

## PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS

### PART – I ACADEMIC UPDATE

#### RELEVANT AMENDMENTS FOR MAY 2023 EXAMINATION

#### (Legislative Amendments / Notifications / Circulars / Rules / Guidelines issued by Regulating Authority)

##### Chapter – 5: Company Audit

As per Companies (Specification of definition details) Amendment Rules, 2022 dated 15 September 2022 the following amendments were made in the Companies (Specification of definition details) Rules, 2014.

In rule 2, in sub-rule (1), for clause (t), the following clause shall be substituted, namely: -

*“(t) For the purposes of sub-clause (i) and sub-clause (ii) of clause (85) of section 2 of the Act, paid up capital and turnover of the small company shall not exceed rupees four crore and rupees forty crore respectively”.*

Hence, small company” means a company, other than a public company whose (i) paid-up share capital of does not exceed four crore rupees, and (ii) turnover as per profit and loss account for the immediately preceding financial year does not exceed forty crore rupees. [Page 5.77]

##### Chapter 7 Audit Committee and Corporate Governance (SEBI (LODR) Regulations, 2015)

1. Insertion of word At least before two-thirds in point no. 1. The Audit Committee shall have minimum three directors as members. **At least** two-thirds of the members of audit committee shall be independent directors, however, in case of a listed entity having outstanding SR (Superior Rights) equity shares, the audit committee shall only comprise of independent directors. (Refer para 4.1 Qualified and Independent Audit Committee [Regulation 18(1)]– Page no.7.4).
2. Deletion of information on **Statement of significant related party transactions (as defined by the Audit Committee), submitted by management under** mandatorily review by Audit Committee as per Part C(B) OF Schedule II. (Refer para 7 Review of Information by Audit Committee on Page no.7.13)
3. Deletion of point no. (iv) The auditor shall ensure that the Chairperson of the board of the top 500 listed entities is - (a) a non-executive director; (b) not related to the Managing Director or the Chief Executive Officer as per the definition of the term “relative” defined under the Companies Act, 2013. It may be noted that this provision shall not be applicable to the listed entities which do not have any identifiable promoters as per the shareholding pattern filed with stock exchanges. It may also be noted that the top 500 entities shall be determined on the basis of market capitalisation, as at the end of the immediate previous financial year. However, as per clause D of Schedule II, in Pat E The listed entity may appoint separate persons to the post of the Chairperson and the Managing Director or the Chief Executive Officer, such that the Chairperson shall (a) be a non-executive director;

and (b) not be related to the Managing Director or the Chief Executive Officer as per the definition of the term "relative" defined under the Companies Act, 2013. **(Refer Para 8.5 Verification regarding Composition of Board [Regulation 17 & 17A on Page no. 7.16]**

3.1. Insertion in Para 8.5 Verification regarding Composition of Board i.e., Regulations 17:

- The listed entity shall ensure that approval of shareholders for appointment of a person on the Board of Directors [or as a manager] is taken at the next general meeting or within a time period of three months from the date of appointment, whichever is earlier.
- Provided that the appointment or a re-appointment of a person, including as a managing director or a whole-time director or a manager, who was earlier rejected by the shareholders at a general meeting, shall be done only with the prior approval of the shareholders:
- Provided further that the statement referred to under sub-section (1) of section 102 of the Companies Act, 2013, annexed to the notice to the shareholders, for considering the appointment or re-appointment of such a person earlier rejected by the shareholders shall contain a detailed explanation and justification by the Nomination and Remuneration Committee and the Board of directors for recommending such a person for appointment or re-appointment. **(Refer Para 8.5 Verification regarding Composition of Board [Regulation 17 & 17A on Page no. 7.17])**

4. Meaning of Independent Director given on Page no. 7.18 to be read as: Independent director" means a non-executive director, other than a nominee director of the listed entity:

- (i) who, in the opinion of the board of directors, is a person of integrity and possesses relevant expertise and experience;
- (ii) who is or was not a promoter of the listed entity or its holding, subsidiary or associate company [or member of the promoter group of the listed entity];
- (iii) who is not related to promoters or directors in the listed entity, its holding, subsidiary or associate company;
- (iv) who, apart from receiving director's remuneration, has or had no material pecuniary relationship with the listed entity, its holding, subsidiary or associate company, or their promoters, or directors, during the **three** immediately preceding financial years or during the current financial year;
- (v) none of whose relatives— (A) is holding securities of or interest in the listed entity, its holding, subsidiary or associate company during the three immediately preceding financial years or during the current financial year of face value in excess of fifty lakh rupees or two percent of the paid-up capital of the listed entity, its holding, subsidiary or associate company, respectively, or such higher sum as may be specified; (B) is indebted to the listed entity, its holding, subsidiary or associate company or their

promoters or directors, in excess of such amount as may be specified during the three immediately preceding financial years or during the current financial year; (C) has given a guarantee or provided any security in connection with the indebtedness of any third person to the listed entity, its holding, subsidiary or associate company or their promoters or directors, for such amount as may be specified during the three immediately preceding financial years or during the current financial year; or (D) has any other pecuniary transaction or relationship with the listed entity, its holding, subsidiary or associate company amounting to two percent or more of its gross turnover or total income: Provided that the pecuniary relationship or transaction with the listed entity, its holding, subsidiary or associate company or their promoters, or directors in relation to points (A) to (D) above shall not exceed two percent of its gross turnover or total income or fifty lakh rupees or such higher amount as may be specified from time to time, whichever is lower.]

- (vi) who, neither himself /herself, nor whose relative(s) — (A) holds or has held the position of a key managerial personnel or is or has been an employee of the listed entity or its holding, subsidiary or associate company or any company belonging to the promoter group of the listed entity, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed: Provided that in case of a relative, who is an employee other than key managerial personnel, the restriction under this clause shall not apply for his / her employment. (B) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of — (1) a firm of auditors or company secretaries in practice or cost auditors of the listed entity or its holding, subsidiary or associate company; or (2) any legal or a consulting firm that has or had any transaction with the listed entity, its holding, subsidiary or associate company amounting to ten per cent or more of the gross turnover of such firm; (C) holds together with his relatives two per cent or more of the total voting power of the listed entity; or (D) is a chief executive or director, by whatever name called, of any nonprofit organisation that receives twenty-five per cent or more of its receipts or corpus from the listed entity, any of its promoters, directors or its holding, subsidiary or associate company or that holds two per cent or more of the total voting power of the listed entity; (E) is a material supplier, service provider or customer or a lessor or lessee of the listed entity;
- (vii) who is not less than 21 years of age.
- (viii) who is not a non-independent director of another company on the board of which any non-independent director of the listed entity is an independent director.

**(Refer Page no.7.18)**

5. Deletion of word “the immediate next Board meeting or” and “whichever is later” in Regulation 25(6) i.e., sub-point no (ix) An independent director who resigns or is removed from the Board of Directors of the listed entity shall be replaced by a new independent

director at the earliest but not later than three months from the date of such vacancy. **(Refer para 10 Obligations With respect to employees including Senior management, key managerial persons, directors and promoters on Page no. 7.22)**

