards (Ind-AS), the company has to prepare its financial statements for the year ended on 31st March, 2024 under Ind-AS. The management of the company is however of the strong view that being a section 8 company having charitable objects, Ind-AS cannot apply to the company. The financial statements are therefore prepared by the management under the earlier GAAP and a note for the same is given in the financial statements. How would you report on these financial statements? [Nov. 19 (5 Marks)]

Ans: Reporting on financial statements:

As per SA 200, the overall objectives of the auditor are:

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

In all cases when reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient, SAs require that auditor disclaim an opinion or withdraw from the engagement.

In the present case, company was required to prepare its F.S. as per Ind-AS, but the F.S. are being prepared under the earlier GAAP. FRF followed by the company is not acceptable.

Conclusion: FRF applied by the management is unacceptable and hence auditor is required to disclaim the opinion in accordance with SA 705 or withdraw from the engagement.

Note: Answer given in suggested Answer of ICAI is based on the provisions of Sec. 129 and Sec. 133 and specifies that the auditor is required to ensure applicable monetary limits w.r.t. Ind- AS and advise the management to prepare the F.S. as per Ind-AS.

Answer given in suggested answer does not seem to be appropriate as requirement of question was how the auditor report on such financial statements, whereas answer is given on applicability of Ind-AS as per legal requirements of company law.

Q.17. CA Madhu is the statutory auditor of Lakshmi Ltd. for the Financial year 2023-24. In respect of loans and advances of ₹ 75 Lakhs given to Sriman Pvt. Ltd., the company has not furnished any agreement to CA Madhu and in absence of the same, he is unable to verify the terms of repayment, chargeability of interest and other terms.

Justify the type of opinion which CA Madhu should give in such situation. Also, Draft an appropriate Opinion paragraph and Basis of opinion paragraph.

[Dec. 21 (5 Marks), MTP-March 23]

Ans: Type of Opinion to be expressed:

In the present case, with respect to loans and advances of ₹ 75 Lakhs given to Sriman Private Ltd., the company has not furnished any agreement to CA Madhu.

In absence of such agreement, CA Madhu is unable to verify the terms of repayment, chargeability of interest and other terms. For an auditor, while verifying any loans & advances, one of the most important audit evidences is the loan agreement. Therefore, the absence of such document in the present case, tantamount to a material misstatement in the financial statements of the company. However, the inability of CA Madhu to obtain such audit evidence is though material but not pervasive so as to require him to give a disclaimer of opinion.

Thus, in the present case, CA Madhu should give a qualified opinion. The relevant extract of the Qualified Opinion Paragraph and Basis for Qualified Opinion paragraph is as under:

Qualified Opinion

In our opinion and to the best of our information and according to the explanations given to us, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the F.S. of Lakshmi Ltd. give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as on 31.03.2024 and profit/ loss for the year ended on that date.

Basis for Qualified Opinion

The Company is unable to furnish the loan agreement with respect to loans and advances of ₹ 75 Lakhs given to Sriman Pvt. Ltd. Consequently, in absence of such agreement, we are unable to verify the terms of repayment, chargeability of interest and other terms.

Q.18. You have been appointed as an auditor of Dharmnath & Sons for FY 2023-24, as entity other than a company incorporated under the Companies Act, 2013, using a fair presentation framework Appointment had been made in the month of April, 2024. The financial statements have been prepared by the management in accordance with the Accounting Standards. The management had prepared by the management in accounts receivable system from November 2023 and still in the implementation phase and thus management is in the process of rectifying system deficiencies and correcting the errors. At the time of implementation of a new system, the earlier system of accounting of receivables had been discarded. The auditor was unable to obtain sufficient appropriate audit evidence about the entity's accounts receivable and inventories. The possible effects of the inability to obtain sufficient appropriate audit evidence are deemed to be both material and pervasive to the financial statements. Write the opinion paragraph and basis of opinion paragraph to be included in the Independent Auditor's Report. [RTP-May 22]

Ans: Opinion Paragraph and Basis of Opinion Paragraph:

Disclaimer of Opinion

We were engaged to audit the financial statements of Dharmnath & Sons ("the entity"), which comprise the balance sheet as on March 31, 2024, the statement of Profit and Loss, (the statement of changes in equity) and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

We do not express an opinion on the accompanying F.S. of the entity. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain SAAE to provide a basis for an audit opinion on these F.S.

Basis for Disclaimer of Opinion

We were not appointed as auditors of the Company until after March 31, 2024, and thus

did not observe the counting of physical inventories at the beginning and end of the year. We were unable to satisfy ourselves by alternative means concerning the inventory quantities held on March 31, 2023, and 2024, which are stated in the Balance Sheets at ₹ xxx and ₹ xxx, respectively. In addition, the introduction of a new computerized accounts receivable system in Nov. 2023 resulted in numerous errors in accounts receivable. As of the date of our report, management was still in the process of rectifying the system deficiencies and correcting the errors. We were unable to confirm or verify by alternative means accounts receivable included in the Balance Sheet at a total amount of ₹ xxx as on March 31, 2024. As a result of these matters, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded inventories and accounts receivable, and the elements making up the statement of Profit and Loss (and statement of cash flows).

Q.19. TEA Ltd., FMCG Company having its tea gardens in north eastern states of the country is exclusively dealing in blending, processing, packing and selling of various brands of Tea. During the year under audit, the company entered into joint venture for purchasing Tea Gardens in Sri Lanka and Kenya. M/s GN & Associates are the statutory auditors of the company for the financial year 2023-24. During the course of audit, the audit team was unable to obtain sufficient appropriate evidence about a single element of the consolidated financial statement being Joint venture investment in Kali Ltd. representing over 90% of the group's net assets having both material and pervasive possible effect to the consolidated financial statements. The group's investment in Kali Ltd. is carried at ₹ 100 crores in the group's consolidated balance sheet.

Draft opinion paragraph and basis of opinion paragraph.

[MTP-Oct. 22]

Ans: Drafting of Opinion Paragraph and Basis of Opinion Paragraph:

M/s GN & Associates are unable to obtain SAAE about the financial information of a joint venture investment that represents over 90% of the group's net assets. The possible effects of this inability to obtain sufficient appropriate audit evidence are both material and pervasive to the consolidated financial statements. Therefore, the statutory auditor should issue a disclaimer of opinion.

Relevant extract of Disclaimer of Opinion and Basis for Disclaimer of Opinion paragraph is as under:

Disclaimer of Opinion

We were engaged to audit the accompanying consolidated financial statements of Tea Ltd., FMCG Company (hereinafter referred to as the "Holding Company") and its subsidiaries (the Holding Company and its subsidiaries together referred to as "the Group), which comprise the consolidated balance sheet as on March 31, 2024, the consolidated statement of Profit and Loss, (consolidated statement of changes in equity) and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies (hereinafter referred to as the "Consolidated Financial Statements").

We do not express an opinion on the accompanying consolidated financial statements of the Group. Because of the significance of the matter described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these consolidated financial statements.

Basis for Disclaimer of Opinion

Group's Investment in its joint venture Kali Ltd. Company is carried at ₹ 100 crores on the Group's consolidated balance sheet, which represents over 90% of the Group's net assets as on March 31, 2024. We were not allowed access to the management and the auditors of XYZ Company, including XYZ Company's auditors' audit documentation. As a result, we were unable to determine whether any adjustments were necessary in respect of the Group's proportional share of Kali Ltd.'s assets that it controls jointly, its proportional share of Kali Ltd.'s liabilities for which it is jointly responsible, its proportional share of Kali Ltd.'s income and expenses for the year, (and the elements making up the consolidated statement of changes in equity) and the consolidated cash flow statement.

Q.20. CA. Uma is the Statutory Auditor of RJ Ltd. for the financial year 2023-24. The company is engaged in the production of electronic products. During the course of the audit, CA. Uma obtained certain audit evidence which led to disclosure of related party transactions and structured finance deals which was not considered with the affirmation leading to misstatement in the financial statements. Discuss how CA. Uma should deal with the situation in the auditor's report and the different options which can be considered? [Nov. 22 (5 Marks)]

Ans: **Auditor's duties in case of inconsistency in Audit evidences:**

- SA 705 "Modifications to the Opinion in the Independent Auditor's Report" deals with the auditor's responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with SA 700 (Revised), the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary.
- The decision regarding which type of modified opinion is appropriate depends upon:
 - (a) Nature of the matter giving rise to modification, that is, whether F.S. are materially misstated or, in the case of an inability to obtain SAAE, may be materially misstated; and
 - (b) Auditor's judgment about pervasiveness of the effects or possible effects of the matter on FS
- Further, auditor shall modify the opinion in the auditor's report when the auditor concludes that based on the audit evidence obtained, the F.S. as a whole are not free from material misstatement.
- In the present case, during the course of audit, CA Uma obtained certain audit evidence which were not consistent with the affirmation made in the financial statements. Therefore, CA Uma should modify his report in accordance with SA 705.

Conclusion: Since CA Uma has obtained audit evidence which are inconsistent with affirmations made in the F.S., CA Uma should modify his opinion as per the circumstances of the case.

- CA Uma shall express a qualified opinion when, having obtained sufficient appropriate audit evidence, he concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements
- CA Uma shall express an adverse opinion, when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

Q.21. CA Abhimanyu is the statutory auditor of PQR Ltd for the FY 2021-24. During the course of audit CA Abhimanyu the following:

- (1) With respect to the debtors amounting to ₹ 150 crores, no balance confirmation was received by the audit team. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The Company has created a provision for doubtful debts to the tune of ₹ 25 Cr. during the year under audit. The Company has stated that the provision is based on receivables which are older than 36 months, which according to the audit team is inadequate and as such the audit team is unable to ascertain the carrying value of trade receivables.
- (2) Further, in respect of Inventories (which constitutes 40% of the total assets of the company). during the reporting period, the management has not undertaken physical verification of Inventories at periodic intervals. Also, the Company has not maintained adequate inventory records at the factory. The audit team was unable to undertake the physical inventory count as such the value of inventory could not be verified.

Under the above circumstances what kind of opinion should CA Abhimanyu give?

[RTP-Nov. 22]

Ans: Type of Opinion to be expressed:

In the present case, CA Abhimanyu is unable to obtain sufficient and appropriate audit evidence with respect to the following:

- (1) The balance confirmation with respect to debtors amounting to ₹ 150 Crores is not available. Further there has been default in payment by the debtors and the provision so made is not adequate. The audit team is also unable ascertain the carrying value of trade receivables.
- (2) With respect to 40% of the company's inventory, neither the physical verification has been done by management nor are adequate inventory records maintained. The audit team is also unable to undertake the physical inventory count as such the value of inventory could not be verified.

In the above two circumstances the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive. Thus, CA Abhimanyu should give a Disclaimer of Opinion.

Relevant extract of Disclaimer of Opinion and Basis for Disclaimer of Opinion paragraph is as under:

Disclaimer of Opinion

We do not express an opinion on the accompanying F.S. of PQR Ltd. Because of the significance of the matters described in the Basis for Disclaimer of Opinion section of our report, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these F.S.

Basis for Disclaimer of Opinion

We are unable to obtain balance confirmation with respect to the debtors amounting to ₹ 150 Crores. Further, there have been defaults on the payment obligations by debtors on the due dates during the year under audit. The Company has created a provision for doubtful debts to the tune of ₹ 25 Crores during the year under audit which is inadequate in the circumstances of the company. The carrying value of trade receivables could not be ascertained. Further, in respect of Inventories (which constitutes 40% of the total assets of the company), during the

reporting period, the management has not undertaken physical verification of inventories at periodic intervals. Also, the company has not maintained adequate inventory records at the factory. We were unable to undertake the physical inventory count and as such the value of inventory could not be verified.

Q.22. In the financial year 2023-24, MSD Ltd. faced an extraordinary event (earthquake), which destroyed a lot of business activity of the company. These circumstances indicate material uncertainty on the company's ability to continue as going concern. Due to such event, it may not be possible for the company to realize its assets or pay off the liabilities during the regular course of its business. The financial statement and notes to the financial statements of the company do not disclose this fact. What kind of opinion should the statutory auditor of MSD Ltd. issue in such circumstances? [MTP-March 22, April 23]

Ans: Type of Opinion to be expressed:

In the present case, there exists a material uncertainty that cast a significant doubt on the company's ability to continue as going concern and the same is not disclosed in the F.S. of MSD Ltd.

As such, F.S. of MSD Ltd. for FY 2023-24 are materially misstated and the effect of the misstatement is so material and pervasive on the financial statements that giving only a qualified opinion will be insufficient and therefore the statutory auditor of MSD Ltd. should issue an adverse opinion.

Relevant extract of Adverse Opinion Paragraph and Basis for Adverse Opinion paragraph is as under:

Adverse Opinion

In our opinion, because of the omission of the information mentioned in the Basis for Adverse Opinion section of our report, the accompanying financial statements do not present fairly, the financial position of MSD Ltd. as on March 31, 2024, and of its financial performance and its cash flows for the year then ended in accordance with the Accounting Standards issued by the ICAI.

Basis for Adverse Opinion

MSD Ltd. has faced an extraordinary event (earthquake), which destroyed a lot of business activity of the company. Due to such event, it may not be possible for the company to realize its assets or pay off the liabilities during the regular course of its business. This situation indicates that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. The F.S. and notes to the financial statements of the company do not disclose this fact.

Q.23. ABC Ltd. has been dealing in tyres since 1995. The company envisaged to expand its business and wanted to manufacture the tyres besides trading. Accordingly, the machinery was imported, installed and manufacturing operations commenced. The Government also gave certain incentives like power subsidy, land acquisition subsidy, etc. After 2 years of operations, company received a notice from the Income Tax authorities to pay tax on incentive received in the form of power subsidy. The demand notice was served for 150.00 lakhs. The company, however filed an appeal with higher tax authorities against the demand and the matter is undecided as on 31.03.2024. Legal team of the Company anticipated that tax liability might mature. The company has not made a provision of anticipated tax liability.

Considering the provisions of Companies Act, 2013, how an auditor of ABC Ltd. should see this matter and report in audit report, if required? [July 21 (5 Marks), MTP-Sep. 22]

Ans: Reporting of Non-provision for tax:

The Council of the ICAI has taken note of the fact that there is a practice prevalent whereby companies do not make provision for tax even when such a liability is anticipated. It has expressed the view that on an overall consideration of the relevant provisions of law, non-provision for tax (where a liability is anticipated) would amount to contravention of the provisions of Sections 128 and 129 of the Companies Act, 2013.

Accordingly, it is necessary for the auditor to qualify his report and such qualification should bring out the manner in which the accounts do not disclose a “true and fair” view of the state of affairs of the company and the profit or loss of the company.

Applying the above to the facts given in the question, auditor should qualify his report. An example of the manner in which the report on the balance sheet and the Statement of Profit and Loss may be qualified in this respect is given below:

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

Q.24. After accepting the statutory audit of M/s All in One Ltd., a departmental store, you became aware of the fact that management of the company have imposed certain limitations on the scope of your assurance function which may adversely affect and result in your inability to obtain sufficient appropriate audit evidence to discharge your responsibility required by the statute. Indicate the consequences and your response to the limitations imposed by the management on your scope. [May 19 (4 Marks)]

Or

While conducting audit of VED Ltd., you as an auditor are not only prevented in completing certain audit procedures but also are not able to obtain audit evidence even by performing alternative procedures. How you will deal with this situation? [Jan. 21 (4 Marks)]

Ans: Limitation after the auditor has accepted the engagement:

- As per SA 705 “Modifications to the Opinion in the Independent Auditor’s Report”, if, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.
- If management refuses to remove the limitation, the auditor shall communicate the matter to TCWG, unless all of TCWG are involved in managing the entity, and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.
- If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall determine the implications as follows:
 - (a) If auditor concludes that the possible effects on the F.S. of undetected misstatements,

- if any, could be material but not pervasive, the auditor shall qualify the opinion; or
- (b) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall:
- (i) Withdraw from the audit, where practicable and possible under applicable law or regulation; or
 - (ii) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.
- If the auditor withdraws, before withdrawing, the auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.