6. The Board of Directors of every listed public company shall constitute the Nomination and Remuneration Committee which shall comprise of at least three directors, all of whom shall be non-executive directors and at least **two-thirds** shall be independent directors. Deletion of condition i.e., in case of a listed entity having outstanding SR equity shares, two thirds of the committee shall comprise of independent directors. Chairperson of the committee shall be an independent director. **(Refer Para 14 Nomination and Remuneration Committee- Regulation 19 and Part D of Schedule II, on Page No. 7.26)**
- 6.1 Insertion in the role of the Nomination and Remuneration Committee :(1A). For every appointment of an independent director, the Nomination and Remuneration Committee shall evaluate the balance of skills, knowledge and experience on the Board and on the basis of such evaluation, prepare a description of the role and capabilities required of an independent director. The person recommended to the Board for appointment as an independent director shall have the capabilities identified in such description. For the purpose of identifying suitable candidates, the Committee may: a. use the services of an external agencies, if required; b. consider candidates from a wide range of backgrounds, having due regard to diversity; and c. consider the time commitments of the candidates. **(Refer Para 14 Nomination and Remuneration Committee- Regulation 19 and Part D of Schedule II, on Page No. 7.27)**
7. The provisions of regulation 21 shall be applicable to:(i). the top 1000 listed entities, determined on the basis of market capitalization as at the end of the immediate preceding financial year; and, (ii). a 'high value debt listed entity'.
- 7.1 The role of the Risk Management Committee shall, inter alia, include the following:
  - (1) To formulate a detailed risk management policy which shall include: (a) A framework for identification of internal and external risks specifically faced by the listed entity, in particular including financial, operational, sectoral, sustainability (particularly, ESG related risks), information, cyber security risks or any other risk as may be determined by the Committee. (b) Measures for risk mitigation including systems and processes for internal control of identified risks. (c) Business continuity plan.
  - (2) To ensure that appropriate methodology, processes and systems are in place to monitor and evaluate risks associated with the business of the Company;
  - (3) To monitor and oversee implementation of the risk management policy, including evaluating the adequacy of risk management systems;
  - (4) To periodically review the risk management policy, at least once in two years, including by considering the changing industry dynamics and evolving complexity;
  - (5) To keep the board of directors informed about the nature and content of its discussions, recommendations and actions to be taken;

- (6) The appointment, removal and terms of remuneration of the Chief Risk Officer (if any) shall be subject to review by the Risk Management Committee. The Risk Management Committee shall coordinate its activities with other committees, in instances where there is any overlap with activities of such committees, as per the framework laid down by the board of directors.

**(Refer Para 16 Risk Management Committee- Regulation 21 and Part D of Schedule II, on Page No. 7.29)**

**8. Para 18 Information to Shareholders [Regulation 36] to be read as:**

- (1) The listed entity shall send the annual report in the following manner to the shareholders: (a) Soft copies of full annual report to all those shareholder(s) who have registered their email address(es) either with the listed entity or with any depository; (b) Hard copy of statement containing the salient features of all the documents, as prescribed in Section 136 of Companies Act, 2013 or rules made thereunder to those shareholder(s) who have not so registered; (c) Hard copies of full annual reports to those shareholders, who request for the same.
- (2) The listed entity shall send annual report referred to in sub-regulation (1), to the holders of securities, not less than twenty-one days before the annual general meeting.
- (3) In case of the appointment of a new director or re-appointment of a director the shareholders must be provided with the following information: (a) a brief resume of the director; (b) nature of expertise in specific functional areas; (c) disclosure of relationships between directors inter-se; (d) names of listed entities in which the person also holds the directorship and the membership of Committees of the board along with listed entities from which the person has resigned in the past three years; and (e) shareholding of non-executive directors in the listed entity, including shareholding as a beneficial owner; (f) In case of independent directors, the skills and capabilities required for the role and the manner in which the proposed person meets such requirements.

The auditor should ascertain from the communications sent, whether in the case of appointment of a new director or re-appointment of a director, the shareholders have been provided with the information stipulated above. **(Refer Para 18 Information to Shareholders [Regulation 36] on Page no. 7.30)**

9. The listed entity shall submit a quarterly compliance report on corporate governance in the format as specified by the Board from time to time to the recognised stock exchange(s) within twenty one (21) days from the end of each quarter.

The listed entity is also required to formulate a policy on materiality of related party transactions and on dealing with related party transactions. This policy should also include clear threshold limits duly approved by the board of directors. Further, such policy shall be reviewed by the board of directors at least once every three years and updated accordingly.

A related party transaction shall be considered material, if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceeds rupees one thousand crore or ten per cent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity, whichever is lower. **[Regulation 23(1)]**

All related party transactions and subsequent material modifications shall require prior approval of the independent directors in audit committee of the listed entity **[Regulation 23(2)]**

Audit committee may grant omnibus approval for related party transactions proposed to be entered into by the listed entity subject certain conditions **[Regulation 23(3)]**.

The listed entity shall submit to the stock exchanges disclosures of related party transactions in the format as specified by the Board from time to time, and publish the same on its website **[Regulation 23(8)]**.

Provided that a 'high value debt listed entity' shall submit such disclosures along with its standalone financial results for the half year.

Provided further that the listed entity shall make such disclosures every six months within fifteen days from the date of publication of its standalone and consolidated financial results.

Provided further that the listed entity shall make such disclosures every six months on the date of publication of its standalone and consolidated financial results with effect from April 1, 2023. **(Refer Para 22.3 Related Party Disclosures given on Page no. 7.35)**

9.1 As per Schedule V - Annual Report, the annual report shall contain the following additional disclosures relating to Related Party:

1. The listed entity which has listed its non-convertible securities] shall make disclosures in compliance with the Accounting Standard on "Related Party Disclosures".
2. The disclosure requirements shall be as follows:

Sr. no.	In the accounts of	Disclosures of amounts at the year end and the maximum amount of loans/ advances/ Investments outstanding during the year.
1.	Holding Company	<ul style="list-style-type: none"> <li>□ Loans and advances in the nature of loans to subsidiaries by name and amount.</li> <li>□ Loans and advances in the nature of loans to associates by name and amount.</li> <li>□ Loans and advances in the nature of loans to firms/companies in which directors are interested by name and amount.</li> </ul>
2.	Subsidiary	Same disclosures as applicable to the parent company in the accounts of subsidiary company.

3.	Holding Company	Investments by the loanee in the shares of parent company and subsidiary company, when the company has made a loan or advance in the nature of loan.
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For the purpose of above disclosures directors' interest shall have the same meaning as given in Section 184 of Companies Act, 2013.

(2A) Disclosures of transactions of the listed entity with any person or entity belonging to the promoter/promoter group which hold(s) 10% or more shareholding in the listed entity, in the format prescribed in the relevant accounting standards for annual results.

3. The above disclosures shall not be applicable to listed banks.

**(Refer Para 22.3 Related Party Disclosures given on Page no. 7.35)**

### **Chapter – 11: Audit of Non-Banking Financial Companies**

Pursuant to the announcement of *Scale Based Regulation (SBR): A Revised Regulatory Framework for NBFCs* on 22 October 2021 to be effective from 01 October 2022, RBI has revised different facets of existing NBFC Classification and regulation like Capital Requirements, Governance Standards, Prudential Regulations, etc. based on four layers that are defined based on their size, activity, and perceived riskiness.

These four layers are NBFC – Base Layer (NBFC-BL), then NBFC- Middle Layer (NBFC-ML), NBFC Upper Layer (NBFC-UL) and lastly NBFC – Top Layer (NBFC-TL). The Top layer is ideally expected to be empty and will be filled by RBI based on required need.

Details of NBFCs populating the various layers is mentioned below:

#### **Base Layer**

The Base Layer shall comprise of (a) non-deposit taking NBFCs below the asset size of ₹1000 crore and (b) NBFCs undertaking the following activities- (i) NBFC-Peer to Peer Lending Platform (NBFC-P2P), (ii) NBFC-Account Aggregator (NBFC-AA), (iii) Non-Operative Financial Holding Company (NOFHC) and (iv) NBFCs not availing public funds and not having any customer interface.

#### **Middle Layer**

The Middle Layer shall consist of (a) all deposit taking NBFCs (NBFC-Ds), irrespective of asset size, (b) non-deposit taking NBFCs with asset size of ₹1000 crore and above and (c) NBFCs undertaking the following activities (i) Standalone Primary Dealers (SPDs), (ii) Infrastructure Debt Fund - Non-Banking Financial Companies (IDF-NBFCs), (iii) Core Investment Companies (CICs), (iv) Housing Finance Companies (HFCs) and (v) Infrastructure Finance Companies (NBFC-IFCs).

#### **Upper Layer**

The Upper Layer shall comprise of those NBFCs which are specifically identified by the Reserve Bank as warranting enhanced regulatory requirement based on a set of parameters and scoring

methodology as provided in the Appendix to this circular. The top ten eligible NBFCs in terms of their asset size shall always reside in the upper layer, irrespective of any other factor.

### **Top Layer**

The Top Layer will ideally remain empty. This layer can get populated if the Reserve Bank is of the opinion that there is a substantial increase in the potential systemic risk from specific NBFCs in the Upper Layer. Such NBFCs shall move to the Top Layer from the Upper Layer.

### **Categorisation of NBFCs carrying out specific activity**

As the regulatory structure envisages scale based as well as activity-based regulation, the following prescriptions shall apply in respect of the NBFCs

- a) NBFC-P2P, NBFC-AA, NOFHC and NBFCs without public funds and customer interface will always remain in the Base Layer of the regulatory structure.
- b) NBFC-D, CIC, IFC and HFC will be included in Middle Layer or the Upper Layer (and not in the Base layer), as the case may be. SPD and IDF-NBFC will always remain in the Middle Layer.
- c) The remaining NBFCs, viz., Investment and Credit Companies (NBFC-ICC), Micro Finance Institution (NBFC-MFI), NBFC-Factors and Mortgage Guarantee Companies (NBFC-MGC) could lie in any of the layers of the regulatory structure depending on the parameters of the scale based regulatory framework.
- d) Government owned NBFCs shall be placed in the Base Layer or Middle Layer, as the case may be. They will not be placed in the Upper Layer till further notice.

### **References to NBFC-ND, NBFC-ND-SI & NBFC-D - From October 01, 2022:**

All references to NBFC-ND shall mean NBFC-BL and all references to NBFC-D and NBFC-NDSI shall mean NBFC-ML or NBFC-UL, as the case may be.

## **Chapter – 16 : Unit 3: Forensic Accounting (Earlier Forensic Audit)**

The word “*Forensic Audit*” in this Chapter including the name of Unit 3 stands changed to “*Forensic Accounting*”. All the references to “*Forensic Audit*” throughout the study material shall stand changed to “*Forensic Accounting*”. Similarly, ‘Forensic Auditor’ should also be read as ‘Forensic Accountant’.

## **Unit I Peer Review -- Chapter – 17: Peer Review & Quality Review**

The Word “*Statement*” or “*Statement on Peer Review*” used throughout the chapter shall be substituted as “*Guidelines*” or “*Peer Review Guidelines, 2022*” respectively.

### **1. In Para-1 Introduction,**

- a. the words “*Technical, Professional and Ethical Standards as applicable including other regulatory requirements thereto and*” shall be substituted with “*Technical, Professional and Ethical Standards as applicable including Audit Quality Maturity*”



*Model wherever applicable or any other regulatory requirements as may be prescribed by the Council or any Committee and"*

- b. At the end of the explanation of term Peer Review the following reference to guidelines shall be added "[sub-clause 14 of clause 2 of Peer Review Guidelines, 2022]"
  - c. For term Reviewer the following definition shall be substitute  
*"Reviewer" - means a member duly approved and empanelled by the Board on fulfilling the qualifications prescribed for a Reviewer as per Guideline 26 of these Guidelines [sub-clause 19 of clause 2 of Peer Review Guidelines, 2022]"*
  - d. Insertion of Branch Peer Reviewer definition :  
*"Branch Peer Reviewer" – means a Reviewer appointed to conduct the Peer Review of the Branch of a Practice Unit. The qualifications and other obligations and duties of the Branch Peer Reviewer shall be the same as that of the Reviewer [sub-clause 5 of clause 2 of Peer Review Guidelines, 2022]"*
  - e. After the definition of Practice Unit, the following definition of New Unit shall be inserted **"New Unit - means a firm whose date of establishment is less than 12 months immediately preceding the date of receipt of application of Peer Review and which may or may not have rendered any assurance service during the said period or a Practice Unit in existence for a period exceeding 12 months but not rendering any assurance services. [sub-clause 12 of clause 2 of Peer Review Guidelines, 2022]"**
  - f. Revised definition of the term Peer Review Board is **"Peer Review Board - means the Board constituted by the Council in terms of these Guidelines from time to time. [The expression "Peer Review Board" is hereinafter referred to as "Board] [sub-clause 13 of clause 2 of Peer Review Guidelines, 2022]"**  
*"The Peer Review Guidelines, 2022 issued by Council are covered under clause (1) of Part II of Second Schedule to the Act and it is obligatory for the Practice Unit to comply with the provisions contained in this Guidelines." [Page17.3]*
2. In **sub-para 2 of Para 3: Scope of Peer Review** the following clause shall be added after clause (iii) and accordingly all the clauses shall stand re-numbered "(iv) Self-evaluation under Audit Quality Maturity Model or any other guideline issued by the Centre for Audit Quality". **[Page 17.5]**
  3. In **definition of Technical, Professional and Ethical Standards of Para 3: Scope of Peer Review** the following clause shall be added after clause (vi) "(vii) Any other Technical, Professional, Ethical Standards and other Standards issued by any authority governing the profession of Chartered Accountancy. [sub-clause 23 of clause 2 of Peer Review Guidelines, 2022]" **[Page 17.6]**
  4. In **definition of Assurance Engagement of Para 3: Scope of Peer Review** the following clause shall be added after clause (viii) "(ix) Any other service rendered, or function

performed by practitioner not prescribed by the Council to be 'Assurance Engagement [sub-clause 2 of clause 2 of Peer Review Guidelines, 2022]" [Page 17.6]

5. Whole **Para 4 Applicability on Page 17.7** shall stand substituted with the below Paragraph:

**"Practice Units subject to Review:** Earlier practice units were classified under Level -I and Level-II category. However, under Peer Review Guidelines this has been replaced with Peer Review Mandate implementation. As per Clause 5 of Peer Review Guidelines, 2022, criteria of Peer Review are defined on following basis:

i.	<b>Mandatory</b> - Peer Review can be mandated for such Practice Units as may be decided by the Council. Or,
ii.	<b>Voluntary</b> - Any Practice Unit may, suo motu, apply to the Board for the conduct of its Peer Review. Or,
iii.	<b>Special Case</b> - The Board, based on specific information received from Secretary, ICAI or Disciplinary directorate or any other Regulator, which in the opinion of the Board requires a special Peer Review of the Practice Unit, may conduct a special Peer Review of the Practice Unit for such a period determined by the Board.

For Mandatory category the Council at its 407th Meeting of the Council held from 7th– 9th January 2022 decided to mandate the Peer Review process for coverage of more firms under Peer Review process i.e. the Peer Review Mandate.

Also, it was clarified that holding a valid Peer Review certificate by Practice Units should be a prerequisite for undertaking audit of all entities falling under phase I; II; III and IV of the mandate from respective dates of mandate becoming operative.