Q.25. ADKS & Co. LLP are the newly appointed statutory auditors of PKK Ltd. During the course of audit, the statutory auditors have come across certain significant observations which they believe could lead to material misstatement of financial statements. Management has a different view and does not concur with the view of the statutory auditors. Considering this the statutory auditors are determining as to how to address these observations in terms of their reporting requirement. Please advise. [MTP-April 19]

Ans: Addressing material misstatements while reporting:

- As per SA 705, if the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement or the auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor shall modify the opinion in his report.
- The auditor in such a case needs to determine the modification as follows:
 - (a) **Qualified Opinion:** The auditor shall express a qualified opinion when:
 - (i) Auditor, having obtained SAAE, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the F.S.; or
 - (ii) The auditor is unable to obtain SAAE on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.
 - (b) **Adverse Opinion:** Auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements
 - (c) **Disclaimer of Opinion:** Auditor shall disclaim an opinion when the auditor is unable to obtain SAAE on which to base the opinion, and the auditor concludes that the possible effects on the F.S. of undetected misstatements, if any, could be both material and pervasive.
The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained SAAE regarding each of the individual uncertainties, it is not possible to form an opinion on the F.S. due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

Q.26. XYZ Ltd. is a company engaged in manufacture of cranes. CA Sudhir is statutory auditor of company for the FY 2023-24. The company has taken long-term funding for fixed capital requirements and short-term funding for its working capital requirements. During the course of audit, CA Sudhir found that the company's financing arrangements are about to expire and the company is unable to renegotiate or obtain the replacement financing. As such the company may be unable to realize its assets and discharge its liabilities in the normal course of business. Notes to accounts annexed to the financial statements discuss the magnitude of financing arrangements, the expiration and the total financing arrangements; however, the financial statements do not include discussion on the impact or the availability of refinancing. Thus, the financial statements (and notes thereto) do not fully disclose this fact. What kind of opinion should CA Sudhir issue in case of XYZ Ltd.?

Ans: Type of opinion to be expressed:

In the present case, XYZ Ltd. is unable to renegotiate or obtain the replacement financing for its long term and short-term funding requirements. This situation indicates the existence of a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern and therefore, XYZ Ltd. may be unable to realize its assets and discharge its liabilities in the normal course of business. Further, the financial statements of XYZ Ltd. do not disclose this fact adequately. Thus, the financial statements of XYZ Ltd. are materially misstated due to the inadequate disclosure of the material uncertainty. CA Sudhir will express a qualified opinion as the effects on the financial statements of this inadequate disclosure are material but not pervasive to the financial statements.

The relevant extract of the Qualified Opinion Paragraph and Basis for Qualified Opinion paragraph is as under:

Qualified Opinion

In our opinion and to the best of our information and according to the explanations given to us, except for the incomplete disclosure of the information referred to in the Basis for Qualified Opinion section of our report, the aforesaid standalone F.S. give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of XYZ Ltd. as on March 31, 2024, and profit/loss, for the year ended on that date.

Basis for Qualified Opinion

As discussed in Note 6, the Company's financing arrangements are about to expire and the Company has been unable to conclude renegotiations or obtain replacement financing. This situation indicates that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. The financial statements do not adequately disclose this matter.

Q.27. ABC Ltd. is a company engaged in the manufacture of iron and steel bars. PP & Associates are the statutory auditors of ABC Ltd. for the FY 2023-24. During the course of audit, CA Prakash, the engagement partner, found that the Company's financing arrangements have expired and the amount outstanding was payable on March 31, 2024. The Company has been unable to renegotiate or obtain replacement financing and is considering filing for bankruptcy. These events indicate a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business. The financial

statements (and notes thereto) do not disclose this fact. What opinion should CA Prakash express in case of ABC Ltd.?

Ans: Type of Opinion to be expressed:

In the present case based on the audit evidence obtained, CA Prakash has concluded that a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, and the entity is considering bankruptcy. The financial statements of ABC Ltd. omit the required disclosures relating to the material uncertainty.

In such circumstances, CA Prakash should express an adverse opinion because the effects on the financial statements of such omission are material and pervasive.

Relevant extract of Adverse Opinion Paragraph and Basis for Adverse Opinion paragraph is as under:

Adverse Opinion

In our opinion, because of the omission of the information mentioned in the Basis for Adverse Opinion section of our report, the accompanying financial statements do not present fairly, the financial position of the entity as on March 31, 2024, and of its financial performance & its cash flows for the year then ended in accordance with the Accounting Standards issued by the ICAI.

Basis for Adverse Opinion

The financing arrangements of ABC Ltd. has expired and the amount outstanding was payable on March 31, 2024. The entity has been unable to conclude renegotiations or obtain replacement financing and is considering filing for bankruptcy. This situation indicates that a material uncertainty exists that may cast significant doubt on the Company's ability to continue as a going concern. The financial statements do not adequately disclose this fact.

Q.28. If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor shall discuss the matter with management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, shall determine whether it is necessary to modify the opinion in the auditor's report in accordance with SA 705.

Under SA 705, in what circumstances does the report of the statutory auditor require modifications? What are the types of modifications possible in the said report?

Ans: Circumstances in which a modified opinion may be issued:

As per SA 705 "Modifications to the Opinion in the Independent Auditor's Report" a modified opinion may be expressed in the following circumstances:

- (a) The auditor concludes that, based on the audit evidence obtained, the F.S. as a whole are not free from material misstatement, may be due to following reasons:
 - Inappropriate method of selection of Accounting Policies;
 - Accounting policies are not consistent with applicable FRF;
 - Disclosures as required by FRF are not given.
- (b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, may be due to following reasons:
 - Limitations imposed by management
 - Circumstances beyond entity control (For Ex.: Accounting records destroyed by fire)

- Circumstances related to Nature and Timing of auditor's work.

Types of Modified Opinion:

- (a) **Qualified opinion:** It is issued under following circumstances:
- Financial statements are materially misstated which in the auditor's judgments are not pervasive.
 - Auditor is unable to obtain Sufficient and appropriate audit evidence which in the auditor judgment are not pervasive
- (b) **Adverse Opinion:** It is issued when financial statements are materially misstated which in the auditor's judgments is having pervasive effect.
- (c) **Disclaimer of Opinion:** It is issued when auditor is unable to obtain sufficient and appropriate audit evidence which in the auditor judgment are having pervasive effect.

Q.29. The auditor's inability to obtain sufficient appropriate audit evidence (also referred to as a limitation on the scope of the audit) may arise from:

- Circumstances beyond the control of the entity;
- Circumstances relating to the nature or timing of the auditor's work; or
- Limitations imposed by management.

Explain with the help of examples.

[RTP-May 20]

Ans: **Examples of situations in which auditor is unable to obtain SAAE:**

(i) Circumstances beyond entity control

- (1) The entity's accounting records have been destroyed.
- (2) The accounting records of a significant component have been seized indefinitely by governmental authorities.

(ii) Circumstances related to Nature and Timing of auditor's work

- (1) Entity is required to use the equity method of accounting for an associated entity, and the auditor is unable to obtain sufficient appropriate audit evidence about the latter's financial information to evaluate whether the equity method has been appropriately applied.
- (2) The timing of the auditor's appointment is such that the auditor is unable to observe the counting of the physical inventories.
- (3) The auditor determines that performing substantive procedures alone is not sufficient, but the entity's controls are not effective.

(iii) Limitations imposed by management

- (1) Management prevents the auditor from observing the counting of the physical inventory.
- (2) Management prevents the auditor from requesting external confirmation of specific account balances.

Q.30. CA. K is appointed statutory auditor of SEEK INDIA LTD under Companies Act, 2013 for the first time. The company is preparing its accounts keeping in view applicable requirements of Division II of Schedule III of Companies Act, 2013. On scrutiny of financial statements of company put up for audit, it was noticed that notes to accounts show ageing of trade payables as per amended requirements of Schedule III of the Companies Act, 2013. The ageing schedule forming part of notes is as under:

Outstanding for following periods from due date of payment (₹ In crore)

Particulars	Less than 1 year	1-2 years	2-3 years	More than 3 years	Total
MSME	NIL	NIL	NIL	NIL	NIL
Others	2	4	3	1	10
Disputed dues-MSME	NIL	NIL	NIL	NIL	NIL
Disputed dues-others	NIL	NIL	NIL	NIL	NIL

Besides above, current ratio, debt-equity ratio, trade payables turnover ratio and net profit ratio disclosed in notes to accounts have slipped drastically as compared to last year and from standard norms. Most of the key financial ratios are in red. There is no other relevant information concerning above in notes to accounts.

Further, on reviewing bank statement of cash credit limit (against hypothecation of paid stocks), it was noticed that there is no debit transaction in the month of March, 2024. On inquiry, he came to know that stock audit of company was conducted in the month of January, 2024 and stock auditors have commented vide their report dated 25.2.2024 that company had negative drawing power due to high creditors. Accordingly, the bankers have refused further debits in cash credit account from start of March, 2024. There is no information in this respect in financial statements and notes to accounts. Discuss how CA K should deal with above for reporting in his audit report under the Companies Act, 2013. [MTP-Oct. 22, RTP-May 23]

Ans: Reporting in case of significant doubt on the entity ability to continue as going concern:

- Based on the facts relating to ageing schedule given in the situation, it is clear that company is not able to pay its creditors on time. Outstanding to creditors for a period of 1 year or more account for 80% of total dues to the creditors from due date of payment. Most of key financial ratios are adverse. Further, bankers have refused further debits in cash credit account due to negative drawing power from March 2023. Cash credit loans are repayable on demand. There is no other information or disclosure available how company plans to run its business without bank finance.
- All these factors are indicators that a material uncertainty exists that may cast a significant doubt on company's ability to continue as going concern. There is no express disclosure of this fact in F.S. Therefore, it is a situation where material uncertainty exists which has cast a significant doubt on company's ability to continue as going concern in accordance with SA 570, "Going Concern".

Conclusion: Keeping in view the fact that although a material uncertainty exists casting a significant doubt on the ability of company to continue as going concern, adequate disclosure of material uncertainty is not made in financial statements, CA K shall give qualified or adverse opinion in accordance with SA-705, "Modifications to the Opinion in the Independent Auditor's Report".

7.4 - SA 706 "Emphasis of Matter Paragraph & Other Paragraphs in the Independent Auditor's Report"

Q.31. PTD Limited is engaged in business of executing construction contracts for its clients. There are non-current receivables outstanding in financial statements of the company as on 31st March, 2024 for ₹ 500 crore. Such amounts represent claims raised by the company on its clients relating to cost overruns necessitated due to delays caused by clients, change in work specifications and related matters. Besides negotiations, the company has also gone for arbitration in some of the said cases. The management of company has considered above

amounts to be fully recoverable as stated in notes to accounts.

CA. Piyush, auditor of the company, has relied only upon management representation in this regard. Besides, he has decided to include the said matter in “Emphasis of Matter” Paragraph in audit report.

How do you view decision to include above matter in “Emphasis of Matter” Paragraph by auditor of the company?

Ans: Reporting of ‘Emphasis of Matter’ Paragraph:

- Emphasis of Matter (EOM) is a paragraph included in the auditor’s report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor’s judgment, is of such importance that it is fundamental to users’ understanding of the financial statements.
- As per SA 706, objective of the auditor, having formed an opinion on the F.S., is to draw users’ attention, when in the auditor’s judgment it is necessary to do so, by way of clear additional communication in the auditor’s report, to:
 - (a) A matter, although appropriately presented or disclosed in the F.S., that is of such importance that it is fundamental to users’ understanding of the F.S. or
 - (b) As appropriate, any other matter that is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report.
- Further, auditor shall include an EOM paragraph in the auditor’s report provided the auditor would not be required to modify the opinion in accordance with SA 705 as a result of the matter.
- In the given situation, auditor has relied upon management representation letter only. He has not performed any other audit procedures like verifying contracts with customers, status of arbitration proceedings etc. Since management representations by themselves do not constitute SAAE, performing necessary audit procedures may lead auditor to conclude that modification in opinion is necessary. In such circumstances, matter cannot be included in EOM Paragraph.
- Therefore, auditor should form his opinion by performing necessary audit procedures and obtaining sufficient appropriate evidence. It is only when he concludes that modification of opinion is not required as a result of said matter in terms of SA 705, the said matter may be included in EOM paragraph.

Q.32. Beta Limited, is a company registered with SEBI, having five subsidiaries M/s XYZ, Chartered Accountants, have been appointed as Statutory Auditors for the audit of the consolidated Financial Accountants have been appointed as March 31, 2024. Out of five subsidiaries, the audit of one subsidiary was conducted by another auditor, M/s Badnam and Company, Chartered Accountants The “Opinion” para of audit report furnished by M/s XYZ Chartered Accountants is given below:

Opinion

In Our opinion and to the best of our information and according to the explanations given to us the consolidated financial statements give a true and fair view, except the financial statement of one subsidiary whose accounts were audited by M/s Badnam and Company, Chartered Accountants and about the same we are not in a position to express our opinion as the audit has not been performed by us:

- (i) In the case of the consolidated Balance Sheet, of the state of affairs of the company as on March 31, 2024.
- (ii) In the case of the consolidated profit and loss account, of the profit/loss for the year ended on that date.

Do you find any deficiencies in the opinion para? If yes, you are required to give your suggestions and redraft the opinion para.

Ans: Identification of deficiencies in opinion Para:

The opinion para contains the following deficiencies:

1. Out of five subsidiaries, the audit of one subsidiary was conducted by another auditor, M/s Badnam and Company - needs to be reported in other matter para.
2. Opinion regarding cash flow statement has not been covered.

As per SA 700 & 706 the redrafted opinion para and other matter para are given hereunder:

Opinion Para

In our opinion and to the best of our information and according to the explanations given to us and based on the consideration of the reports of the other auditors on the financial statements of the subsidiaries as noted below, the consolidated financial statements give a true and fair view in conformity with the accounting principles generally accepted in India:

- (a) in the case of the consolidated Balance Sheet, of the state of affairs of the Company as on March 31, 2024;
- (b) in the case of the consolidated Profit and Loss Account, of the profit/loss for the year ended on that date; and
- (c) in the case of the consolidated Cash Flow Statement, of the cash flows for the year ended on that date.

Other Matter Para

We did not audit the financial statements of one subsidiary, whose financial statements reflect total assets (net) of XXXX as on March 31, 2024, total revenues of XXXX and net cash outflows amounting to XXXX for the year then ended. These financial statements have been audited by other auditor's M/s Badnam and Company, Chartered Accountants whose reports have been furnished to us by the Management, and our opinion is based solely on the reports of the other auditors. Our opinion is not qualified in respect of this matter.

Q.33. Enumerate certain important matters which can be included in 'Emphasis of Matter Paragraph' in an Auditor's Report.

Ans: Matters which can be included in Emphasis of Matter Paragraph in Auditor's Report:

- As per 706 "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report" Emphasis of Matter is a paragraph which is included in auditor's report to draw users' attention to important matter(s) which are already disclosed in Financial Statements and are fundamental to users' for understanding of Financial Statements.
- Specific requirements for the auditor to include Emphasis of Matter paragraphs in the auditor's report in certain circumstances. These circumstances include:
 - (a) When a FRF prescribed by law or regulation would be unacceptable but for the fact that it is prescribed by law or regulation.
 - (b) To alert users that the financial statements are prepared in accordance with a special purpose framework.

- (c) When facts become known to the auditor after the date of the auditor's report and the auditor provides a new or amended auditor's report (i.e., subsequent events).
- Matters which can be included in 'EOM Paragraph' in an Auditor's Report, may be listed as below:
 - (a) Uncertainty relating to the future outcome of an exceptional litigation or regulatory action.
 - (b) A significant subsequent event that occurs between the date of the financial statements and the date of the auditor's report.
 - (c) Early application (where permitted) of a new accounting standard that has a pervasive effect on the financial statements in advance of its effective date.
 - (d) A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position.

Q.34. Where should the placement of the key audit matters section be in the auditor's report? [RTP-May 22]

Ans: **Placement of the key audit matters section in the auditor's report:**

- Generally, the Key Audit Matters section is required to be placed after the Basis for Opinion paragraph and before the Management's Responsibility paragraph.
- In case, 'Material uncertainty relating to going concern' section is required as per SA 570(Revised), then KAM section is placed after that section.
- Further, regarding placement of KAM section, SA 706, "Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report" provides as under:
When a Key Audit Matters section is presented in the auditor's report, an EOM paragraph may be presented either directly before or after the Key Audit Matters section, based on the auditor's judgment as to the relative significance of the information included in the Emphasis of Matter paragraph. The auditor may also add further context to the heading "Emphasis of Matter", such as "Emphasis of Matter - Subsequent Event", to differentiate the Emphasis of Matter paragraph from the individual matters described in the Key Audit Matters section.

Q.35. AKB Associates, a renowned audit firm in the field of CA practice for past two decades. The firm was appointed to conduct statutory audit of Rica Ltd. an unlisted company, which is engaged in the business of paper manufacturing. It decided to commence the audit for the recently concluded financial year. Once after making significant progress in the audit, the auditors made the following observations:

Observation 1: The management had disclosed in the financials that, during the year, one of the warehouses of the Company was affected due to a major flood. As a result of the same, the Company had incurred some losses. But the management was of the view that it was not material.