Accordingly, the Peer Review Mandate (Revised), operative from April 1, 2022, has been made in following four stages:

Phase	Category of firms covered for Mandatory Peer Review	Date from which Peer Review is Mandatory
I(*)	Practice Units which propose to undertake Statutory Audit of enterprises whose equity or debt securities are listed in India or abroad as defined under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015: For these Practice Units, there is a pre-requisite of having Peer Review Certificate.	1st April 2022
II	Practice Units which propose to undertake Statutory Audit of unlisted public companies having	1st April 2023

	<ul style="list-style-type: none"> <li>▢ paid-up capital of not less than rupees five hundred crores or</li> <li>▢ having annual turnover of not less than rupees one thousand crores or</li> <li>▢ having, in aggregate, outstanding loans, debentures and deposits of not less than rupees five hundred crores</li> </ul> <p>as on the 31<sup>st</sup> March of immediately preceding financial year: For these Practice Units, there is a pre-requisite of having Peer Review Certificate.</p> <p><b>OR</b></p> <p>Practice Units rendering attestation services and having 5 or more partners: For these Practice Units, there is a pre-requisite of having Peer Review Certificate before accepting any Statutory audit.</p>	
<b>III</b>	<p>Practice Units which propose to undertake the Statutory Audit of entities which have raised funds from public or banks or financial institutions of over Fifty Crores rupees during the period under review or of anybody corporate including trusts which are covered under public interest entities : For these Practice Units, there is a pre-requisite of having Peer Review Certificate.</p> <p><b>OR</b></p> <p>Practice Units rendering attestation services and having 4 or more partners: For these Practice Units, there is a pre-requisite of having Peer Review Certificate before accepting any Statutory audit.</p>	<b>1st April 2024</b>
<b>IV</b>	<p>Practice Units which propose to undertake audits of branches of Public Sector banks : For these Practice Units, there is a pre-requisite of having Peer Review Certificate.</p> <p><b>OR</b></p> <p>Practice Units rendering attestation services and having 3 or more partners: For these Practice Units, there is a pre-requisite of having Peer Review Certificate before accepting any Statutory audit.</p>	<b>1st April 2025</b>

(\*) for auditors from this category, Peer Review is already mandatory by SEBI; this mandate is a further requirement stipulated by the ICAI.

Thus, at each phase, before undertaking statutory audit, the concerned Practice Unit should possess Peer Review Certificate.

**For example:**

- i) for the Practice Units, from 1st April, 2023, there is a pre-requisite of having Peer Review Certificate for undertaking Statutory Audit of unlisted public companies having paid-up capital of not less than rupees five hundred crores or having annual turnover of not less than rupees one thousand crores or having, in aggregate, outstanding loans, debentures and deposits of not less than rupees five hundred crores as on the 31st March of immediately preceding financial year or
- ii) From 1st April, 2024, Practice Units rendering attestation services and having 4 or more partners should have a Peer Review Certificate before undertaking any statutory audit.

On the date, Peer Review becoming mandatory for a Practice Unit, if it is in possession of Peer Review Certificate, there is no need of once again subjecting the Practice Unit to Peer Review, till conclusion of the validity period of the said Certificate. It is necessary for such a Practice Unit to possess a new Peer Review Certificate on conclusion of validity of Peer Review Certificate that was available at the time Peer Review becoming mandatory.”

6. Insertion of minimum of 6 members requirement and in Para 5 Peer Review Board which should be read as under:

***“The Board shall consist of a minimum of six and a maximum of twelve members to be appointed by the Council, of whom not less than fifty per cent shall be from amongst the members of the Council.”***

7. In Para 5 Peer Review Board, Meeting Requirements to be read as :

*“Provisions related to the time, place and quorum of Meetings of the Peer Review Board as well as procedure for transaction of business shall be governed by the Chartered Accountants Regulation, 1988.”*

8. In **Para 5.1 Eligibility to be a Reviewer**, in point 1, ‘7 year audit experience’ to be read as ‘7 years of assurance practice experience’.
9. In para 5.3 Confidentiality para (b) ‘unless’ word to be read as ‘**except**’ and last para to be read as ***“A Declaration of Confidentiality (Form 4) shall be signed by all members of the Board and the Board’s Secretariat.”***

10. Whole **Para 7.1 Selection of Practice Unit & appointment of Reviewer and 7.2 Planning on Pages 17.14 and 17.15** shall stand substituted with the below Paragraph:

**“Procedure for initiating Peer Review:**

- (1) Practice Units which desire to get Peer Reviewed shall make an application for Peer Review in the Application cum Questionnaire in Form 1.

- (2) In case the Peer Review is initiated by the Board, the Application cum Questionnaire in Form 1 should be submitted by the Practice Unit on the request of the Peer Review Board Secretary.
- (3) The Application mentioned under clauses 6(1) and 6(2) above received by the Board shall be duly numbered.
- (4) On receipt of the said Application cum Questionnaire, names of three Reviewers shall be recommended by the Board to the Practice Unit within three working days.
- (5) The Practice Unit shall select one out of the three recommended Reviewers and intimate to the Board within one working day of receipt of the names.
- (6) The Board shall appoint the Peer Reviewer selected by the Practice Unit in accordance with these Guidelines.
- (7) The Board shall intimate the Reviewer so selected to submit a Declaration of Confidentiality in Form 2 to the Practice Unit within two working days from the receipt of choice of name of the Reviewer from the Practice Unit.
- (8) The Practice Unit shall also provide a copy of the Application cum Questionnaire in Form 1 submitted to the Board as per clause 6 (1) or 6(2) above to the Reviewer within two working days of the appointment of the Reviewer.

**Peer Review Procedure to be followed by the Peer Reviewer:**

- (1) Before commencement of Peer Review, the Peer Reviewer shall ensure that the Declaration of confidentiality is furnished to the Practice Unit and acknowledgement of receipt thereof is obtained by him.
- (2) On receiving the Application cum Questionnaire in Form 1 from the Practice Unit, the Peer Reviewer shall initiate the Peer Review by intimating the Practice Unit of proposed visit and the proposed samples selected to be kept ready by the Practice Unit. The proposed samples selected are to be intimated by the Peer Reviewer in Form 5 prescribed by the Board.
- (3) The Reviewer may seek further/ additional clarification in Form 6 from the Practice Unit on the information furnished/ not furnished by the Practice Unit in the Questionnaire. The Practice Unit shall provide this additional information to the Reviewer within one working day.
- (4) The Reviewer shall, within two working days of receiving the information from the Practice Unit, select assurance service engagements that he would like to review and intimate the same to the Practice Unit and the Peer Review Board in Form 5.
- (5) The Reviewer shall plan for an “on-site review” visit for initial meeting in consultation with the Practice Unit. The Reviewer shall give the Practice Unit at least two working days to keep ready necessary records of the selected assurance services in Form 5.

- (6) The Reviewer and Practice Unit shall mutually co-operate and ensure that the entire review process is completed within twenty working days from the date of receipt of application from the Practice Unit for being Peer Reviewed or from the date of notifying the Practice Unit about its selection for Review as the case may be.
  - (7) In case of Peer Review of a New Unit, the Reviewer and Practice Unit shall mutually co-operate and ensure that the entire review process is completed within seven working days from the date of receipt of application cum questionnaire from the Practice Unit for being Peer Reviewed"
11. In **point (i) of Para 7.3 Execution** the words "seven working days" should be substituted with "six working days". **[Page 17.15]**
  12. In **Para 7.3 Execution** the following paragraphs shall be added:  
**"Procedure for Peer Review of a New Unit :**
    1. Peer Review of a New Unit is to be conducted based on the antecedents of partners and policy parameters announced by the Practice Unit for conduct of attest function. The Reviewer has to verify the same from the Application cum Questionnaire submitted by the Practice Unit in Form 1 as well as an onsite visit to the Practice Unit which shall be restricted to one day.
    2. The Reviewer shall thereafter submit a Report to the Board in the formats as prescribed by it." **[Page 17.15]**
  13. **Para 7.4 Reporting to be read as Reporting by the Peer Reviewer**  
 After completing the on-site review, the Reviewer, shall submit the Peer Review Report to the Board along with Form 9 if in his opinion, the Practice Unit has adequate systems and procedures in compliance with the Technical, Professional and Ethical Standards. A copy of the report shall also be forwarded to the Practice Unit.
    - (1) In case, in the opinion of the Peer Reviewer, the systems and procedures of the Practice Unit are deficient or non-compliant with reference to any matter that has been noticed by him or if there are other matters where he wants to seek clarification, he shall communicate his findings to the Practice Unit, in a Preliminary Report issued by him.
    - (2) The Practice Unit shall, within two working days of the date of receipt of the findings, make its submissions or representations, in writing to the Reviewer.
    - (3) If the Reviewer is satisfied with the reply received from the Practice Unit, he shall submit an unqualified Peer Review Report to the Board along with Form 9. A copy of the report shall also be forwarded to the Practice Unit.
    - (4) In case the Reviewer is of the opinion that the response submitted by the Practice Unit under clause 9(4) above is not satisfactory, the Reviewer shall submit a Qualified Report to the Board incorporating his reasons for the same along with Form 9. A copy

of the report shall also be forwarded to the Practice Unit.

- (5) The Peer Review Report should state that the system of quality control for the assurance services of the Practice Unit for the period under Review has been designed so as to carry out the assurance services in a manner that ensures compliance with Technical, Professional and Ethical Standards.
- (6) The Peer Reviewer shall ensure to submit the following documents along with the Peer Review Report:
  - (i) Annexures to the Report as prescribed by the Board
  - (ii) Copy of Questionnaire as received from the Practice Unit
  - (iii) List of samples selected by him in accordance with the criteria prescribed by the Board
  - (iv) Preliminary Report, if issued, along with Practice Unit's submissions on the same.
- (7) The Practice Unit as well as the Reviewer shall ensure that all documents submitted to the Board are duly dated, signed and complete in all aspects.
- (8) The Reviewer and Practice Unit shall mutually co-operate and ensure that the entire review process is completed within twenty working days from the date of receipt of application from the Practice Unit for being Peer Reviewed or from the date of notifying the Practice Unit about its selection for Review as the case may be.
- (9) In case of Peer Review of a New Unit, the Reviewer and Practice Unit shall mutually co-operate and ensure that the entire review process is completed within seven working days from the date of receipt of application cum questionnaire from the Practice Unit for being Peer Reviewed." [Page 17.17]

**14. Review of report by the Peer Review Secretariat under the supervision and directions of Peer Review Board Secretary**

- (1) The Peer Review Board Secretary shall ensure that the Peer Review report is accompanied by all the documents as mentioned under Clause 9 (7) of the Guidelines. It shall also ensure that the documents are complete in all aspects.
- (2) All reports shall be placed before the Board or its Sub-Committee for its consideration and issuance of Peer Review Certificate.
- (3) In case of a qualified report, the Peer Review Board Secretary shall place the report before the Board for consideration. The Board may decide for a "Follow On" Review after a period of one year from the date of issue of report by the Peer Reviewer. If the Board so decides, the period of one year may be reduced but shall not be less than six months from the date of issue of the report.

**15. Issuance of Peer Review Certificate**

- (1) In case of an unqualified report issued by the Peer Reviewer, the Peer Review Board Secretary shall place the report before the Board or its Sub-Committee for consideration and issuance of Peer Review Certificate to the Practice Unit, but only after the Peer Reviewer confirms the fee receipt from the Practice Unit by him.
- (2) A Peer Review Certificate shall be issued to New Units subject to the Procedures followed by the reviewer as prescribed under Clause 8 of these Guidelines and other clauses of these Guidelines, as the case may be.
- (3) The Certificates so issued by the Board or the Sub-Committee shall be noted by the Board at its meeting.
- (4) The Certificate shall be duly signed by the Chairman, Vice Chairman and Secretary of the Board mentioning the validity period.
- (5) The Peer Review Board Secretary shall serve the Peer Review Certificate upon the Practice Unit.
- (6) The Peer Review Board Secretary shall update the List of Practice Units having a valid Peer Review certificate incorporating the names of Practice Units to whom the Peer Review certificates have been issued on the ICAI website.
- (7) In cases where a Qualified Report has been issued by the Reviewer and has been considered by the Board, the Peer Review Board Secretary shall inform the Practice Unit that a Peer Review certificate cannot be issued along with the reasons therefor as well as inform about the due date for conducting a follow on review as may be decided by the Board.

16. In **Para 7.6 Validity of Peer Review Certificate** the following shall be added at the end of the paragraph:

“The Peer Review Certificate issued to a Practice Unit shall be valid for a period of three years or such other period as may be decided by the Board commencing from the date of receipt of Peer Review report by the Board. The validity of the Peer Review Certificate issued to New Units shall be decided by the Board.

The Council may for such reasons as may be prescribed by it extend the validity of existing Peer Review certificate granted to a Practice Unit. The Practice Unit shall make an Application in Form 8 requesting for extension of validity”.

**Chapter – 18: Professional Ethics**

The Council at its 413<sup>th</sup> meeting held in August, 2022 decided the above-mentioned deferred provisions contained in Volume-I of Code of Ethics, 2019 which have been deferred from 1st July, 2020 till 30th September, 2022 will be made applicable **from 1st October 2022 with certain amendments.**



The significant amendments are as under: -

S. No.	Existing provision	Revised provision
<b>Fees - Relative Size</b> <b>[Paragraphs 410.3 to R410.6]</b>		
1.	Disclosure is required where for two consecutive years, the gross annual professional fees from audit client represent more than 15% of the total fees of the firm.	Differentiated disclosure requirements:- <b>For non Public Interest Entities (PIE)-</b> Disclosure is required where for two consecutive years, the gross annual professional fees from an audit client represent more than 40% of the total fees of the firm.  <b>For public interest entities-</b> Disclosure is required where for two consecutive years, the gross annual professional fees from an audit client represent more than 20% of the total fees of the firm.
2.	Exemption from applicability of the provision where total Fees received by Firm does not exceed 5 lacs of rupees.	Exemption from applicability of the provision where total Fees received by Firm does not exceed 20 lacs of rupees.
3.	Exemption from the applicability of the provision in the case of audit of government Companies, public undertakings, nationalised banks, public financial institutions or where appointments of auditors are made by the Government.	In addition to these categories, 'Regulators' has been added.
4.	Disclosure to Those Charge with Governance of audit client	Disclosure to the Institute
5.	Pre-Issuance review or Post issuance Review: Action to be taken to address the threat created due to fees dependency as aforesaid.	Repealed

<b>Tax Services to Audit Clients</b> <b>[Subsection 604]</b>		
6.	In case of Assistance in the resolution of Tax disputes, the term "Court" is explained as under: - "What constitutes a "Court" depends on how tax proceedings are heard in India"	In case of Assistance in the resolution of Tax disputes, the term "Court" is explained as under: - "For the purpose of this subsection, "Court" does not include a Tribunal".
<b>Responding to Non-Compliance with Laws and Regulations (NOCLAR) applicable to Professional Accountants in service</b> <b>(Section 260)</b>		
7.	Applicable to all employees of listed entities	Applicable to Senior Professional Accountants in service, being employees of listed entities.
8.	Senior professional accountants in service ("senior professional accountants") are directors, officers or senior employees able to exert significant influence over, and make decisions regarding, the acquisition, deployment and control of the employing organization's human, financial, technological, physical and intangible resources.	No Change.  It is further explained that the senior professional accountants refer to key managerial personnel.
<b>Responding to Non-Compliance with Laws and Regulations (NOCLAR) applicable to Professional Accountants in public practice</b> <b>(Section 360)</b>		
9.	Applicable to Audit engagement of all listed entities	Applicable to Audit engagements of entities the shares of which are listed on recognized stock exchange(s) in India and have net worth of 250 crores of rupees or more.  The applicability of Section 360 will subsequently be extended to all listed entities, at the date to be notified later.

10.	The term “Audit Engagement” defined in Glossary as applicable to entire Code: - “A reasonable assurance engagement in which a professional accountant in public practice expresses an opinion whether financial statements are prepared, in all material respects (or give a true and fair view or are presented fairly, in all material respects), in accordance with an applicable financial reporting framework, such as an engagement conducted in accordance with Standards on Auditing. This includes a Statutory Audit, which is an audit required by legislation or other regulation”	No change in definition with respect to rest of the Volume-I of Code of Ethics. “For the purpose of Section-360 “Audit” or “Audit engagement” shall mean a reasonable assurance engagement in which a professional accountant in public practice expresses an opinion whether financial statements give a true and fair view in accordance with an applicable financial reporting framework”.
11.	Measures to be taken in case of imminent breach.	Repealed

**Note:** Students are also advised to refer RTP of Paper 1 Financial Reporting (for AS, Ind AS and other updates) and Paper 4 Part A -Corporate Laws (for academic updates relating to Company Law).