Observation 2: Due to flood, few records maintained by the Company with respect to a particular transaction was completely destroyed and there was no duplicate record maintained by the Company. However, those details were not pervasive, but material.

You are required to advise, whether AKB Associates should report Observations 1 and 2 in its audit report? If so, under which heading should it be reported? [RTP-Nov. 20]

Ans: Reporting of modifications and EOM Para:

Observation 1:

Facts of the case: The management had disclosed in the financials that, during the year, one of the warehouses of the Company was affected due to a major flood. As a result of the same, the Company had incurred some losses. But the management was of the view that it was not material.

Relevant provisions: As per SA 706, “Emphasis of Matter Paragraph & Other Matter Paragraph in the Independent Auditor’s Report”, an Emphasis of Matter Paragraph refers to matter appropriately disclosed in the financials, that in the auditor’s judgment is of such importance that it is fundamental to users’ understanding of the financials.

Reporting requirements: The auditor shall report about the consequences of the flood which affected the Company’s warehouse under Emphasis of Matter Paragraph.

Observation 2:

Facts of the case: Due to flood, few records maintained by the Company with respect to a particular transaction was completely destroyed and there was no duplicate record maintained by the Company. However, those details were not pervasive, but material.

Relevant provisions: As per SA 705, “Modification to Opinion in the Independent Auditor’s Report”, where the auditor is unable to obtain sufficient and appropriate audit evidence and where such matter is material but not pervasive, the auditor shall issue a qualified opinion.

Thus, in the given situation, on account of flood few records pertaining to particular transactions was completely destroyed and in the absence of duplicate records, the auditor was unable to obtain sufficient and appropriate audit evidence and those details were material but not pervasive.

Reporting requirements: In accordance with SA 705, auditor is required to issue qualified opinion.

Q.36. Difficult Books Limited is engaged in manufacturing of active pharmaceutical ingredients. Due to change in laws and regulations, every company engaged in manufacturing in active pharmaceutical ingredients would now require production capacity license which will restrict the production of companies. Management of the company assessed the impact of the change in law over the financial position of company and appropriately disclosed the same in the financial statement.

Audit Team of the company evaluated management’s disclosure and found it appropriate and sufficient. However, considering the said matter as most important and fundamental to users understanding regarding financial statement the audit team decided to disclose the same in Other Matter Paragraph. You as an Engagement Partner are required to guide the Audit Team with respect to reporting of the said matter in Audit Report. [MTP-Oct. 22]

Ans: Emphasis of Matter Para and Other Matter Para in Audit Report:

- As per SA 706, “Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor’s Report” if the auditor considers it necessary to draw users’ attention to a matter presented or disclosed in the financial statements that, in the auditor’s judgment, is of such importance that it is fundamental to users’ understanding of the financial statements, the auditor shall include an Emphasis of Matter paragraph in the auditor’s report provided:

- (i) The auditor would not be required to modify the opinion in accordance with SA 705 as a result of the matter; and
 - (ii) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.
- In the instant case, since Difficult Books Limited is engaged in manufacturing of active pharmaceutical ingredients, would now require production capacity license which will restrict the production of companies, due to change in laws and regulations. Management of the Difficult Books Limited assessed the impact of the change in law over the financial position of company and appropriately disclosed the same in the financial statement.
 - Audit team evaluated management's disclosure and found it appropriate & sufficient. However, considering the said matter as most important and fundamental to users understanding regarding financial statement the audit team decided to disclose the same.

Conclusion: As the matter discussed is already disclosed and presented appropriately in financial statement and is of such importance that is fundamental to the users understanding of the financial statement, it required to be disclosed under Emphasis of Matter paragraph. Therefore, decision of audit team to disclose the same in Other Matter Paragraph is not in order, it should be disclosed in Emphasis of Matter Paragraph.

Q.37. D Ltd., a Delhi based company having turnover of ₹ 25 crores, has a branch at USA having a turnover of ₹ 10 lakhs (as converted from US dollars). The area where the branch office is located in USA was severely affected by storms and the office along with all accounting records was completely destroyed. Due to the unavailability of records, the financial statements of D Ltd. for the financial year 2023-24 did not include the figures pertaining to the said branch. As the statutory auditor of D Ltd., how will you report on the same?

Ans: **Reporting on financial statements when information of component is not included:**

- As per SA 200 "Overall Objectives of the Independent Auditor and Conduct of Audit in accordance with Standards on Auditing" in conducting an audit of financial statements, the overall objective of the auditor is to obtain reasonable assurance about whether the Financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable FRF. In all cases when reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient, the SAs require that the auditor disclaim an opinion or withdraw from the engagement.
- In the present case, D Ltd., a Delhi based company having turnover of ₹ 25 crores, has a branch at USA having a turnover of ₹ 10 lakhs (as converted from US dollars). The area where the branch office is located in USA was severely affected by storms and the office along with all accounting records was completely destroyed. Due to the unavailability of records, the financial statements of D Ltd. for the financial year 2023-24 did not include the figures pertaining to the said branch.
- In the present situation, company is required to make appropriate disclosures in the notes to accounts in this regard. Based on the disclosures made in the financial statements,

auditor is required to include an Emphasis of Matter Para in the auditor's report as per requirement of SA 706. If, however no disclosure is made in the financial statements, auditor need to qualify the audit report as turnover of the branch is only ₹ 10 lakhs which does not seems to have pervasive effect as the total turnover of the company is ₹ 25 Crores.

Conclusion: If appropriate disclosures are given in Notes to Accounts, an unmodified opinion with Emphasis of Matter para need to be issued. However, if appropriate disclosures are not given in Notes to Accounts, auditor should qualify the report in accordance with SA 705.

Note: Answer given in Suggested Answer of ICAI is based on the provisions of Sec. 143(8) and specifies who can conduct branch audit.

Answer given in suggested answer does not seems to be appropriate as requirement of question was how the auditor report, whereas content of answer is primarily on the basis of who can conduct branch audit. In a case where branch records are not available, then there is no logic of mentioning the provisions relating to the concept of branch audit. Answer needs to be given from perspective of company auditor, how to deal in such a situation.

Q.38. In respect of the audit of BDS Ltd., the statutory auditor of the company noticed some matters. The statutory auditor wants to draw the user's attention towards such matters, though his opinion is not modified in respect of such matters. Draft the relevant paragraphs of the audit report for the following matters:

- (1) The company has a plan to resume its construction activities with respect to one of its thermal power projects, The activity of such power plant was suspended in the FY 2020-21. The thermal power project comprises of the plant and equipment amounting to ₹ 5.95 crores and capital work in progress of ₹ 147.50 crores.
- (2) The financial statements of 5 branches are included in the Standalone Financial Statements of BDS Ltd. whose financial statements reflect total assets of ₹ 90 crores as on 31.03.2024 and total revenue from operations of ₹ 40 crores for the year ended on that date. The financial statements of these branches have been audited by the branch auditors.

Ans: **Emphasis of Matter Para and Other Matter Para in Audit Report:**

Emphasis of Matter

We draw attention to the following note of the standalone financial statements: Note 27 regarding the plans of the Company to resume construction/developmental activities of a thermal power project. The carrying amounts related to the project as on 31st March, 2024 comprise of plant and equipment of ₹ 5.95 crores and capital work in progress of ₹ 147.50 crores. Our opinion is not modified in respect of this matter.

Other Matter

We did not audit the financial statements of 5 branches included in the Standalone Financial Statements of the company whose financial statements reflect total assets of ₹ 90 crores as on 31.03.2024 and total revenue from operations of ₹ 40 crores for the year ended on that date. The financial statements of these branches have been audited by the branch auditors whose reports have been furnished to us, and our opinion insofar as it relates to the amounts and disclosures included in respect of these branches, is based solely on the report of the branch auditors.

Our opinion is not modified in respect of this matter.

7.5 - Notes on Accounts & Qualifications; Audit Report & Certificate; Communication with TCWG

Q.39. Distinguish between Notes on Accounts and Qualifications.

Ans: Notes on Accounts vs. Qualifications:

Notes on Accounts	Qualifications
Notes represents management's stand on a matter Qualification and assessment on all matters involving difference of opinion between them and the auditors.	Qualifications represents auditor disagreement on the matters with Management.
Notes of a qualificatory nature appear in the accounts and forms part of Financial Statements.	Qualifications are stated by auditor in the auditor's report.
Management may insist upon the auditor for not modifying his audit opinion considering the management has disclosed full facts & assessment of the matter through notes on the F.S.	Auditor needs to exercise his professional judgment to determine whether disclosures in the notes alone would suffice or a qualification is needed in audit report.
Notes on accounts includes information which is necessary to make the financial statements understandable by the users.	Qualification must be expressed by the Auditor in a clear and unambiguous manner.

Q.40. Compare and explain the following: Reporting to Shareholders vs. Reporting to TCWG

Ans: Reporting to Shareholders vs. Reporting to TCWG:

Reporting to Shareholders	Reporting to TCWG
Sec. 143 of Companies Act, 2013 deals with the provisions relating to reporting to Shareholders. Thus, it is a Statutory Audit Report which is addressed to the members.	SA 260 deals with the provisions relating to reporting to TCWG.
Statutory Audit Report is on true and fair view and as per prescribed Format.	It is a reporting on matters those charged with governance like scope of audit, audit procedures, audit modifications, etc.
Statutory Audit Reports are in public domain.	Reporting to TCWG is an internal document i.e., private report.

Q.41. Compare and explain the following: Audit Qualification vs. Emphasis of Matter.

Ans: Audit Qualification vs. Emphasis of Matter:

Audit Qualification	Emphasis of Matter (EOM)
SA 705 deals with provisions relating to Audit Qualification.	SA 706 deals with the provisions relating to Emphasis of Matter.
Audit Qualifications are modifications to Auditors opinion where auditor concludes that there is a material misstatement in the F.S. due to which the modification to the	<ul style="list-style-type: none"> ▪ EOM is a paragraph which is included in auditor's report to draw users' attention to important matter(s) which are already disclosed in F.S. and are

opinion of the auditor is necessary.	<ul style="list-style-type: none"> ▪ fundamental to users' for understanding of F.S. ▪ EOM presupposes that there is Sufficient Appropriate audit evidence and the matter has been correctly disclosed.
<p>Audit Qualifications are given when auditor has concluded that F.S. are materially misstated or do not confirm to FRF.</p> <p>Depending upon nature of material misstatement being pervasive or otherwise the appropriate type of modified opinion is issued.</p>	EOM is a paragraph which is issued when the auditor feels that it is necessary to invite attention to a particular matter which has been appropriately disclosed in F.S. which in the opinion of the auditor is necessary for better understanding of the F.S.

Q.42. Write a short note on Certificate for Special Purpose vs. Audit Report.

Ans: Report and Certificate:

Audit Report: An audit report is a formal statement usually made after an enquiry, examination or review of specified matters under report & includes the reporting auditor's opinion thereon. While issuing an audit report, auditor is responsible to ensure that his opinion is in due accordance with facts, and that it is arrived at by the application of due care & skill.

Meaning of Certificate: A certificate is a written confirmation of the accuracy of the facts stated therein and does not involve any estimate or opinion. Such certificates are often required by Government authorities in support of statements or other information prepared by an enterprise. Such certificates represent that the auditor has verified certain figures and is satisfied about their accuracy.

Report	Certificate
It is an expression of opinion on true & fair view of financial statements & books of account.	It is a confirmation of correctness and accuracy of subject matter for which certificate is being issued.
Report is based on practitioner professional judgment.	Certificate is based on actual facts & figures.
Scope of audit is wide and generally covers an opinion on complete set of financial statements.	Scope of certificate is narrow and restricted to subject matter only.
Audit report is generally issued annually as per the requirements of statute.	Certificates are issued as per the specific requirements of law.
Auditor's responsibility in case any misstatement is not being identified, is subject to his negligence in performance of his duties.	In case of wrong certification, auditor is held liable irrespective of due diligence.

7.6 - SA 710 “Comparative Information - Corresponding Figures and Comparative Financial Statements”

Q.43. Mr. A, a practicing Chartered Accountant, audited the financial statements of C Ltd. for the previous year 2022-23 and expressed an unmodified opinion. C Ltd. was of the view that Mr. A is not conducting the audit properly and therefore, for the current year 2023-24, it appointed Ms. B, a leading practicing Chartered Accountant to conduct the audit and present Comparative Financial Statements. Ms. B, while performing the auditing procedures, found that C Ltd. has undercharged the wages of ₹ 10 lakhs during the previous year resulting in overstatement of profits. What are the further procedures, Ms. B is required to pursue?

Ans: Auditor’s Procedures in respect of examination of comparative financial statements:

1. SA 710 “Comparative Information - Corresponding Figure & Comparative Financial Information deals with the auditor’s responsibilities regarding comparative information in an audit of F.S.
2. To examine comparative information, auditor is required to perform the following procedures:
 - Determine whether F.S. include Comparative information required by FRF, & Whether such information is classified appropriately.
 - Evaluate Whether the comparative information agrees with the amounts and other disclosures presented in the prior period; and
3. In given case, auditor identified material misstatement for the previous year, F.S. of which are audited by Mr. A; Ms. B Current Auditor is required to discuss the matter with the management and issue suitable report based on the action taken by the management in this regard.

Conclusion: Ms. B is required to communicate the matter to the management and request them to inform the same to Mr. A. After revision or non-revision of the prior period’s F.S., Ms. B may report accordingly.

Q.44. It was observed from the modified audit report of the financial statements of AS Ltd. for the year ended on 31st March, 2023 that depreciation of 2.50 crores for the year 2022-23 had been charged off to the statement of Profit and Loss instead of including it in “Carrying value of asset under construction”. State in relation to the audit for the year ended on 31st March 2024, whether such modification in the previous year’s audit report would have any audit implication for the current year and if yes, how would you deal with it in your audit report? [Nov. 18 (5 Marks), MTP-Oct. 20, March 23]

Ans: **Impact of Modification in the predecessor auditor’s report:**

- SA 710 “Comparative Information - Corresponding Figure and Comparative Financial Information deals with the auditor’s responsibilities regarding comparative information in an audit of F.S.
- As per SA 710, when the auditor’s report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modified opinion is resolved and properly accounted for or disclosed in the financial statements in accordance with the applicable FRF, auditor’s opinion on the current period need not refer to the previous modification.
- As per SA 710, if the auditor’s report on the prior period, as previously issued, included a modified opinion and the matter which gave rise to the modification is unresolved,

the auditor shall modify the auditor's opinion on the current period's financial statements. In the Basis for Modification paragraph in the auditor's report, the auditor shall either:

- (a) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or
- (b) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

- In the instant case, it was observed from the modified audit report of the financial statements of AS Ltd. for the year ended on 31st March, 2023 that depreciation of ₹ 2.50 crores for the year 2022-23 had been charged off to the statement of Profit & Loss instead of including it in "Carrying value of asset under construction".

Conclusion: If AS Ltd. does not correct the treatment of depreciation to the extent of ₹ 2.50 crore for previous year, the auditor will have to modify his report for both current and previous year's figures as mentioned above. If, however, the figures and provisions are corrected, the auditor need not consider to the earlier year's modification.

Q.45. You as a statutory auditor had audited the financial statements of A Ltd., a listed company, for F.Y, 2022-23. The company has included the comparative financial information in the financial statements prepared for the current F.Y. 2023-24. You as an auditor want to obtain sufficient appropriate audit evidence that comparative financial information has been presented, in all material aspects, in accordance with the requirements in the applicable financial reporting framework. List out audit procedures, as specified in relevant SA, which you are required to follow for the purpose. [Dec. 21 (5 Marks)]

Ans: Auditor's Procedures in respect of examination of corresponding figures:

SA 710 "Comparative Information - Corresponding Figure and Comparative Financial Information deals with the auditor's responsibilities regarding comparative information in an audit of financial statements.

To examine the comparative information, auditor is required to perform the following procedures:

- (a) Determine whether F.S. include Comparative information required by applicable FRF, & whether such information is classified appropriately.
- (b) Evaluate the following:
 - Whether the comparative information agrees with the amounts and other disclosures presented in the prior period; and
 - Whether the accounting policies reflected in the comparative information are consistent with those applied in the current period.
 - * Whether, changes in accounting policies, if any, have been properly accounted for & adequately presented and disclosed.
- (c) If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists.

- (d) If the auditor had audited the prior period's financial statements, the auditor shall also follow the relevant requirements of SA 560, "Subsequent Events".
- (e) As required by SA 580, "Written Representations", the auditor shall request written representations for all periods referred to in the auditor's opinion. The auditor shall also obtain a specific written representation regarding any prior period item that is separately disclosed in the current year's statement of profit and loss.