## PART – II : QUESTIONS AND ANSWERS

### QUESTIONS

#### PART A: MULTIPLE CHOICE QUESTIONS

##### Integrated Case Scenario 1.

Good Deposit Limited a NBFC registered with RBI under section 45-IA of the RBI Act and listed on National Stock Exchange, appointed ABC & Co. Chartered Accountants as their statutory Auditor for the financial year ending on 31 March 2023. Mr. J the audit partner of ABC & Co. extracted the monthly net owned fund position from the books of Goods Deposit Limited. ABC & Co was peer-reviewed last in January 2019, and its peer review certificate was valid until January 2022. ABC & Co did not apply for Peer Review after January 2022 till the date of the acceptance of the audit.

Month	Net Owned Funds (as calculated based on monthly position)
April 2022	₹ 350 Lakh
May 2022	₹ 350 Lakh
June 2022	₹ 320 Lakh
July 2022	₹ 310 Lakh
August 2022	₹ 290 Lakh
September 2022	₹ 250 Lakh
October 2022	₹ 240 Lakh
November 2022	₹ 190 Lakh
December 2022	₹ 180 Lakh
January 2023	₹ 240 Lakh
February 2023	₹ 270 Lakh
March 2023	₹ 310 Lakh

The Board of Good Deposits Limited consisted of 9 directors, of which five were non-executive, including a woman director, and two were independent. Out of the above, the Chairperson of the Board was a regular non-executive director and promoter of the Company. The Company was not out of the 1000 top listed entities for the past five years.

During the year, Mr. J recommended to the Board and Audit Committee to have internal auditors. However, Board, citing budget issues, rejected the Audit Partner's recommendation. Board, however, assured that they would consider next year to have an internal audit department within the Company.

**On the basis of the abovementioned facts, you are required to choose the most appropriate answer for the following MCQs:**

**QUESTIONS:**

- Mr J reported, under Clause 3(A)(III) of Master Direction - Non-Banking Financial Companies Auditor's Report (Reserve Bank) Directions, 2016, that Good Deposit Limited is not eligible to hold its Certificate of Registration under section 45-IA of the RBI Act, as during the year the Net Owned Funds went below the minimum required limit. Management of the NBFC had a different opinion that a certificate pertaining to the Net Owned Funds from the Statutory Auditor is required with reference to the position of the Company as at the end of the financial year ended 31 March and not based on each month's position. Kindly guide Mr J with respect to the requirement under Master Direction.
  - Every NBFC shall submit a Certificate from its Statutory Auditor that it is eligible to hold a Certificate of Registration under Section 45-IA of the RBI Act. Such a certificate

should be with reference to the position of the Company as of the end of the financial year ended 31 March.

- (b) Every NBFC shall submit a Certificate from its Statutory Auditor that it is eligible to hold a Certificate of Registration under Section 45-IA of the RBI Act. Such a certificate should be with reference to the position of the Company as of the end of each month.
  - (c) Every NBFC shall submit a Certificate from its Statutory Auditor that it is eligible to hold a Certificate of Registration under Section 45-IA of the RBI Act. Such a certificate should be with reference to the position of the Company throughout the financial year.
  - (d) Only NBFC-MFI shall submit a Certificate from its Statutory Auditor that it is eligible to hold a Certificate of Registration under Section 45-IA of the RBI Act. Such a certificate should be with reference to the position of the Company throughout the financial year.
2. Mr J was of the opinion that the Composition of the Company's Board of Directors is not in compliance with the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015. Kindly Guide the management with respect to the provision, which is not complied by the management, specified in Regulation 17 of SEBI LODR Regulations.
- (a) Where the regular non-executive Chairperson is a promoter of the listed entity or is related to any promoter or person occupying management positions at the level of the Board of director or at one level below the Board of directors, at least half of the Board of directors of the listed entity shall consist of independent directors.
  - (b) Where the Chairperson of the Board of directors is a non-executive director, at least one-third of the Board of directors shall comprise of independent directors and where the listed entity does not have a regular non-executive chairperson, at least half of the Board of directors shall comprise of independent directors.
  - (c) The Board of directors shall have an optimum combination of executive and non-executive directors with at least one-woman director, and not less than fifty per cent of the Board of directors shall comprise of non-executive directors.
  - (d) Where the Chairperson of the Board of directors is a non-executive director, at least one-fourth of the Board of directors shall comprise of independent directors and where the listed entity does not have a regular non-executive chairperson, at least one-third of the Board of directors shall comprise of independent directors.
3. At the time of accepting the Audit of Good Deposit Limited, the quality engagement partner objected that ABC & Co. does not hold a peer review certificate and hence cannot accept the statutory audit of the NBFC. Mr J was of the opinion that ABC & Co were falling under the Level-II category, and hence, they are required to get themselves peer reviewed once in 4 years. Kindly guide Mr J with respect to the peer review requirements as per Peer Review Guidelines 2022.

- (a) Every Practice Unit falling under the category of Level II is required to get peer-reviewed once in every 4 years. ABC & Co. was last peer reviewed in January 2019, and accordingly, they need to get themselves peer reviewed by January 2023.
  - (b) As per the peer review mandate, Practice Units which propose to undertake Statutory Audits of enterprises whose equity or debt securities are listed in India or abroad as defined under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, for these Practice Units, there is a pre-requisite, starting from 1 April 2022, of having Peer Review Certificate before undertaking the Statutory Audit assignment.
  - (c) Every Practice Unit falling under the category of Level II is required to get peer-reviewed once every 3 years. ABC & Co. was last peer reviewed in January 2019, and accordingly, they need to get themselves peer reviewed by January 2022.
  - (d) Practice Units are required to wait for the allotment of Peer Reviewers by the Board. Once the names of Peer reviewers are intimated by the Practice Unit, then the Practice Unit can initiate the process of Peer Review with the reviewer.
4. Mr J wants to highlight the matter with respect to the absence of internal audit function in his audit report under the Emphasis of Matter paragraph. However, management was of the view that the audit partner was not right by disclosing the said matter in his audit report as it was an internal matter, and the audit team had not identified any material evidence which could impact the opinion of the auditor. Kindly guide Mr J whether proposed reporting under Emphasis of Matter (EOM) para in the Audit Report is correct.
- (a) EOM paragraph included in auditor's report 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. Hence reporting under EOM is correct.
  - (b) EOM paragraph included in auditor's report refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, auditor's responsibilities or auditor's report. Hence reporting under EOM is incorrect.
  - (c) EOM paragraph included in auditor's report 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. Hence reporting under EOM is incorrect.
  - (d) EOM paragraph included in auditor's report refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, auditor's responsibilities or auditor's report. Hence reporting under EOM is correct.

5. Kindly guide Mr J regarding areas where he may need to report the absence of Internal Audit Function in the Company in Audit Report.
- (a) The auditor is required to report the matter in the Basis of Qualification paragraph of his audit report as the Auditor was unable to place reliance on the internal audit function of the Company.
  - (b) The auditor is required to report the same under Para 3(xiii) of the CARO (Companies Auditor's Report Order), 2020.
  - (c) The auditor is required to report the same under Para 3(xiv) of the CARO (Companies Auditor's Report Order), 2020.
  - (d) The auditor is required to report the said matter in Key Audit Matters as per SA 701, which requires significant professional judgement and user attention.

**Independent MCQs**

6. Mr. D is a practising Chartered Accountant from Mangalore. He has been practising as a sole proprietor for past two decades. Mr. D's daughter Ms. S is a newly qualified chartered accountant, who cleared the final exam just three months ago. Immediately after qualifying, she also wanted to set up a sole proprietary concern and practice on her own. After setting up the firm, she printed her own visiting card as follows:

**S & Co., Chartered Accountants**

Proprietrix.: Ms. S, FCA, B. Com

Office: JJ Nagar, Mangalore.

Phone: 9123456780

In view of above visiting card, whether Ms. S will be held guilty of professional misconduct? If so, under which clause?

- (a) No, Ms. S won't be guilty of misconduct. As per recent decision of the council, a CA in practice can give any details in the visiting card, except for vision of the firm.
- (b) Yes, Ms. S will be guilty of professional misconduct as per Clause 7 of Part I of First Schedule.
- (c) Yes, Ms. S will be guilty of professional misconduct as per Part III of Second Schedule.
- (d) Yes, Ms. S will be guilty of professional misconduct as per Clause 1 of Part III of First Schedule.

7. M/s ADI & Associates are the statutory auditors of PRAKASH Ltd. for the financial year 2022-23. While conducting the audit, CA Saurabh, the engagement partner noticed the following:

- Payments to various government employees not supported by any document.
- Notices received from various regulatory authorities.
- Payments of various fines and penalties
- Heavy payments to legal counsels.
- Unusual cash payments

CA Saurabh should consider the above as indicative of:

- (a) Doubt on the accounting system of PRAKASH Ltd.
  - (b) Doubt of non-compliance to laws by PRAKASH Ltd.
  - (c) Doubt on the going concern assumption of PRAKASH Ltd.
  - (d) Doubt on Internal Controls of PRAKASH Ltd.
8. You have been given an assignment of audit of IT department of a PSU. A checklist was handed over to you which contained many questions such as,
- ◆ Are external (offsite) data backups maintained at a place outside the premises?
  - ◆ Are separate usernames and passwords assigned to individual users?
  - ◆ Are periodical changes of passwords ensured?

The type of audit being conducted is likely to be:

- (a) Compliance audit.
  - (b) Propriety audit.
  - (c) Comprehensive audit.
  - (d) Financial audit.
9. Sudarshan & Co. was one of the joint auditors of Trilok Insurance Co. Ltd. Mr. Mukesh, one of the engagement team members, of the said joint auditor, was examining the expenses included in different accounts.

While verifying the expenses incurred in relation to employees, Mr. Mukesh made a list of the same as follows, which he was going to discuss with his senior: -

Particulars	₹	Included in which account?
Payment of Salaries to employees	95 lakh	Employees' Remuneration and Welfare Benefits Account



Reimbursement of premium in respect of employees' health cover	15 lakh	Employees' Remuneration and Welfare Benefits Account
Training and non-training expenses incurred for employees	28 lakh	Employees' Remuneration and Welfare Benefits Account
Expenses incurred towards medical treatment of employees not having health cover	12 lakh	Employees' Remuneration and Welfare Benefits Account
Incentives paid to employees of the company who have solicited insurance policies	36 lakh	Commission account

Whether it can be said that Trilok Insurance Co. Ltd. has properly accounted for the expenses incurred in relation to employees?

- (a) No, training and non-training expenses incurred for employees should be bifurcated and shown separately and expenses incurred towards medical treatment of employees not having health cover should be included in 'Others' account.
  - (b) No, reimbursement of premium in respect of employees' health cover should be included in 'Others' account and incentives paid to employees should be included in Employees' Remuneration and Welfare Benefits Account.
  - (c) No, expenses incurred towards medical treatment of employees not having health cover should be included in 'Others' account and non-training expenses have to be shown separately.
  - (d) No, non-training expenses have to be shown separately and incentives paid to employees should be included in Employees' Remuneration and Welfare Benefits Account.
10. PARAS bank had an NPA account of M/s SUPARAS showing recoverable amount of ₹ 35 lakh in the books. It sold the NPA for ₹ 37 lakh. Please select as to which of the following options is the correct accounting:
- (a) Let the amount remain in SUPARAS account.
  - (b) Credit the excess of ₹ 2 lakh to profit on sale of assets.
  - (c) Credit the excess of ₹ 2 lakh to Provision for loss on sale of NPAs.
  - (d) Return ₹ 2 lakh to the party purchasing the NPA.

## PART B : DESCRIPTIVE QUESTIONS

### Standards on Auditing, Statements and Guidance Notes

11. Mangal & Co., Chartered Accountants, have been appointed Statutory Auditors of Mani Ltd. for the financial year 2021-22. 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.

12. CA P is the auditor of Master Data Ltd. for the year 2021-22. The company requests the auditor to undertake an exercise involving only verification of trade receivables for half year ending 30<sup>th</sup> September 2021. The company wants to be satisfied that trade receivables are properly confirmed and reconciled.

In this regard, CA P has to verify the arithmetical accuracy of trade receivables, obtain confirmation of trade receivables and ensure verification of proper reconciliations with confirmations.

He is in a dilemma as to whether he can give a report providing assurance to the company in this respect. Guide CA P with reasoning. Assume that above exercise can be undertaken and there is no legal bar.

#### **Audit Strategy Planning and Programming**

13. (a) Krishna Ltd is a small-sized 25 years old company having business of manufacturing of pipes. Company has a plant based out of Haridwar and have their corporate office in Meerut. Recently the company appointed new firm of Chartered Accountants as their statutory auditors.

The statutory auditors want to enter into an engagement letter with the company in respect of their services but the management has contended that since the statutory audit is mandated by law, engagement letter may not be required. Auditors did not agree to this and have shared a format of engagement letter with the management for their reference before getting that signed. In this respect management would like to understand that as per SA 210 (auditing standard referred to by the auditors), if the agreed terms of the engagement shall be recorded in an engagement letter or other suitable form of written agreement, what should be included in terms of agreed audit engagement letter?

- (b) Suvrat Ltd had a net worth of INR 2100 crore and Ind AS are applicable to them. The company had various derivative contracts – options, forward contracts, interest rate swaps etc. which were required to be fair valued for which company got the fair

valuation done through an external third party. The statutory auditors of the company involved an auditor's expert to audit valuation of derivatives. Auditor and auditor's expert were new to each other i.e., they were working for the first time together but developed a good bonding during the audit. The auditor did not enter into any formal agreement with the auditor's expert. Please advise.

#### **Risk Assessment and Internal Control**

14. (a) During the course of audit of Treasure Ltd., CA Gautam is concerned with the quality and effectiveness of internal control. Towards achieving his objective, he wants to assess and evaluate the control environment. Guide CA Gautam with well-defined set of the Standard Operating Procedures in the assessment and evaluation of control.
- (b) Auditors are required to obtain an understanding of internal control relevant to the audit when identifying and assessing its effectiveness and risk of material misstatement. During the audit of Acharya Ltd., you observed that significant deficiency exists in the internal control system, and you want to ascertain the same. Elucidate the various indicators of significant deficiencies which will help you in assessing the efficiency of internal control system of the organization.

#### **Special Aspects of Auditing in an Automated Environment**

15. Wish for New Foundations Ltd., a pharmaceutical company, collected the data from some hospitals and their experts tried to understand medical needs of elderly people. After complete study, their experts developed an application where this company will provide complete health care after charging a nominal amount from the customers, if customers download this application in their mobile phones. CA Sheetal in his audit has used data analytics method also known as Computer Assisted audit techniques.

Give illustrations of suggested approach to get the benefit from the use of CAATs.

#### **The Company Audit**

16. 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 31<sup>st</sup> March. During the audit for the year ended 31<sup>st</sup> March 202X, the auditor M/s Y&S Associates noted the following points:
  - (i) On 15<sup>th</sup> 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 17<sup>th</sup> 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.

### Audit Report

17. (a) CA. K is appointed statutory auditor of SEEK INDIA PVT LTD under the Companies Act 2013 for the first time. The company is preparing its accounts, considering the applicable requirements of Division I of Schedule III of the Companies Act, 2013. On scrutinising, the company's financial statements for an audit, it was noticed that notes to accounts show the ageing of trade payables as per amended requirements of the Schedule III of the Companies Act, 2013.