Q.46. For the year ended on 31st March, 2023, the audit report of Avinash Ltd., contained a qualification regarding non-provision for diminution in the value of investments to the extent of ₹ 50 lakhs. As an Auditor of the Company for the year 2023-24, how would you report, If:

- (i) The Company does not make provision for diminution in the value of investments in the year 2023-24.
- (ii) The Company makes adequate provision for diminution in the year 2023-24.

[May 18 (5 Marks)]

Ans: Auditor's responsibilities w.r.t. Corresponding figures:

- As per SA 710, "Comparative Information - Corresponding Figures & Comparative Financial Statements When the auditor's report on the prior period, as previously issued, included a modified opinion and the matter which gave rise to the modified opinion is resolved and properly accounted for or disclosed in the financial statements in accordance with the applicable FRF, the auditor's opinion on the current period need not refer to the previous modification.
- SA 710 further states that if the auditor's report on the prior period, as previously issued, included a modified opinion and the matter which gave rise to the modification is unresolved, the auditor shall modify the auditor's opinion on the current period's financial statements.
- In the Basis for Modification paragraph in the auditor's report, the auditor shall either:
 - (i) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or
 - (ii) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

Conclusion:

- (a) If P Ltd. does not make provision the auditor will have to modify his report for both current and previous year's figures as mentioned above.
- (b) If, however, the provision is made, the auditor need not refer to the earlier year's modification.

7.7 - SA 720 "The Auditor's Responsibilities relating to Other Information."

Q.47. LMP Associates, Chartered Accountants, conducting the audit of PQR Ltd., a listed Company for the year ended on 31st March, 2024 is concerned with the auditor's responsibilities relating to other information, both financial and non-financial, included in the Company's annual report. While regarding other information, LMP Associates

considers whether there is a material inconsistency between other Information & the financial statements. As a basis for the consideration the auditor shall evaluate their consistency, compare selected amounts or other items in the other information with such amounts or other items in the financial statements. Guide LMP Associates with examples of “Amounts” or “other items” that may be included in the “other information” with reference to SA 720. [Nov. 19 (5 Marks), MTP-April 21]

Ans: Reading and considering the Other information:

SA 720 “Auditor’s Responsibilities relating to Other Information” deals with auditor’s responsibilities relating to Other Information, whether financial or non-financial information included in an entity’s annual report.

Other information may include amounts or other items that are intended to be the same as, to summarize, or to provide greater detail about, the amounts or other items in the financial statements. Examples of such amounts or other items may include:

(A) Amounts:

1. Items in a summary of key financial results, such as net income, earnings per share, dividends, sales and other operating revenues, and purchases and operating expenses.
2. Selected operating data, such as income from continuing operations by major operating area, or sales by geographical segment or product line.
3. Special items, such as asset dispositions, litigation provisions, asset impairments, tax adjustments, environmental remediation provisions, & restructuring & reorganization expenses.
4. Liquidity & capital resource information, such as cash, cash equivalents & marketable securities; dividends; & debt, capital lease & minority interest obligations.
5. Capital expenditures by segment or division.
6. Amounts involved in, and related financial effects of, off-balance sheet arrangements.

(B) Other Items:

1. Explanations of critical accounting estimates & related assumptions.
2. Identification of related parties & descriptions of transactions with them.
3. Descriptions of the nature of off-balance sheet arrangements.
4. Descriptions of guarantees, indemnifications, contractual obligations, litigation or environmental liability cases.
5. Descriptions of changes in legal or regulatory requirements, such as new tax or environmental regulations.
6. General descriptions of the business environment and outlook.
7. Descriptions of trends in market prices of key commodities or raw materials.
8. Contrasts of supply, demand and regulatory circumstances between geographic regions.

Q.48. GS & Co., Chartered Accountants, have been appointed Statutory Auditors of MAP Ltd. for the F.Y 2023-24. The audit team has completed the audit and is in the process of preparing audit report Management of the company has also prepared draft annual report. Audit in-charge was going through the draft annual report and observed that

the company has included an item in its Annual Report indicating downward trend in market prices of key commodities/raw material as compared to previous year. However, the actual profit margin of the company as reported in financial statements has gone in the reverse direction. Audit Manager discussed this issue with partner of the firm who in reply said that auditors are not covered with such disclosures made by the management in its annual report, it being the responsibility of the management.

Do you think that the partner is correct in his approach on this issue?

Discuss with reference to relevant Standard on Auditing the Auditor's duties with regard to reporting. [Nov. 20 (4 Marks), MTP-Oct. 21, April 23; RTP-May 23]

Ans: Auditor's responsibilities as to Other Information included in Annual Report:

- SA 720 "The Auditor's Responsibilities relating to Other Information" deals with the auditor's responsibilities relating to Other Information, whether financial or non-financial information included in an entity's annual report. Accordingly, descriptions of trends in market prices of key commodities or raw materials is an example of amounts or other items that may be included in the other information.
- The auditor's discussion with management about a material inconsistency (or other information that appears to be materially misstated) may include requesting management to provide support for the basis of management's statements in the other information. Based on management's further information or explanations, the auditor may be satisfied that the other information is not materially misstated. For example, management explanations may indicate reasonable and sufficient grounds for valid differences of judgment.

Auditor's duties with regard to reporting:

If the auditor concludes that a material misstatement of the other information exists, the auditor shall request management to correct the other information. If management:

- (i) Agrees to make the correction, the auditor shall determine that the correction has been made; or
- (ii) Refuses to make the correction, the auditor shall communicate the matter with those charged with governance and request that the correction be made.

Conclusion: Considering the requirements of SA 720 as stated above, it can be concluded that partner is not correct in his approach.

Q.49. ING Associates, Chartered Accountants, conducting the audit of XYZ Ltd., a listed Company for the year ended on 31st March 2024 is concerned with the auditor's responsibilities relating to misstatements in other information, both financial and non-financial, included in the Company's annual report. While reading other information, ING Associates considers whether there is any material misstatement of the other information in the Company. After performing their procedures, the auditor concludes that a material misstatement of the other information exists. ING Associates discussed with the management about the other information that appeared to be materially misstated to the auditor and also requested management to provide evidence for the basis of management's statements in the other information along with supporting documents. Guide ING Associates as how to respond to that material misstatement of other information obtained prior to the date of auditor's report. Will your answer be different in case ING Associates conclude the same after the date of auditor's report? [MTP-Oct. 20]

Ans: Auditor's responses on a material misstatement in the Other Information:

- SA 720 "The Auditor's Responsibilities relating to Other Information" deals with the auditor's responsibilities relating to Other Information, whether financial or non-financial information included in an entity's annual report.
- If the auditor concludes that a material misstatement of the other information exists, the auditor shall request management to correct the other information. If management:
 - (a) Agrees to make the correction, the auditor shall determine that the correction has been made; or
 - (b) Refuses to make the correction, the auditor shall communicate the matter with TCWG and request that the correction be made.
- If the auditor concludes that a material misstatement exists in other information obtained prior to the date of the auditor's report, and the other information is not corrected after communicating with TCWG, the auditor shall take appropriate action, including:
 - (a) Considering the implications for the auditor's report and communicating with TCWG about how the auditor plans to address the material misstatement in the auditor's report,
 - (b) Withdrawing from the engagement, where withdrawal is possible under applicable law or regulation.
- If the auditor concludes that a material misstatement exists in other information obtained after the date of the auditor's report, the auditor shall:
 - (a) If the other information is corrected, perform the procedures necessary in the circumstances; or
 - (b) If the other information is not corrected after communicating with TCWG, take appropriate action considering the auditor's legal rights and obligations, to seek to have the uncorrected material misstatement appropriately brought to the attention of users for whom the auditor's report is prepared.

7.8 - Duties of Auditor

Q.50. CA G, was appointed by DP Ltd., as Statutory Auditor. While doing the audit of DP Ltd., CA G observed that certain loans and advances were made without proper securities; certain trade receivables and trade payables were adjusted inter se; and personal expenses were charged to revenue. As a company auditor comment on the reporting responsibilities of CA G. [Nov. 19 (5 Marks)]

Ans: Inquiry into Propriety Matters u/s 143(1):

- Section 143(1) of the Companies Act, 2013 requires the auditor to conduct inquiry into certain matters and if the auditor finds answer of any of these matters in adverse, auditor is required to report, otherwise no reporting is required. In relation to observations stated in the question, auditor should inquire as follows:
 1. Clause (a) of Sec. 143(1) requires the auditor to inquire "Whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members".
 2. Clause (b) of section 143(1), requires the auditor to inquire "whether transactions which are represented merely by book entries are prejudicial to the interests of the company".

3. Clause (e) of section 143(1) requires the auditor to inquire “Whether personal expenses have been charged to revenue account”.

- If auditor finds that the loans and advances have not been properly secured, he may enter an adverse comment in the report without modifying opinion on F.S. if the loans and advances are properly described and presented in terms of Part I of Schedule III to the Companies Act.
- If relation to his observation regarding inter se adjustment of trade receivables and trade payables, being a book entry, auditor should have inquired into the legitimate interests of the company. If appears prejudicial, he may enter adverse comment in the report.
- Regarding charging of personal expenses to revenue account auditor should inquire whether such expenses are incurred on the basis of the company’s contractual obligations, or in accordance with accepted business practice. If personal expenses incurred by the company are not covered by contractual obligations or by accepted business practice and charged to revenue account, it would be the duty of the auditor to report thereon.

Conclusion: In instant case, Mr. G, statutory auditor, needs to enquire in light of above provisions, as a result of the enquiries if he is satisfied then there is no further duty to report on these matters.

Q.51. As an auditor, how would you deal with the following: In the audit of ABC Private Limited, auditor came across cases of payments to Directors, whereby, expenses of a personal nature were re-imbursed. [Nov. 20 (4 Marks)]

Ans: Personal Expenses of Directors:

- All payments to Directors as remuneration or perquisites whether in the case of a public or private company need to be authorised in accordance with the Companies Act as well as Articles of Association of the company.
- If the terms of appointment of a Director include payment of expenses of a personal nature, then such expenses can be incurred by the company; otherwise, no such expense can be incurred or reimbursed by the company.
- In the instant case the auditor has to ensure that the payment is authorized by the Articles of Association and the same has been covered by terms of appointment.
- Further as this payment is also covered u/s 143(1), and hence auditor is also required to inquire into the matter and make a disclosure in his report accordingly.

Q.52. You have been appointed statutory auditor of a company for the financial year ended 31st March, 2023 in place of the retiring auditor. During the course of audit, you observe that a fraud had been committed by a general manager who retired in March 2023. While going into further details, it was found that the fraud was going on since last 2-3 years and the total amount misappropriated was likely to exceed ₹ 100 lakhs. As statutory auditor, what would be your reporting responsibilities to the government? [Nov. 17 (5 Marks)]

Ans: Auditor’s duties to report fraud to the Central Government:

- Sec. 143(12) of Companies Act, 2013 requires that if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amounts as may be prescribed, is being or has been

committed in the company by its officers or employees, auditor shall report the matter to the C.G. within such time and in such manner as may be prescribed. For this purpose, Rule 13 prescribes the amount of ₹ 1 Cr. or more.

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

- (1) If an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of ₹ 1 Cr. or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the CG.
- (2) The auditor shall report the matter to the CG as under:
 - (a) the auditor shall report the matter to the Board or the Audit Committee, as the case may be, immediately but not later than 2 days of his knowledge of the fraud, seeking their reply or observations within 45 days;
 - (b) on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the CG within 15 days from the date of receipt of such reply or observations;
 - (c) in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of 45 days, he shall forward his report to the CG along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;
 - (d) the report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same;
 - (e) the report shall be on the letterhead of the auditor containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number; and
 - (f) the report shall be in the form of a statement as specified in Form ADT-4.

Q.53. Mr. Raj, the engagement partner of R.O.K. & Co., in connection with statutory audit of Waria Ltd., had assigned the responsibility of enquiring into propriety matters of the Company as required by section 143(1) of the Companies Act, 2013, to Mr. Samay, an engagement team member. Mr. Samay while making such enquiries, was having following queries, as tabulated below, which he ought to get resolved from Mr. Raj, as follows:

Sr. No.	Query of Mr. Samay
1	What documents to be seen in case of loan given by the company in lieu of hypothecation of goods from lender as a security for the purpose of reporting as per clause (a) of Sec. 143(1)?
2	What shall be cost of Debentures and Bonus Shares sold by the company for which the cost is not ascertainable for the purpose of reporting as per clause (c) of Sec. 143(1).

3	Whether the shares allotted by Waria Ltd. against a loan taken by it from a NBFC can be considered to be allotted for cash for the purpose of reporting as per clause (1) of Sec.143(1)?
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Assuming that you are Mr. Raj the engagement partner, please provide answer to the queries of Mr. Samay? [MTP-March 21]

Ans: Responses to Queries raised by Samay:

Query 1: What documents to be seen in case of loan given by the company in lieu of hypothecation of goods from lender as a security for the purpose of reporting as per clause (a) of section 143(1) of the Companies Act, 2013?

Response: Mr. Samay should see deed of Hypothecation or other document creating the charge. together with a statement of stocks held at the balance sheet date in order.

Query 2: What shall be the cost of Debentures and Bonus Shares sold by the company for which the cost is not ascertainable for the purpose of reporting as per clause (c) of section 143(1) of the Companies Act, 2013?

Response:

For Debentures sold: Where the cost of debentures sold is not ascertainable, the book value thereof at the date of sale may be treated as the cost for the purposes of this clause.

For Bonus Shares sold: When bonus shares are received, the number of shares in the portfolio would be increased by the bonus shares while the cost of the total portfolio would remain the same as before. The result would be that the average cost per unit of the total holding would come down proportionately. The usual accounting practice for apportioning the cost of a part of the total holding on the sale thereof is to take it at its average cost.

Query 3: Whether the shares allotted by Waria Ltd. against a loan taken by it from a NBFC can be considered to be allotted for cash for the purpose of reporting as per clause (f) of section 143(1) of the Companies Act, 2013?

Response: The law on the subject has hitherto been that, where the consideration for the issue of shares is an adjustment against a bona fide debt payable in money on demand by the company, the shares are deemed to have been subscribed in cash.

According to the legal opinion obtained by the ICAI, the expression “shares allotted for cash” may also include shares allotted against a debt. Therefore, in cases which are covered by the decision in Spargo’s case, no comment is required by the auditor, even though the company may have in the Return of Allotment u/s 75, shown such shares as allotted against adjustment of a debt. Thus, the shares allotted by Waria Ltd. against a loan taken by it from a NBFC can be considered to be allotted for cash.

7.9 - Matters to be included in Auditor’s Report under CARO, 2020

Q.54. The Property, Plant and Equipment of Amir Ltd. included ₹ 25.75 crores of earth removing machines of outdated technology which had been retired from active use and had been kept for disposal after knock down. These assets appeared at residual value and had been last inspected ten years back. As an Auditor, what may be your reporting concern in view of CARO, 2020 on matters specified above? [MTP-April 21]

Ans: Reporting w.r.t. Fixed Assets:

- Para 3(i) of CARO, 2020 requires the auditor to comment:
 - ⇒ whether the property, plant and equipment assets have been physically verified by the management at reasonable intervals;

- ⇒ whether any material discrepancies were noticed on such verification and if so;
- ⇒ whether the same have been properly dealt with in the books of account.
- In the present case, PPE included ₹ 25.75 crores of earth removing machines of outdated technology which had been retired from active use and had been kept for disposal after knock down. These assets appeared at residual value and had been last inspected ten years back.
- Inspection of abovementioned machine was done 10 years back. Though it is a retired machine, however value is ₹ 25.75 crores which is a significant amount, requires physical verification at regular intervals.

Conclusion: Auditor is required to state the fact about discrepancies in system of physical verification of machineries held for disposal.

Q.55. Jam Private Limited was engaged in business of manufacture of Cycles. CA Roy was appointed as a Statutory Auditor of the Company for the financial year 2021-22. During the year under audit, Jam Private Limited obtained working capital facilities from ABC Bank Limited for ₹ 10 crore hypothecating the Stock of goods as primary security. On inquiry CA Roy was informed by management that stock statements are furnished periodically to ABC Bank Limited and the details of submission of quarterly stock statement are as follows:

Period of Quarter	Stock Value as per Books of Account as at the end of the quarter (₹ in Crore)	Stock Value as per quarterly statement submitted to ABC bank limited as at the end of quarter (₹ in Crores)
Q1-2021-22	11.50	14.00
Q2-2021-22	14.75	17.00
Q3-2021-22	11.50	14.00
Q4-2021-22	15.25	15.25

The management of Jam Private Limited did not disclose the above variations in Notes to accounts forming part of financial Statements of the Company for the year 2021-22. The management replied that there are no variations as on the Balance sheet date and further they are of the view that stock statement furnished to bank is only a formality and computed arbitrarily only for the purpose of securing higher drawing power and hence statutory auditors need not be bothered.

Is the contention of the management valid? As a Statutory Auditor how CA Roy should deal and discuss the disclosure/reporting requirements if any, as per the Companies Act, 2013 and CARO, 2020. [May 22 (5 Marks); MTP-March 23]

Ans: Reporting requirements under Companies Act, 2013 and CARO, 2020

- As per Schedule III of the Companies Act, 2013, where the Company has borrowings from banks or financial institutions on the basis of security of current assets, it shall disclose the following:
 - (a) whether quarterly returns or statements of current assets filed by the Company with banks or financial institutions are in agreement with the books of account.
 - (b) if not, summary of reconciliation and reasons of material discrepancies, if any to be adequately disclosed. w.r.t. Inventories.
- Clause (b) of Para 3(ii) of CARO, 2020 requires the auditor to report whether during any point of time of the year, the company has been sanctioned working capital limits in

excess of ₹ 5 crore, in aggregate, from banks or financial institutions on the basis of security of current assets; whether the quarterly returns or statements filed by the company with such banks or financial institutions are in agreement with the books of account of the Company, if not, give details.

- In the given case, company has obtained working capital facilities from ABC Bank Limited for ₹ 10 crore hypothecating the stock of goods as primary security. Quarter-wise stock statements filed by the company with the banks are not in agreement with the books of account.

Conclusion: Contention of the management that there are no variations as on the Balance sheet date and statutory auditors need not be bothered is not correct. Such variations need to be disclosed in Notes to Accounts forming part of financial statements and also need to be reported by auditor under CARO, 2020. CA. Roy should report the differences as per the Companies Act, 2013 and CARO 2020 as follows:

Q.56. Gautam Limited had borrowed ₹ 1,000 crore from XYZ Bank, the principal of which was repayable after 5 years and interest was payable at the end of each year. For 4 years, Gautam Limited paid the interest amount on time. Gautam Limited defaulted the 5th instalment of interest payment and principal which was due on June 30, 2022. On March 31, 2023, Gautam Limited approached XYZ bank and MNO bank to restructure the existing liability. As a result, the existing principal and outstanding and overdue interest was restructured into a new loan amounting to 1,100 crore. The management did not provide any disclosure for the default on the loan on the belief that the old loan ceased to exist and the new loan has maturity after 5 years.

During the statutory audit for the financial year 2022-23, KP & Co. identified this transaction and obtained the relevant documents and understanding. Based on the underlying documents, it was identified that the said restructuring agreement was approved and signed on April 8, 2023, by both of the banks. As a result, on March 31, 2023, the restructuring was still not approved.

In the light of the above scenario, kindly guide the statutory auditors in the reporting of this transaction. [RTP-Nov. 22]

Ans: Reporting w.r.t. repayment of dues:

- As per Para 3(ix)(a) of CARO, 2020 auditors of a company are required to comment in his report whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, the period and amount of default to be reported as per the format below:

Nature of borrowing, including debt securities	Name of lender*	Amount not paid on due date	Whether principal or interest	No. of days delay or unpaid	Remarks, If any

*Lender-wise details to be provided in case of defaults to banks, financial institutions and Government.

- In the given case, the company Gautam Limited defaulted in payment of the principal amount of the loan due of 1000 crore on 30 June 2022 and the interest instalment of 100 crore. The said default continued till the end of the year and on 8 April 2023, a

restructuring agreement was signed by the banks and company for restructuring the outstanding loan. Moreover, no disclosure was provided by the company with respect to the said matter.

Conclusion: Auditor is required to report under Clause (ix) of Para 3 of CARO, 2020, i.e., whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, then provide the details of the period and the amount of default.

Also, the auditor needs to consider the impact of such non-disclosure and the non-compliance with the FRF and accordingly the auditor needs to either issue a qualified opinion or an adverse opinion as per SA 705.

Q.57. SPM Ltd., about to complete fifty years of age since its incorporation in the F.Y 2023-2024, decided during the F.Y. 2022-23 to upgrade its registered office at an important location in Mumbai city. As part of planned package, it decided to acquire a land very adjacent to the site of registered office, which had been owned by Mr. Parry who is a director of the Company. Since he was reluctant to part with the ownership, he had been persuaded to convey the property in favour of the company in exchange of a site owned by the company located at the next street to the street where the registered office is situated, which is 1.50 times larger in area than that of the site owned by the director adjacent to the Registered office. Happier with what he was offered in negotiation, Mr. Parry agreed for transferring the property in favour of the company in a deed of exchange duly executed by authorized persons of the Board, and Mr. Parry. The registration formalities were completed by 31st Dec., 2022. Assuming that you are engagement partner for the audit of the accounts of the company for the financial year ended on 31st March, 2023, give a list of additional audit procedures and reporting requirements, if any, that this transaction might trigger in your audit. [May 23 (5 Marks)]

Ans: Reporting under CARO, 2020:

- Para 3(xv) of CARO, 2020 requires the auditor to comment “whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether provisions of Section 192 of Companies Act, 2013 have been complied with”.
- Reporting requirements under this clause are in two parts. The first part requires the auditor to report on whether the company has entered into any non-cash transactions with the directors or any persons connected with such director/s. The second part of the clause requires the auditor to report whether the provisions of section 192 of the Act have been complied with. Therefore, the second part of the clause becomes reportable only if the answer to the first part is in affirmative.
- For reporting on the first part of this clause, the starting point of the auditor’s procedures could be obtaining a management representation as to whether the company has undertaken any non-cash transactions with the directors or persons connected with the directors. The auditor would need to corroborate the management representation with sufficient appropriate audit evidence.
- The second part of this clause requires the auditor to report whether the company has complied with the provisions of section 192 in this regard. Section 192(1) and (2) of the Act envisage the following compliances in respect of such transactions:

- (i) Company should have obtained a prior approval for such arrangement by a resolution in the general meeting.
 - (ii) If the concerned Director or connected person is a director of the company's holding company, the latter too should have obtained a similar prior approval for the arrangement by a resolution at its general meeting.
 - (iii) Notice for approval of the resolution should contain details of the arrangement along with the value of assets involved duly calculated by a registered valuer.
- Auditor should check compliance with section 192(2) of the Act and verify the notice of the general meeting that it includes particulars of arrangement along with the value of the assets involved in such arrangements.

Suggested paragraph on reporting:

According to information and explanations given to us, Company has entered into non-cash transactions with one of the directors/persons connected with the director during the year, by the acquisition of assets by assuming directly related liabilities, which in our opinion is covered under the provisions of Sec. 192 of the Act, and for which approval has not yet been obtained in a general meeting of the Company. In case said non-cash transactions are entered into by company after obtaining prior approval of shareholders in general meeting, then, factual position giving details of approval must be disclosed.

Q.58. Whilst the Audit team has identified various matters, they need your advice to include the same in your audit report in view of CARO, 2020:

- (a) The long-term borrowings from the parent has no agreed terms and neither the interest nor the principal has been repaid so far. [MTP-Nov. 21]
- (b) The Company is in the process of selling its office along with the freehold land available at Chandigarh and is actively on the lookout for potential buyers. Whilst the same was purchased at ₹ 25 Lakhs in 2008, the current market value is ₹ 250 Lakhs.
This property is pending to be registered in the name of the Company, due to certain procedural issues associated with the Registration though the Company is having a valid possession and has paid its purchase cost in full. The Company has disclosed this amount under Fixed Assets though no disclosure of non-registration is made in the notes forming part of the accounts. [MTP-Oct. 21]
- (c) An amount of 3.25 Lakhs per month is paid to M/s. WE CARE Associates, a partnership firm, which is a 'related party' in accordance with the provisions of the Companies Act, 2013 for the marketing services rendered by them. Based on an independent assessment, the consideration paid is higher than the arm's length pricing by 0.25 Lakhs per month. Whilst the transaction was accounted in the financial statements based on the amounts' paid, no separate disclosure has been made in the notes forming part of the accounts highlighting the same as a 'related party' transaction. [MTP-Oct. 19, MTP-Nov. 21]
- (d) The Internal Auditor of the Company has identified a fraud in the recruitment of employees by the HR department wherein certain sums were alleged to have been taken as kickback from the employees for taking them on board with the Company. After due investigation, the concerned HR Manager was sacked. The amount of such kickbacks is expected to be in the range of ₹ 12 Lakhs.

[MTP-March 19, Oct. 21., RTP-May 19]

Ans: Reporting under CARO, 2020:

- (a) Auditor is required to report the matter as per Para 3(xiii) of CARO, 2020 which requires him to report “whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards”.
- (b) Auditor is required to report the matter as per Para 3(i)(c) of CARO, 2020 which requires him to report, “whether the title deeds of all the immovable properties disclosed in the financial statements are held in the name of the company. If title deeds are not held in name of the company, details thereof to be provided in the below mentioned format:

Description of Property	Gross carrying value	Held in name of	Whether promoter, director or their relative or employee	Period held - indicate range, where appropriate	Reason for not being held in name of company*

*Also indicate if in dispute.

- (c) Auditor is required to report the matter as per Para 3(xiii) of CARO, 2020 which requires him to report whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards”.

Reporting is required, as one of related party transaction amounting ₹ 3.25 lakhs per month i.e. in lieu of marketing services has been noticed of which amount ₹ 0.25 lakh per month is exceeding the arm’s length price has not been disclosed highlighting the same as related party transactions as per AS 18.

- (d) Auditor is required to report the matter as per Para 3(xi) of CARO, 2020 which requires him to report, “whether any fraud by the company or any fraud on the Company has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated.”

Reporting is required, as a fraud has been identified in recruitment of employees by the HR Department wherein certain sums were alleged to have been taken as kickback from the employees of company amounting to ₹ 12 lakhs approx.

Q.59. LIU Private Limited is a company based out of Mumbai. The company had an authorised capital of ₹ 200 lakh and paid-up capital plus reserves of ₹ 95 lakh as of 31st March. During the audit for the year ended 31st March 202X, the auditor M/s Y&S Associates noted the following points:

- (i) On 15th December, the company had total bank borrowings of ₹ 75 lakh. On the said date, the company received a new loan of 30 lakh for a new project that was to be developed. However, the project was shelved on 17th December due to technical reasons, and the whole loan was paid on the same date.
- (ii) During the financial year, a new proceeding was initiated against the company for holding a benami property worth ₹ 2.5 crore. However, the company’s legal team had advised that the case would not withstand the law and would be dismissed during

the hearing in April of next financial year.

- (iii) The company had incurred a cash loss of 39 lakh during the financial year compared to a cash profit of ₹ 15 lakh in the previous financial year. The total turnover of the company for the financial year was ₹ 45 Crore.

During the year, the Y&S Associates had offered to resign from acting as the company's auditors. However, they later decided to postpone their resignation to the following year. At the conclusion of the audit, there was a difference of opinion between two articled assistants (Jack & Jill), who were assigned to the engagement, concerning disclosing the points mentioned above in the Companies (Auditor's Report) Order 2020. Jack was of the opinion that the proceeding initiated under Benami Property Act need not be disclosed since the expert legal team had informed them that the case would not withstand the law. However, he insisted that the cash loss shall be disclosed along with the amount. Jill was of the opinion that CARO is not at all applicable to the company, hence nothing needs to be reported. They both approached the firm's partners (Mr. Y & Mr. S) to resolve their argument. Mr Y supported Jack's viewpoint & Mr S supported Jill's viewpoint. Now, both partners approached their Senior Partner to get clarification on the same. As a Senior Partner, kindly clarify the correct disclosure requirement. [RTP-May 23]

Ans: Applicability of CARO, 2020:

CARO 2020 is applicable to every company, including a foreign company, except,

- (i) a banking company;
- (ii) an insurance company;
- (iii) a company licensed to operate under section 8 of the Companies Act,
- (iv) a One Person Company and a small company, and
- (v) a private limited company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than ₹ 1 crore as on the balance sheet date and which does not have total borrowings exceeding ₹ 1 crore from any bank or financial Institution at any point of time during the financial year and which does not have a total revenue as disclosed in Scheduled II to the Companies Act, 2013 (including revenue from discontinuing operations) exceeding 10 crore during the financial year as per the financial statements.

In the given case though LIU is a private company, and its paid-up capital is less than ₹ 1 crore as on the balance sheet date, it is to be noted that for the period 15th December to 17th December, the total borrowings of the company had exceeded ₹ 1 crore (75 lakh + 30 lakh). The borrowings are less than ₹ 1 crore as of the balance sheet date and the authorised capital is ₹ 200 lakh, are irrelevant to the current scenario. Also, the turnover of the company was greater than ₹ 40 crore. Hence, CARO 2020 is applicable to LIU Private Limited.

Reporting requirements under CARO, 2020:

- (i) As per Para 3(1)(e) of CARO 2020, auditor shall report whether any proceedings have been Initiated or pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 and rules made thereunder, if so, whether the company has appropriately disclosed the details in its financial statements.

In the given situation, a new proceeding was initiated against the company for holding a benami property worth ₹ 2.5 crores during the financial year. However, the company's legal team had advised that the case would not withstand the law and would be dismissed

during the hearing, which would be held in April of the next financial year.

Therefore, above observation of a new proceeding initiated against the company for holding a benami property worth ₹ 2.5 crores need to be disclosed as per Para 3(1)(e) of CARO 2020.

- (ii) As per Para (xvii) of CARO 2020, auditor shall include a statement on whether the company has incurred cash losses in the financial year and in the immediately preceding financial year, if so, state the amount of cash losses.

In the given situation, the company incurred a cash loss of ₹ 39 lakh during the financial year. Hence, a cash loss of ₹ 39 lakh during the financial year need to be reported as per clause (xvii) of para 3 of CARO 2020.

- (iii) As per clause (xviii) of para 3 of CARO 2020, auditor shall include a statement on whether there has been any resignation of the statutory auditors during the year, if so, whether the auditor has taken into consideration the issues, objections or concerns raised by the outgoing auditors.

In the instant case, there has been no resignation made by the statutory auditors during the financial year. The mere fact that Y&S Associates were thinking of resigning does not matter in the current scenario, and hence this clause shall not be applicable in the given situation.

Q.60. You are appointed as the Auditor of XMP Pvt. Ltd. for financial year 2022-23 after the resignation of RS & Co. Chartered Accountants, as statutory auditor of the company. RS & Co., had certain concerns on the accounting matters of the company, leading to change of auditors. All the compliances u/ss 139 & 140 are made by the company with regard to resignation and appointment.

During the course of audit, it came to your notice that a survey has been conducted on December 7, 2022 by the Income Tax Department and department has unearthed unrecorded sales of ₹ 5 lakhs which had been made in cash on different dates during the year 2021-22. XMP Pvt. Ltd. has purchased gold from such collections and these transactions are not recorded. Company surrendered and disclosed these transactions before the assessing officer and paid taxes thereon. However, company has not recorded those transactions in books of account even after surrender before Income Tax authorities.

You want to report the above matters in CARO, but the management requested you not to report them. Comment with respect to auditor's response to the management and his reporting requirements to the shareholders. [Nov. 22 (5 Marks)]

Ans: Considerations of issues raised by outgoing auditor:

- Clause (xviii) of Para 3 of CARO, 2020 requires the auditor to report whether there has been any resignation of the statutory auditors during the year, if so, whether the auditor has taken into consideration the issues, objections or concerns raised by the outgoing auditors.
- The incoming auditor should consider the reasons for resignation. The incoming auditor should also refer to last audit/review report issued by the outgoing auditor to understand the modifications, if any, in the audit/review report.
- Clause (viii) of Paragraph 3 of CARO, 2020 requires the auditor to report whether any transactions not recorded in the books of account have been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act,

1961, if so, whether the previously unrecorded income has been properly recorded in the books of account during the year.

- In the given case outgoing auditor, RS & Co. had certain concerns on the accounting matters of the company, leading to change of auditors. Further incoming auditor came to notice that there were unrecorded cash sales of ₹ 5 lakhs during the year 2021-22 & purchased gold; company surrendered and disclosed these transactions before the assessing officer and paid taxes thereon. However, company has not recorded those transactions in books of account even after surrender before Income Tax authorities. Management requested auditor not to report the matters.

Conclusion: Management request cannot be accepted. Auditor is under a duty to report the matter under Clauses (viii) and (xiii) of Para 3 of CARO, 2020. In addition, auditor is required to determine the impact of undisclosed transactions on the financial statements of current year & make suitable modifications in audit report as per requirements of SA 705.

Q.61. In the course of audit of MM Ltd., your audit team has identified the following matter:

All amount of ₹ 4 Lakhs per month for the marketing services rendered is paid to M/s. MG Associates, a partnership firm in which Director of MM Ltd. is also a managing partner, with a profit sharing ratio of 30%. Based on an independent assessment, the consideration paid is higher than the arm's length pricing by ₹ 1.50 Lakhs per month. Whilst the transaction was accounted in the financial statements based on the amounts paid, no separate disclosure has been made in the notes forming part of the accounts.

Give your comments for reporting under CARO.

[Nov. 20 (4 Marks)]

Ans: Reporting of Related Party Transactions under CARO:

- Clause (xiii) of Para 3 of CARO, 2020, requires auditor to report whether all transactions with the related parties are in compliance with Secs. 177 & 188 of Companies Act, 2013 where applicable and the details have been disclosed in the F.S. etc., as required by the applicable ASs.
- Therefore, the duty of the auditor, under this clause is to report:
 - (i) Whether all transactions with the related parties are in compliance with sections 177 and 188 of the Companies Act, 2013.
 - (ii) Whether related party disclosures as required by relevant Accounting Standards (AS 18, as may be applicable) are disclosed in the financial statements.
- In the given case, MG Associates is a related party and also rendering marketing services to MM Ltd. in return of Consideration of ₹ 4 Lakhs which is related party transaction. No separate disclosure has been made in the notes to accounts in this context, which was required to be made.

In view of above, Auditor shall report as under:

1. Nature of the related party relationship and the underlying transaction: MG Associates is a partnership firm in which Director of MM Ltd. is also a managing partner, with a profit sharing ratio of 30%. Payment of ₹ 4 Lakhs to MG Associates is a related party transaction.
2. Amount involved is consideration for the Marketing services rendered by MG Associates (₹ 4 Lakhs p.m.) is higher than the arm's length pricing by ₹ 1.50 Lakhs p.m. (₹ 18 Lakhs p.a.)

Q.62. As an auditor, how will you report under CARO in each of the following situation?

- (i) Since more than seven months, payment of electricity bills to company established under statute is outstanding.
- (ii) The company had imported goods 5 years back and were placed in bonded warehouse till the end of financial year under Audit. The company has not paid import duty as goods have not been removed from such warehouse. The company has also not paid rent and interest expenditure payable on the amount of custom duty.
- (iii) The company has received income tax assessment order along with demand notice from Assessing officer. The company has not paid dues payable as the same is not acceptable to the company. The company has neither preferred appeal against the order nor an application for rectification of mistake has been made. The company has just merely represented to the Assessing Officer.
- (iv) The company in view of voluminous pay-roll data consistently follows the method of making lump sum deposit of estimated amount of ESI collections and adjust the excess or deficit against next following months' deposit and the difference of the said amount always remains insignificant. [Jan. 21 (5 Marks)]

Ans: Reporting under CARO:

Clause (vii)(a) of Para 3 of CARO, 2016 requires the auditor to state in his report whether the company is regular in depositing undisputed statutory dues including provident fund, Employees' State Insurance, Income-tax, Sales-tax, Services tax, Duty of Customs, Duty of Excise, Value Added Tax, cess and any other statutory dues to the appropriate authorities & if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than 6 months from the date they became payable, shall be indicated.

It is important to mention that any sum, which is to be regularly paid to an appropriate authority under a statute (whether Central, State or Local or Foreign) applicable to the company, should be considered as a "statutory due" for the purpose of this clause. In other words, obligation to pay a statutory due is created or arises out of a statute, rather than being based on an independent contractual or legal relationship.

Conclusion: Based on the above stated provisions, following conclusions may be drawn:

- (i) Any sum payable to an electricity company as electricity bill would not constitute a statutory due as dues has arisen on account of contract of supply of goods or services between the parties. Thus, reporting under CARO is not required for electricity dues.
- (ii) In case of imported goods placed in a bonded warehouse, payment of import duty is to be made when the goods are removed from the bonded warehouse. However, till the time the importer opts to remove the goods from the warehouse, the importer is required to incur the rent and interest expenditure on the amount of customs duty payable. Since payment of custom duty is not due in the current case, the question of regularity does not arise in respect of custom duty.

Interest and rent that are required to be incurred u/s 61 of the Customs Act, 1962 would come under other statutory dues and the auditor would have to examine & comment upon the regularity of the company in depositing such interest and rent.

- (iii) In relation to income tax assessment order received by the company along with demand notice, (iii) the auditor is required to check whether time limit for filing the appeal or application for rectification of mistake has expired or not. In case such time limit has

expired, disputed amount will become undisputed statutory due (as mere representation to the concerned Department shall not be treated as a dispute).

Auditor is also required to ascertain whether such dues are outstanding for a period of more than 6 months from the date they became payable. Accordingly, after ensuring the above, if the statutory dues are outstanding for more than 6 months the auditor is required to report the same under clause (vii) (a) of CARO.

However, in case the statutory dues are not outstanding for a period of more than 6 months from the date they became payable the auditor is not required to report the same under CARO.

- (iv) If the method as stated in the question is consistently followed and the difference between the total dues and the lumpsum deposit is not significant, it need not be considered that dues have not been regularly deposited and no unfavourable comment is necessary. Thus, no reporting is required for the same under CARO.

Q.63. Mr. Arjun was appointed as the engagement partner on behalf of Bhism & Co., a Chartered Accountant Firm, for conducting statutory audit assignment of Sinwar Ltd., unlisted public company. Mr. Brijesh, one of the senior engagement team members, was given the responsibility to audit the matters as per the requirements of CARO, 2020 and in that connection, he made the following observations, that may be relevant for reporting as per the said Order:

Sr. No.	Observations
(a)	One of the Plant and Equipment taken on a lease ('right of use' asset) by Sinwar Ltd. was revalued based on the valuation by a registered valuer and the net carrying value of Plant and Equipment in aggregate was changed from ₹ 4 crore to ₹ 4.45 crore.
(b)	During the year under consideration, cash credit limit of ₹ 5.5 crore was sanctioned to Sinwar Ltd. by DMC Bank based on the security of current assets which was reduced to ₹ 4.5 crore after 6 months. In this connection, quarterly returns have been filed by the company with the DMC bank which are in agreement with Books of Account.

You are required to examine the contention of Mr. Brijesh regarding reporting of the above observations in accordance with CARO, 2020. [RTP-May 22]

Ans: Reporting requirements under CARO, 2020:

- (a) As per Para 3(i) (d) of CARO, 2020, the auditor is required to report whether the company has revalued its Property, Plant and Equipment (including Right of Use assets) or intangible assets or both during the year and, if so, whether the revaluation is based on the valuation by a Registered Valuer; specify the amount of change, if the change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment or intangible assets.

In the given situation, Sinwar Ltd. has revalued one of the Plant and Equipment taken on a lease ('right of use' asset) based on the valuation by a registered valuer. The amount of change in the value of such Plant and Equipment is ₹ 45 lakh. As the net carrying value of Plant and Equipment in aggregate was changed from ₹ 4 crore to ₹ 4.45 crore i.e. change was 10% or more.

Conclusion: Auditor is required to report the amount of change of ₹ 45 lakh in accordance with Para 3(i) (d) of CARO, 2020.

- (b) As per Para 3(ii) (b) of CARO, 2020, the auditor is required to report whether during any point of time of the year, the company has been sanctioned working capital limits in excess of ₹ 5 crores, in aggregate, from banks or financial institutions on the basis of security of current assets; whether the quarterly returns or statements filed by the company with such banks or financial institutions are in agreement with the books of account of the Company, if not, give details.

In the given situation, Sinwar Ltd. has been sanctioned a cash credit limit of ₹ 5.5 crores by DMC Bank during the year under consideration, which is exceeding the prescribed limit of ₹ 5 crores based on the security of current assets. Further, quarterly returns have also been filed by the company with the DMC bank in this connection which is in agreement with Books of Account.

Conclusion: Auditor is required to report the working limit sanctioned to Sinwar Ltd. and disagreement of quarterly statements with the books of account.

7.10 - Other Comprehensive Questions

Q.64. The audit report of Kolsi (P) Ltd. for F.Y. 2022-23 was issued by Bishnoi & Co. on 25th July, 2023. However, a case was filed against Kolsi (P) Ltd. on 4th August, 2023, with the Civil Court, with respect to an incident caused in its factory on 17th January, 2023, the outcome of which may result in paying heavy penalty by Kolsi (P) Ltd.

Mr. Raj Bishnoi, the partner of Bishnoi & Co., discussed the said matter with the management and it was determined to amend the financial statements for F.Y. 2022-23. Further, Mr. Raj inquired how the management intended to address the said matter in the financial statements to which he was told that the said matter was going to be disclosed as a “Contingent Liability for a Court case” to the foot note in the balance sheet with no additional disclosures.

The management told Mr. Raj that such disclosure was enough as he would further going a description of the said court case and its outcome in the ‘Emphasis of Matter’ paragraph in his amended audit report.

In the context of aforesaid case scenario, please answer the following questions:

- (1) Whether Mr. Raj on behalf of Bishnoi & Co., has properly adhered to his responsibilities in accordance with SA 560, on becoming aware of the court case filed against Kolsi (P) Ltd.?
- (2) Whether the contention of management of Kolsi (P) Ltd. is valid with respect to the disclosure of the court case in the financial statements? [RTP-Nov. 21]

Ans: Auditor’s Responsibilities as per SA 560:

- As per SA 560, ‘Subsequent Events’, auditor has no obligation to perform any audit procedures regarding F.S. after date of auditor’s report. However, when, after date of auditor’s report but before the date the F.S. issued, a fact becomes known to auditor that, had it been known to auditor at date of the auditor’s report, may have caused him to amend auditor’s report, the auditor shall:

- (1) Discuss the matter with management and, where appropriate, TCWG.
- (2) Determine whether the financial statements need amendment and, if so.
- (3) Inquire how management intends to address the matter in the financial statements.

- In the given case, on becoming aware of the court case filed against the company, Mr. Raj discussed the said matter with the management and it was determined to amend the F.S. Also, he inquired how the management intended to address the said matter in the F.S.
- However, if management does not take the necessary steps to ensure that anyone in receipt of the previously issued F.S. is informed of the situation and does not amend the F.S. in circumstances, auditor shall notify management and TCWG that the auditor will seek to prevent future reliance on the auditor's report. If despite such notification management or TCWG do not take these necessary steps, auditor shall take appropriate action to seek to prevent reliance on the auditor's report in accordance with SA 560.

Disclosure of the court case in the financial statements

As per SA 706, 'Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report', an Emphasis of Matter paragraph is not a substitute for:

- (a) A modified opinion in accordance with SA 705 (Revised) when required by the a specific audit engagement; circumstances of
- (b) Disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation; or
- (c) Reporting in accordance with SA 570 when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern.

In the given case, management of company has presumed that as the auditor was going to provide a description of the said court case and its outcome in the 'EOM paragraph in his amended audit report, there was no further need for it to provide additional disclosures about the court case in the F.S.

Conclusion: Contention of management is not valid as 'Emphasis of Matter' paragraph cannot be used as a substitute for disclosures required to be made in the financial statements as per the applicable financial reporting framework or that is otherwise necessary to achieve fair presentation, which is the responsibility of the management.

PART- II MULTIPLE CHOICE QUESTIONS

1. During the conduct of audit, it was found that the management has intentionally made material misstatements in the several items of the financial statements to deceive the users of the financial statements, to reduce the pressures of meeting market expectations and to increase the reputation of the company. What would be the implications on the auditor's report if no adjustments are made to the financial statements regarding the misstatements made by the management?
 - (a) The auditor would issue a qualified audit opinion stating that 'except for' these matters the financial statements are fairly presented. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
 - (b) The auditor would issue an adverse audit opinion stating that 'except for these matters the financial statements are fairly presented. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
 - (c) The auditor would issue an adverse audit opinion stating that financial statements 'do not

give a true and fair view'. The auditor should also include a 'Basis for Adverse Opinion' paragraph below the opinion paragraph.

- (d) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true & fair view'. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.

2. While auditing the complete set of consolidated financial statements of Tulips Ltd., a listed company, using a fair presentation framework, M/s Pintu & Co., a Chartered Accountant firm, discovered that the consolidated financial statements are materially misstated due to the non-consolidation of a subsidiary. The material misstatement is deemed to be pervasive to the consolidated financial statements. The effects of the misstatement on the consolidated financial statements have not been determined because it was not practicable to do so.

Thus, M/s Pintu & Co. decided to provide an adverse opinion for the same and further determined that, there are no key audit matters other than the matter to be described in the Basis for Adverse Opinion section. Comment whether M/s Pintu & Co. needs to report under SA 701 'Communicating Key Audit Matters in the Independent Auditor's Report'?

- (a) M/s Pintu & Co. have the option to follow SA 701, thus, need not to report any key audit matters.
- (b) SA 701 is mandatory in the case of audit of listed entities, however, as there are no key audit matters other than the matter to be described in the Basis for Adverse Opinion section, no 'Key Audit Matters' para needs to be stated under audit report.
- (c) SA 701 is mandatory in the case of audit of listed entities, however, as there are no key audit matters other than the matter to be described in the Basis for Adverse Opinion section, M/s Pintu & Co. shall state, under 'Key Audit Matters' para, that 'except for the matter described in Basis for Adverse Opinion section, we have determined that there are no other key audit matters to communicate in our report.'
- (d) M/s Pintu & Co. is under compulsion to follow SA 701 as the audit is of a listed company and shall report under 'Key Audit Matters' para the matter same as stated in 'Adverse Opinion' para regarding non-consolidation of a subsidiary.

3. If the prior period financial statements were not audited, the auditor shall state the same in.

- (a) Key audit matter section.
- (b) Emphasis of matter paragraph.
- (c) Going concern paragraph.
- (d) Other matter paragraph.

4. In case of audits of listed entities, other information section is required in auditor's report when at the date of auditor's report:

- (a) Auditor has obtained some or all of the other information.
- (b) Auditor has obtained all of the other information.
- (c) Auditor has obtained or expects to obtain the other information.
- (d) Auditor has obtained some of the other information.

5. In case of audits of unlisted corporate entities, other information section is required in auditor's report when at the date of auditor's report:

- (a) Auditor has obtained some or all of the other information.
- (b) Auditor has obtained all of the other information.
- (c) Auditor has obtained or expects to obtain the other information.
- (d) Auditor has obtained some of the other information.

6. VBN & Associates, chartered accountants are Statutory auditors of Gold Ltd. for the year ended 31st March, 2024. While conducting audit for the year, the auditor have come to know that the fraud amounting to ₹ 2 crore was done by one of the employees. Under Sec. 143(12) of Companies Act, 2013, you are required to suggest whether as a statutory auditor, VBN & Associates is required:

- (a) To report fraud to Audit Committee/Board of Directors of Gold Ltd. and in Auditor's Report.
- (b) To report fraud to shareholders of Gold Ltd. and no further reporting.
- (c) To report fraud only in Auditor's Report.
- (d) To report fraud to Central Government and in Auditor's Report.

7. SKJ Private Ltd. has annual turnover of INR 200 crore and profits of INR 25 crore. Company is engaged in the business of textiles and has fairly stable operations over the years. There has not been much growth in the company in the last few years despite the attempts of the management. Currently the management is more focused towards cost cutting and has been considering all the options to achieve that objective.

Statutory auditors of company have been auditing the F.S. for the last 3 years and have issued clean reports over these years.

During financial year ended 31 March 2023, management got a large project from a new customer which resulted in significant increase in the turnover of the company. However, the profitability of the company did not improve much because the margins in the contract were not high.

Statutory auditors during the course of their audit of F.S. for the year ended 31 March 2023 (their fourth year of audit) did not agree with the revenue recognition criteria followed by the company. Since the matter was significant, lot of discussions/ debates happened between the auditor and the management. But it was finally agreed that the auditors would qualify their audit report.

Auditors wanted that the management should explain this matter in detail in the notes to accounts to the financial statement over which the auditors are qualifying the audit report. However, the management had a different view. Management said that if the auditor is qualifying his report then why should the management also highlight that matter in the financial statement and hence refused to include any note for the same.

On account of the conflict, since audit is not getting concluded. You are required to suggest how the matter get resolved?

- (a) In the given situation, if the management does not agree to give a note in the financial statements then the auditor should not hold the audit report. However, in such a case, the auditor would need to give disclaimer of opinion in his report instead of qualification.
- (b) The argument of the management seems correct. Auditor cannot do both the things i.e. to qualify and then also get that highlighted in the financial statements. That note would not be beneficial for the users of the financial statements.

- (c) In case of such matters related to revenue recognition, it is always better to give detailed explanation in the notes to accounts to the financial statements. If the explanation is satisfactory then the auditor should also consider giving emphasis of matter instead of qualification.
- (d) The requirement of the auditor is beneficial for the company because by giving an explanation of the matter, on which auditor has given a qualification, in the notes to accounts, the management would be able to explain their perspective/ point of view to the users of the financial statements. In that case, auditor while giving the qualification can give reference to the notes to accounts otherwise the entire matter would form part of the audit report. However, the auditor should not hold his report if the management does not want to give any explanation in the notes to accounts.

8. M/s ABC & Associates, a firm of chartered accountants was appointed as statutory auditors by IRCON Ltd. for the audit of their financial statements for the financial year 2022-23. During the course of audit, the auditors noticed a fraud of ₹ 1.36 Crores done by an officer of the company. The officer sanctioned and made the payment to fake vendors for purchase of fixed assets; however, the assets were not entered in the Fixed Assets Register. The auditor reported the fraud in his audit report to the shareholders of the company presented in the AGM, but did not mentioned the name of the parties involved.

The Board of Directors of the company are complaining against the auditor as he has not complied with his duty to report fraud as per Sec. 143(12) of the Companies Act, 2013. Advise on the duty of the auditor as per Companies Act in relation to reporting of the fraud done by officers or employees of the company?

- (a) If the auditor has reason to believe that a fraud has been conducted by the officers or employees of the company, the auditor shall report the matter to the Central Government immediately.
- (b) If the amount of fraud is more than 100 lacs; the auditor should have reported the matter within 2 days of his knowledge to the Board of Directors/Audit committee of the company seeking their reply or observations within 45 days. After completion of 45 days the auditor should forward his report to the Central Government along with the reply if any received from Board/Audit Committee.
- (c) The auditor's duty is restricted to reporting the fraud to shareholders and he is not required to report the matter to Board of Directors/Audit Committee/Central Government.
- (d) The auditor can submit his report on fraud to shareholders but is required to mention the name of the parties involved in fraud, as per Section 143(12) of the Companies Act, 2013. [MTP-April-19]

9. ABC Pvt. Ltd. had turnover of ₹ 39 crores as at 31 March 2023. The Company had taken a loan of ₹ 39 crores from various banks and financial institutions during the year ended 31 March 2023. These loans were paid by the Company before 31 March 2023. The Company is of the view that the auditors' reporting on adequacy & operating effectiveness of internal financial controls (IFC) u/s 143(3)(i) of the Companies Act, 2013 would not be required. The auditors of the Company have a different view. Choose the correct answer?

- (a) The turnover of ABC Pvt. Ltd. is below required threshold and hence reporting on adequacy and operating effectiveness of IFC will not be applicable.
- (b) The turnover of ABC Pvt. Ltd. is below required threshold and loan amount was fully paid before year end i.e. 31 March 2023. Hence reporting on adequacy and operating effectiveness of IFC will not be applicable.
- (c) The borrowings of the company are above threshold, hence reporting on adequacy & operating effectiveness of IFC would be applicable.
- (d) The turnover of ABC Pvt. Ltd. is below required threshold & loans were repaid before year end i.e. 31 March 2023, applicability of IFC becomes optional. [RTP-May 19]

10. KJA Ltd. is in the business of manufacturing of tiles and sanitaryware. The company has a large inventory every year. Annual turnover of the company is INR 3000 crores. The company has 7 plants across India. The management of the company carries out physical verification of inventory every year at the time of reporting date. During the year ended 31 March 2023, it was found by the management that the inventory sheets of 31 March 2022 did not include five pages containing details of inventory worth INR 24.5 crores. Management has included this inventory in the valuation of inventory as of 31 March 2023. Management has also explained that considering the size of the company this may happen at times as the inventory is huge and lying at various locations. Moreover, the amount of the inventory is insignificant if considered as a percentage of revenue or inventory. State how you will deal with this matter as an auditor in the accounts of the company (towards substantive audit procedures and excluding the impact on auditor's assessment under Internal Financial Control Framework) for the year ended 31 March 2023.

- (a) Since the matter is not relevant/material to current period figures, no reporting in respect of this matter would be required in the auditor's report for the year ended 31 March 2023.
- (b) Management should restate the financials to adjust the error. Otherwise auditor may modify his opinion on current year's financial statements considering the materiality.
- (c) Considering the matter is not relevant/material to current period figures, the management may include a note in the financial statements and basis that no reporting in respect of this matter would be required in the auditor's report for the year ended 31 March 2023.
- (d) Include an emphasis of matter because of the effects or possible effects of the error in the auditor's report for the year ended 31 March 2023. [RTP-May 19]

11. While conducting the current year audit of Finolex Ltd, the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements. This misstatement was related to recognition of research and development expenditure. The provisions of Ind AS 38 Intangible Assets relating to capitalisation of development expenditure was not applied properly. On this, unmodified opinion had been previously issued. The current auditor verified that the misstatement had not been dealt with as required under Ind AS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Accordingly, the current auditor will:

- (a) Express a qualified or an adverse opinion in the auditor's report on the current period financial statements modified with respect to the corresponding figures included therein.

- (b) Express an unmodified opinion in the auditor's report on the current period financial statements since it was related to the prior year.
- (c) Express a qualified opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.
- (d) Express an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.

[MTP-Oct. 19]

12. ABC Ltd. is a listed company engaged in the business of software and is one of the largest company operating in this sector in India. The company's annual turnover is ₹ 10,000 crores with profits of ₹ 2,000 crores.

During the course of the audit, the audit team spends significant time on audit of revenue - be it planning, execution or conclusion. The audit team for this engagement comprises of approx. 70-80 members. The company's contracts with its various customers are quite complicated and different. The efforts towards audit of revenue also involve significant involvement of senior members of the audit team including the audit partner.

After completion of audit for the year ended 31 March 2023, the audit partner was discussing significant matters with the management wherein he also communicated to the management that he plans to include revenue recognition as key audit matter in his audit report. The management was quite surprised to understand this from the auditor and did not agree with revenue recognition to be shown as key audit matter in the audit report. As per the management, the auditors didn't have any modification and such a matter getting reported as key audit matter would not go down well with various stakeholders and would significantly impact the financial positions of the company in the market. The auditors were not able to convince the management in respect of this point and there was a difference of opinion.

You are requested to give your view in respect of this matter.

- (a) The concern of the management is valid. For such a large sized company, such type of matter getting reported as key audit matter is not appropriate.
- (b) The assessment of the auditor is valid. Such a matter qualifies to be a key audit matter and hence should be reported accordingly by the auditor in his audit report.
- (c) Reporting revenue as key audit matter when the auditor does not have observation in that area leading to any modification in his report, would not be appropriate.
- (d) This being the first year of reporting of key audit matters, the auditor should take a soft stand and should avoid reporting such controversial matters in his report. [RTP-Nov. 19]

13. A Ltd. is engaged in the business of providing management consultancy services and have been in operation for the last 15 years. The company's financial reporting process is very good and its statutory auditors always issued clean report on the audit of the financial statements of the company. The auditors were required to be rotated due to mandatory audit rotation requirement of the Companies Act, 2013.

MN & Associates, a firm of Chartered Accountants, was appointed as the new auditor of the company for a term of 5 years and have to start their first audit for the financial year ended 31 March 2023. The auditors had a detailed and clear discussion with the management that they will perform their audit procedures in respect of opening balances along with the audit procedures for the financial year ended 31 March 2023. Management agreed with that & the

audit was completed as per the plan.

The auditors did not have any significant observations and hence they communicated to the management that their report will be clean. Management was quite happy with this & also requested the auditors to share draft report before issuing the final report.

In the draft audit report, all the particulars were fine except 'other matters paragraph' wherein the auditors gave a reference that the financial statements for the comparative year ended 31 March 2022 was audited by another auditor. Management asked the audit team to remove this paragraph as the auditors had performed all the audit procedures on opening balances also. But the auditors did not agree with the management.

Please advise the auditor or the management whoever is incorrect with the right guidance.

- (a) Contention of the management is valid. After performing all the audit procedures, an auditor should not pass on the responsibility to another auditor by including such references in his audit report.
- (b) Any auditor has two options, either to perform audit procedures on opening balances or given such reference of another auditor in his report. Auditor cannot mix up the things like this auditor has done. It is completely unprofessional.
- (c) In the given situation even if the auditor wants to give such reference, the management and the auditor should have taken approval from the previous auditor at the time of appointment of new auditor. In this case, it cannot be done.
- (d) The report of the auditor is absolutely correct and is in line with the auditing standards. An auditor is required to include such reference in his report as per the requirements of the auditing standard. [RTP-Nov. 19]

14. The auditor shall express opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements

- (a) Adverse
- (b) Qualified
- (c) Disclaimer of opinion
- (d) Clean

[MTP-May 20]

15. Before concluding the audit, there was a difference of opinion between the audit committee and the auditors as to which among the following are the areas which the auditor should take into account to determine "Key Audit Matter" as per SA 701:

- (I) The effect on audit of significant transactions that took place in the FY.
- (II) Areas of high risk as assessed and reported by management's expert.
- (III) Significant auditor judgment relating to areas in the financials that involved significant management judgment.

As per SA 701- Communicating Key audit matters in the Independent auditor's Report, which among the above-mentioned areas should CA & Co. take into account to determine "Key Audit Matter"?

- (a) (I) & (III)
- (b) (II) only
- (c) (I) & (II)
- (d) (I), (II) & (III)

[RTP-Nov. 20]

16. NIC Chartered Accountants was appointed as statutory auditors by PNG Ltd. for the audit of their financial statements. During the course of audit, the auditors noticed a fraud of ₹ 101 lac committed by an officer of the Company. The officer sanctioned and made the payment to fake vendors for purchase of fixed assets; however, the assets were not entered in the Fixed Assets Register. The auditor reported the fraud in his audit report to the shareholders of the Company presented in the Annual General Meeting, but did not mention the name of the parties involved. The Board of Directors of the Company asked ICAI to take necessary action against the auditor as he did not comply with his duty to report fraud as per Section 143(12) of the Companies Act, 2013. What is the duty of the auditor as per the Companies Act, 2013 in reporting the fraud committed by officers/ employees of the Company?

- (a) As per the Companies Act, 2013, since the amount of fraud is more than ₹ 100 lac; auditor should have reported the matter within 2 days of his knowledge to the BOD/Audit committee of the Company seeking their reply or observations within 45 days. After completion of 45 days, auditor should forward his report to the C.G. along with the reply, if any, received from Board/Audit Committee.
 - (b) As per the Companies Act, 2013, during the course of audit if the auditor has reason to believe that a fraud has been committed by the officers or employees of the Company, the auditor shall report the matter to the Central Government immediately.
 - (c) The auditor's duty is restricted to reporting the fraud to shareholders and he is not required to report the matter to the Board of Directors/Audit Committee/Central Government.
 - (d) The auditor can submit his report on fraud to shareholders but is required to mention the name of the parties involved in fraud, as per Section 143(12) of the Companies Act, 2013.
- [RTP-Nov. 20]

17. CA Ram identified that there was a misstatement last year and the same is still not corrected. Although unmodified audit report was issued last year by CA Ram. Guide CA Ram on the audit opinion considering the fact that the last year's misstatement has been identified in the current year and unmodified opinion was issued in the last year?

- (a) In accordance with SA 710, CA Ram should give unmodified opinion, but include other matters paragraph in the audit report as last year's profit is being reflected in reserve & surplus.
- (b) In accordance with SA 710, CA Ram should seek legal opinion.
- (c) In accordance with SA 710, CA Ram should qualify current period audit report with respect to corresponding figures only.
- (d) In accordance with SA 710, CA Ram should give unmodified opinion, but last period's modified opinion should be highlighted in Emphasis of matter paragraph.

[MTP-March 21]

18. CA Kamal is the statutory auditor of Autocover Ltd. for the FY 2023-24. The company is engaged in the business of manufacture of car accessories. CA Kamal noticed that the inventories of the company amounting to ₹ 46 crores (equal to 25% of the total assets of the company) at the end of the year do not exist. Also, sales amounting to ₹ 33 crores (equal to 10% of the total sales during the year) have not actually occurred. CA Kamal noticed both the

material discrepancies just before the finalisation of the audit report for the year ending 31.03.2024. CA. Kamal considers that the above misstatement would distort the true and fair view to a greater extent.

What is correct course of action that CA Kamal should consider in such a situation?

- (a) CA Kamal should consider withdrawing from the audit engagement or issuing a disclaimer of opinion for the FY 2023-24.
- (b) CA Kamal should consider issuing an adverse opinion and mentioning both the material discrepancies in the basis for adverse opinion paragraph of the auditor's report.
- (c) CA Kamal should ask the management to explain both the discrepancies in the notes to accounts and he himself should highlight the matter in the Key Audit matter paragraph of the auditor's report.
- (d) CA Kamal should give a qualified opinion along with the specific mention of the matters in the Emphasis of matter paragraph in the auditor's report along with appropriate disclosure in the notes to accounts to be made by the management of Autocover Ltd.

[MTP-March 21]

19. Preparing the financial statements in accordance with the applicable financial reporting framework is the responsibility of the management of ABC Ltd. Which of the following is correct in regard to the disclosure of such management responsibility?

- (a) This is implied responsibility of management and is presumed in an audit of financial statements and therefore need not be specifically mentioned anywhere.
- (b) The management may undertake to accept such responsibility through an engagement letter itself.
- (c) The auditor's report should describe the management responsibility in a section with heading "responsibility of management for financial statements".
- (d) The auditor's report should refer to the responsibility of auditors and not that of the management as the same is obvious.

[MTP-March 21]

20. During the conduct of audit, it was found that the management has intentionally made material misstatements in the several items of the financial statements to deceive the users of the financial statements, to reduce the pressures of meeting market expectations and to increase the reputation of the company. What would be the implications on the auditor's report if no adjustments are made to the financial statements regarding the misstatements made by the management?

- (a) The auditor would issue a qualified audit opinion stating that 'except for' these matters the financial statements are fairly presented. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
- (b) The auditor would issue an adverse audit opinion stating that 'except for' these matters the financial statements are fairly presented. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.
- (c) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true and fair view'. The auditor should also include a 'Basis for Adverse Opinion' paragraph below the opinion paragraph.
- (d) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true (and fair view'. The auditor should also include a 'Basis for Qualified Opinion' paragraph below the opinion paragraph.

[MTP-April 21]

21. While verifying the salary expense of employees, the auditor has been asked to rely on the values as per SAP software and some hard copy reports and documents as the HRMS package (source software) has become corrupt during the year and the management is not having any data backup.

How should the auditor deal with this issue?

- (a) The auditor should issue a disclaimer of opinion as records are destroyed and he is unable to obtain sufficient appropriate audit evidence.
- (b) The auditor should perform alternative procedures to obtain sufficient & appropriate audit evidence before disclaiming the opinion.
- (c) The auditor should issue an adverse opinion stating that it is deficiency in internal controls.
- (d) The auditor can rely on the SAP data & there is no need for qualification of report.

[MTP-April 21, April 22]

22. Description of each key audit matter in the “key audit matters section” needs to cover except following aspects:

- (a) Reference to related disclosures, if any, in the financial statements.
- (b) Explanation on the matter given by management
- (c) How the matter was addressed in the audit.
- (d) Why the matter was considered to be one of most significance in the audit and therefore determined to be a key audit matter.

[MTP-Nov. 21]

23. M/s Brahmi and Associates have been appointed as the statutory auditor of Prompton Leaves Limited, a manufacturer of gas geysers for the FY 2022-23. During the course of audit, the auditor found that two customer complaints have been filed against the company in the FY 2022-23, for the use of sub-standard pipes and wires in manufacture of gas geysers. The gas geyser blasted at high temperature leading to severe injuries to the family of complainant along with damage to their property. They have sought a demand of rupees 10 crore. However, the lawyer of Prompton Leaves Limited believes that such claim is unsustainable as the incident occurred due to short circuit at both the complainants place. The management of Prompton Leaves Limited accordingly did not include any reference to the litigation in the financial statements. The auditor obtained legal advice from some independent lawyer according to whom the outcome of the case is not ascertainable as of now.

- (a) The statutory auditor should give an unqualified opinion.
- (b) The statutory auditor should give an unqualified opinion with Emphasis of Matter paragraph.
- (c) The statutory auditor should withdraw from the audit engagement.
- (d) The statutory auditor should give a qualified opinion.

24. As per SA 701- Communicating Key audit matters in the Independent auditor’s Report, which among the following areas should CA & Co. take into account to determine “Key Audit Matter”?

- (i) The effect on audit of significant transactions that took place in the financial year.
- (ii) Areas of high risk as assessed and reported by management’s expert.

(iii) Significant auditor judgment relating to areas in the financials that involved significant management judgment.

- (a) (i) & (ii)
- (b) (ii) only
- (c) (i) & (iii)
- (d) (i), (ii) & (iii)

25. Moon Ltd. is a company engaged in the manufacture of iron and steel bars. VP & Associates are the statutory auditors of Moon Ltd. for the FY 2022-23. During the course of audit, CA Vikash, the engagement partner, found that the Company's financing arrangements have expired, and the amount outstanding was payable on March 31, 2023. The Company has been unable to re-negotiate or obtain replacement financing and is considering filing for bankruptcy. These events indicate a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business. The financial statements (and notes thereto) do not disclose this fact. What opinion should CA Vikash express in the case of Moon Ltd.?

- (a) Unmodified opinion.
- (b) Qualified opinion.
- (c) Adverse opinion.
- (d) Disclaimer of opinion.

[RTP-May 22]

MCQs on CARO, 2020

26. One of your team members has recently qualified as a chartered accountant and joined your team to audit a portfolio of audit clients who are private companies. One of the clients Surrey Pvt. Ltd. is a hotel in the small town near Jaipur. The revenue generated for the current year ended is ₹ 10.5 crores and the entity is not a holding or subsidiary of any public company. The owner of the business Mr. Hazelwood runs this family business from last 10 years. Your team member is keen to know whether Surrey Pvt. Ltd. is required to comment on the matter prescribed under CARO 2020. Which of your explanations to him are correct?

- (a) The entity's revenue exceeds ₹ 10 crores. Hence, no need to comment on the matter prescribed under CARO, 2020.
- (b) The entity is not a holding or subsidiary of any public company, hence no need to comment on the matter prescribed under CARO, 2020
- (c) The entity's revenue for the year is ₹ 10.5 cr. which exceed the limit of ₹ 10 cr. Hence, the entity has to provide the comment on the matter prescribed under CARO, 2020.
- (d) The entity is not a holding or subsidiary of any public company, hence there is a need to comment on the matter prescribed under CARO, 2020. [MTP-March 19]

27. Kinfin Private Limited had taken overdrafts from three banks (Bank A, Bank B and Bank C) with a limit of ₹ 40 lacs each against the security of fixed deposit it had with those banks & an unsecured overdraft from a financial institution (Financial Institution X) of ₹ 36 lacs. As on 30th October 2022, the management used the overdraft fully of the A & C bank to the tune of ₹ 40 lacs each. However, the overdraft of second bank (Bank B) was not used until 31st December, 2022. On 31st December, 2022, Management took overdraft of B bank &

very next day management paid the overdraft of C bank as the rate of interest charged by Bank C on overdraft facility was 15% whereas, the rate of interest charged by Bank B was 12%. As at 31st March 2023 only overdraft of Bank A and Bank B were used fully, overdrafts of Bank C and Financial Institution X were unused. The paid-up capital and reserves of the company as at that date was 85 lacs and its revenue for the financial year ended on 31st March 2023 was ₹ 8.95 crores. The management of the company is of the opinion that CARO, 2020 is not applicable to it because turnover and paid-up capital were within the limits prescribed. With respect to the loans, management was of the view that the total outstanding as at 31 March 2023 is less than the prescribed limit. The company further contended that loan limit is to be reckoned per bank or financial institution and not cumulatively. Comment.

- (a) The CARO, 2020 is applicable to the company as the turnover of the company exceeds the prescribed limit.
- (b) The CARO, 2020 is not applicable to the company as the turnover of the company does not exceeds the prescribed limit.
- (c) The CARO, 2020 is not applicable to the company as the borrowing of the company does not exceeds the prescribed limit.
- (d) The CARO, 2020 is applicable to the company as the borrowing of the company exceeds the prescribed limit. [MTP-Nov. 21]

28. While reporting under clause (ii) of Paragraph 3 of CARO, 2020, which of the following is correct:

- (a) The 10% threshold for reporting must be applied on a gross basis before adjusting excesses and shortages within the class of an inventory and must be based on value for each class of Inventory.
- (b) The 10% threshold for reporting must be applied on a gross basis before adjusting excesses and shortages within the class of an inventory and must be based on value for all classes of Inventory.
- (c) The 10% threshold for reporting must be applied on a net basis after adjusting excesses and shortages within the class of an inventory and must be based on value for each class of Inventory.
- (d) The 10% threshold for reporting must be applied on a net basis after adjusting excesses and shortages within the class of an inventory and must be based on value for all classes of Inventory. [MTP-April 22]

29. KFintech Pvt Ltd was having paid-up share capital and reserves of ₹ 150 lakh including paid-up share capital of ₹ 90 lakh at the end of FY 21-22. During FY 22-23, KFintech borrowed ₹ 80 Lakh from Bank A and ₹ 140 Lakh from Bank B. The amount borrowed from Bank B was repaid during the same FY. For FY 21-22 the turnover of the company was ₹ 1,850 lakh. Select the appropriate option with respect to the applicability of CARO 2020:

- (a) CARO, 2020 will be applicable as the paid-up capital and reserves exceeding the limit specified in the Order i.e., one crore rupees.
- (b) CARO, 2020 will be applicable as the company has paid-up capital and reserves exceeding the limit specified in the Order i.e., one crore rupees and have total borrowings exceeding one crore rupees from any bank or financial institution at any point of time during the financial year.

- (c) CARO, 2020 will not be applicable as the company repaid the amount borrowed from bank B before the end of the financial year and hence, the borrowings do not exceed the limit specified in the Order.
- (d) CARO, 2020 will not be applicable as the company will fall under the exemption provided in the order for Small Company as per section 2(85) of the Companies Act 2013. [MTP-Sep. 22]

30. CA. A, the auditor of XYZ Limited resigned from the post due to his personal reasons. CA. B was appointed as the subsequent auditor of the company by the Board of Directors. During the conclusion of the audit for the FY, should CA. B mention about CA. A's resignation in the Companies (Auditor's Report) Order 2020?

- (a) Yes. As per clause (xviii) of para 3 of CARO, CA. B should report the resignation of CA. A and state if he has taken into consideration the issues or objections raised by CA. A.
- (b) No. Since the resignation of CA. A is due to his own personal reason, the same need not be reported under CARO.
- (c) Yes. As per clause (xxi) of para 1 of CARO, CA. B should report the resignation of CA. A and state if he has taken into consideration the issues or objections raised by CA. A.
- (d) No. CARO 2020 does not state any requirements to report resignation of auditor. However, the same needs to be mentioned by CA. B in the Audit Report under Other Matter Paragraph, as per SA 706. [MTP-Oct. 22]

31. While auditing with respect to compliance with CARO, 2020, Mr. Omprakash, for additional reporting purpose, observed the following, relevant to Para 3(vii) of CARO, 2020:

Statutory Dues	Undisputed Amount (₹ in lakh)	Date Payable	Date Paid
Provident Fund	1.50	24 September, 2022	27 March, 2023
GST	2.45	23 October, 2022	24 April, 2023
Customs Duty	0.65	20 September, 2022	10 April, 2023
Income Tax Demand for A.Y. 20-21	0.55	23 October, 2022	Not paid till date

Also, a representation was made to GST Department for waiving a penalty of 1 lakh for late payment of GST demand. What total amount of statutory dues need to be reported by Mr. Omprakash as per Para 3 of CARO?

- (a) ₹ 3.10 lakh.
- (b) ₹ 0.65 lakh.
- (c) ₹ 3.65 lakh.
- (d) ₹ 2.70 lakh.

Answer Key

1. (c) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true and fair view'. The auditor should also include a 'Basis for Adverse Opinion' paragraph below the opinion paragraph.
2. (c) SA 701 is mandatory in the case of audit of listed entities, however, as there are no key

audit matters other than the matter to be described in the Basis for Adverse Opinion section, M/s Pintu & Co. shall state, under 'Key Audit Matters' para, that 'except for the matter described in the Basis for Adverse Opinion section, we have determined that there are no other key audit matters to communicate in our report.

3. (d) Other matter paragraph.
4. (c) Auditor has obtained or expects to obtain the other information.
5. (a) Auditor has obtained some or all of the other information.
6. (d) To report fraud to Central Government and in Auditor's Report.
7. (d) The requirement of the auditor is beneficial for the company because by giving an explanation of the matter, on which auditor has given a qualification, in the notes to accounts, the management would be able to explain their perspective/ point of view to the users of the financial statements. In that case, auditor while giving the qualification can give reference to the notes to accounts otherwise the entire matter would form part of the audit report. However, the auditor should not hold his report if the management does not want to give any explanation in the notes to accounts.
8. (b) If the amount of fraud is more than 100 lacs; the auditor should have reported the matter within 2 days of his knowledge to the Board of Directors/Audit committee of the company seeking their reply or observations within 45 days. After completion of 45 days the auditor should forward his report to the C.G. along with the reply if any received from Board/Audit Committee.
9. (c) The borrowings of the company are above threshold, hence reporting on adequacy & operating effectiveness of IFC would be applicable.
10. (b) Management should restate the financials to adjust the error. Otherwise, auditor may modify his opinion on current year's financial statements considering the materiality.
11. (a) Express a qualified or an adverse opinion in the auditor's report on the current period financial statements modified with respect to the corresponding figures included therein.
12. (b) The assessment of the auditor is valid. Such a matter qualifies to be a key audit matter and hence should be reported accordingly by the auditor in his audit report.
13. (d) The report of the auditor is absolutely correct and is in line with the auditing standards. An auditor is required to include such reference in his report as per the requirements of the auditing standard.
14. (a) Adverse
15. (a) (I) & (III)
16. (a) As per the Companies Act, 2013, since the amount of fraud is more than 100 lac; the auditor should have reported the matter within 2 days of his knowledge to the Board of Directors/Audit committee of the Company seeking their reply or observations within 45

days. After completion of 45 days, the auditor should forward his report to the Central Government along with the reply, if any, received from Board/ Audit Committee

17. (c) In accordance with SA 710, CA Ram should qualify current period audit report with respect to corresponding figures only.
18. (b) CA Kamal should consider issuing an adverse opinion and mentioning both the material discrepancies in the basis for adverse opinion paragraph of the auditor's report.
19. (c) The auditor's report should describe the management responsibility in a section with heading "responsibility of management for financial statements".
20. (c) The auditor would issue an adverse audit opinion stating that financial statements 'do not give a true and fair view'. The auditor should also include a 'Basis for Adverse Opinion' paragraph below the opinion paragraph.
21. (b) The auditor should perform alternative procedures to obtain sufficient and appropriate audit evidence before disclaiming the opinion.
22. (b) Explanation on the matter given by management.
23. (d) The statutory auditor should give a qualified opinion.
24. (c) (i) & (iii)
25. (c) Adverse opinion.
26. (c) The entity's revenue for the year is 10.5 Cr. which exceed the limit of 10 cr. Hence, the entity has to provide the comment on the matter prescribed under CARO, 2020.
27. (d) The CARO, 2020 is applicable to the company as the borrowing of the company exceeds the prescribed limit.
28. (c) The 10% threshold for reporting must be applied on a net basis after adjusting excesses and shortages within the class of an inventory and must be based on value for each class of Inventory.
29. (d) CARO, 2020 will not be applicable as the company will fall under the exemption provided in the Order for Small Company as per section 2(85) of the Companies Act, 2013.
30. (a) Yes. As per clause (xviii) of para 3 of CARO, CA. B should report the resignation of CA. A and state if he has taken into consideration the issues or objections raised by CA. A.
31. (b) ₹ 0.65 lakh.

PART- III INTEGRATED CASE SCENARIO

CA. Raghav is in midst of finalizing audit reports of five clients. On reviewing each file, it is noticed as under:

- (A) In case of a company engaged in business of selling of agricultural products which are outside ambit of GST, engagement team has found that substantial part of revenues of the company (about 80%) is generated through cash sales. However, there is no proper system and internal control to verify accuracy of revenues generated through cash sales. Therefore, team has been unable to verify such revenues generated through cash sales.
- (B) TS Limited has been dragged to court by BS Limited for stealing its trade secrets using cyber theft and filed a claim for ₹ 50 crore. On reviewing audit file of TS Limited, CA Raghav finds that legal opinion of company's standing counsel is ambiguous. There are precedent case laws both in favour and against on such issue. The financial statements of TS Limited are silent on this litigation matter.
- (C) It is noticed on review of audit file of a client that net profit before tax was ₹ 2 crore on a turnover of ₹100 crore. There is an export receivable from a chain of stores outstanding in financial statements of ₹ 3 crore for which there is no chance of recovery. The said chain of stores has gone bankrupt. There is also no hope of recovering money through ECGC (Export credit Guarantee Corporation) due to certain technical issues. Debt has not been written off by the client despite being communicated to client.
- (D) On reviewing file of a small finance bank, it was noticed that team has drafted following paragraph proposed to be included under Emphasis of Matter paragraph:
 "Concerns are raised regarding "Going Concern" status of the Bank. However, the Bank feels that it continues to remain a "Going Concern" in view of reasons stated in note 10.
 Our opinion is not modified in respect of this matter."
- (E) On reviewing file of a client, it is noticed that team was not informed about finished goods of Rs. 1 crore lying at a location taken on rent in February 2023. The said issue was flagged at time of reconciling inventories by the team. Hence, team could not attend physical inventory counting. The alternative procedures cannot be performed in absence of adequate records pertaining to above location. Total inventories reflected in financial statements is Rs. 8 crores. PBT of client is ₹ 10 crores.

- Q.1.** As regards description regarding revenues generated through cash sales of a company, which of the following statements is most appropriate in terms of SA 705?
- Qualified opinion will be issued and basis for qualified opinion will also be provided.
 - Adverse opinion will be issued and basis for adverse opinion will also be provided.
 - A disclaimer of opinion will be issued and basis for disclaimer of opinion will also be provided. Besides, statement in audit report will be changed from "financial statements have been audited" to "auditor was engaged to audit financial statements."
 - A disclaimer of opinion will be issued and basis for disclaimer of opinion will also be provided. Besides, statement in audit report will be changed from "financial statements have been audited" to "financial statements have not been audited."
- Q.2.** Considering litigation matter of TS Limited, which of the following statements is most appropriate in this regard?
- Unmodified opinion needs to be expressed by auditor.
 - It amounts to non-disclosure of a material contingent liability by the company. Adverse opinion needs to be expressed by auditor.
 - It amounts to non-disclosure of a material contingent liability by the company. Qualified opinion needs to be expressed by auditor.

(d) The company has not made a material provision resulting in material misstatement.
Adverse opinion

Q.3. Considering description of issue regarding non-recoverability of export receivable of Rs. 3 crore from a chain of stores, which type of opinion is appropriate to be issued in audit report?

- (a) Disclaimer of opinion
- (b) Unmodified opinion
- (c) Qualified opinion
- (d) Adverse opinion

Q.4. As regards matter of going concern in respect of a small finance Bank, which of the following statements is most appropriate?

- (a) The para drafted by team is proper and in accordance with SA 570 since auditor has decided to give unmodified opinion.
- (b) The para drafted by team is proper and in accordance with SA 570 since matter has been disclosed in notes to accounts by bank management.
- (c) Instead of giving emphasis of matter paragraph, separate paragraph on 'Material Uncertainty Related to Going Concern' in report should be given in accordance with SA 570.
- (d) Separate paragraph on 'Material Uncertainty Related to Going Concern' under the heading "Emphasis of matter" paragraph in report should be given in accordance with SA 570.

Q.5. Regarding issue of not informing team regarding inventory of finished goods lying at a location taken on rent in February 2023, which type of opinion is appropriate to be issued in case of this client?

- (a) Modified opinion
- (b) Qualified opinion
- (c) Unmodified opinion
- (d) Either Modified or Qualified opinion

Answer Key

- 1. (c) A disclaimer of opinion will be issued and basis for disclaimer of opinion will also be provided. Besides, statement in audit report will be changed from "financial statements have been audited" to "auditor was engaged to audit financial statements."
- 2. (c) It amounts to non-disclosure of a material contingent liability by the company. Qualified opinion needs to be expressed by auditor.
- 3. (d) Adverse opinion
- 4. (c) Instead of giving emphasis of matter paragraph, separate paragraph on 'Material Uncertainty Related to Going Concern' in report should be given in accordance with SA 570.
- 5. (b) Qualified opinion