The ageing schedule forming part of the notes is as under: -

Outstanding for following periods from the 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 month of March 2022. On inquiry, he came to know that the company's stock audit was conducted in January, 2022 and stock auditors have commented vide their report dated 25.2.2022 that the company had negative drawing power due to high creditors. Accordingly, the bankers have refused further debits in the cash credit account since March 2022.

Further, upon inquiry with the management, it was identified that management did not have any major future contracts to boost their revenue and financial position.

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 Companies Act, 2013.

- (b) CA. Bharat has been appointed as Statutory Auditor of RISHABH Ltd. for the financial year 2021-2022. 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. Bharat 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 RISHABH Ltd.

#### **Audit of Consolidated Financial Statements**

18. CA. Vishudh is the auditor of Brilliant Ltd., a parent company which presents Consolidated Financial Statements. The management of Brilliant Ltd. has provided the list of the components included in the Consolidated Financial Statements. As an auditor of Consolidated Financial Statements, CA Vishudh has to verify that all the components have been included in the Consolidated Financial Statements and review the information provided by the management in identifying the components. State the procedures to be followed by CA. Vishudh in respect of completeness of this information.

#### **Audit of Banks**

19. BOT Limited is enjoying cash credit facility sanctioned from Nariman Point, Mumbai branch of KNB Bank for ₹250 crore. However, for practical considerations, various sub-limits have been fixed for the borrower company for operation at Solapur, Pune and Nashik branches of the same bank.

The manager of the Solapur branch notices that there are no credit transactions in sub-limit account being operated at the Solapur branch for more than 90 days as on 31<sup>st</sup> March, 2022.

Discuss the approach of CA. Muni, statutory branch auditor of Nariman Point branch, Mumbai of KNB Bank, in the matter of asset classification of the above borrower account. Also discuss considerations for classifying said account at the Solapur branch.

**Audit under Fiscal Laws**

20. CA. Gunjan is conducting tax audit of a company. The client is engaged in business of manufacturing and export of carpets (Turnover ₹100 crore in year 2021-22). The financial statements of the company show amount of ₹4 crore credited in Statement of Profit and Loss on account of "Duty Drawback".
- (a) How should she perform audit procedures to comply with specific reporting requirements under Form 3CD in this respect?
- (b) It was noticed that amount of ₹ 5 lac of duty drawback pertaining to few export shipments has not been credited in Statement of Profit and loss. The above noted amount was admitted by customs authorities in month of March 2022. However, it was electronically transferred to bank account of the company in next financial year. How should she deal with the matter?

**Audit of Public Sector Undertakings**

21. Siddha Ltd., a company wholly owned by central government was disinvested during the previous year, resulting in 40% of the shares being held by public. The shares were also listed on the BSE. Since the shares were listed, all the listing requirements were applicable, including publication of quarterly results, submission of information to the BSE etc.
- Mahavir, the FM of the company is of the opinion that now the company is subject to stringent control by BSE and the markets, therefore the auditing requirements of a limited company in private sector under the Companies Act 2013 would be applicable to the company and the C&AG will not have any role to play. Comment.

**Due Diligence, Investigation and Forensic Audit**

22. CA. Sanjana is acting as Credit manager in branch of DFC Bank Limited. A company has approached the branch for a request to sanction credit facilities worth ₹10 crore for meeting usual business requirements. It is a prospective new client. She checks past history of the company, back ground of promoters & directors, shareholding pattern and nature of business. Assessment of financial results of past years and future projections is also undertaken. She also carries out SWOT analysis of the company.
- Besides, assessment of net worth of directors is also undertaken. Status of CIBIL score and position of name of promoters/directors in RBI defaulter list is also verified.
- She also makes discreet inquiries from few clients of the branch engaged in similar line of activity regarding credit worthiness of company, its promoters and directors.
- Based on above-
- (a) Identify activity being performed by CA Sanjana and discuss its nature.
- (b) Would your answer be different if this activity was to be performed by a person not qualified as a Chartered Accountant? Can a non-CA perform such activity? State reason.

(c) Name any three other areas where identified activity can be undertaken.

### Peer Review and Quality Review

23. Secretarial staff of the Quality Review Board (QRB) is in the process of preparing a panel for submission to Board to enable it to initiate reviews of the quality of audit services provided by members of ICAI. The draft panel has been prepared by Mr. P, a junior staff in QRB secretariat and it has moved up in hierarchy for vetting by a senior staff, Mr. R, before being put up in the upcoming meeting of Quality review board for its consideration.

The draft panel contains details of following entities audited by different audit firms: -

Name of entity	Listing status	Sector	Paid up capital*	Annual turnover*	Outstanding loans & deposits*	Name of audit firm
XYZ Ltd.	Unlisted Public	Education technology	450	1200	450	BB & Co.
PQR Ltd.	Listed in BSE, NSE and NYSE	Manufacturing	1000	5000	750	GPR & Co.
X Insurance Ltd.	Unlisted	Health insurance	250	1500	400	DS & Co.
AAZ Ltd.	Unlisted	Manufacturing	200	800	200	CT & Co.

\* Figures are of immediately preceding year and are in ₹ Crore.

Is the inclusion of names of audit firms of corresponding entities in the draft panel to be put up before QRB appropriate? Guide Mr. R.

### Professional Ethics

24. Mr. S is a practising chartered accountant based out of Chennai. During the weekends, he involved himself in equity research and used to advise his friends, relatives and other known people who are not his clients. Apart from this, he was also involved as a paper-setter for Accountancy subject in the school in which he studied. He also owned agricultural land and was doing agriculture during his free time. During the year 20X1, heavy losses were incurred in agricultural activity due to natural calamities and misfortune, and he lost almost all of his wealth and became undischarged insolvent. After a few court hearings, finally, in the year 20X3, he was declared discharged insolvent and obtained a certificate from the court stating that his insolvency was caused by misfortune without any misconduct on his part. You are required to comment on the above situation with reference to the Chartered Accountants Act, 1949 and Schedules thereto, (especially from the point of section 8: Entry of name in Register of Members).

25. Write a short note on the following:
- (a) Categorisation of NBFCs carrying out specific activity.
  - (b) Role of the Risk Management Committee.
  - (c) Qualities of Operational Auditor.

### SUGGESTED ANSWERS

#### PART A : ANSWERS TO MULTIPLE QUESTIONS

- 1. (a)
- 2. (a)
- 3. (b)
- 4. (c)
- 5. (c)
- 6. (d)
- 7. (b)
- 8. (a)
- 9. (d)
- 10. (c)

#### PART B : DESCRIPTIVE QUESTIONS

11. **Responding When the Auditor Concludes That a Material Misstatement of the Other Information Exists:** As per SA 720, "The Auditor's Responsibility in Relation to Other Information", 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 in the given case are given hereunder:**

As per SA 720, "The Auditor's Responsibility in Relation to Other Information", 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.

Contention of the partner of the firm that auditors are not concerned with such disclosures made by the management in its annual report, is incorrect.

12. In the given case situation, auditor has to verify trade receivables for half year ending 30<sup>th</sup> September, 2021. Such a process/exercise is only a fact finding and reporting exercise. The auditor has to report the facts as these are. Like, he would have to state whether confirmation from a particular debtor has been received or not.

The auditor can issue an assurance report in case of audit and review engagements. By providing assurance, the auditor provides comfort to users of financial statements. Assurance in the above context refers to the auditor's satisfaction as to the reliability of an assertion made by one party for use by another. To provide such assurance, the auditor assesses the evidence collected as a result of procedures conducted and expresses a conclusion. The degree of satisfaction achieved and, therefore, the level of assurance which may be provided is determined by the procedures performed and their results.

However, the types of services described in the given situation falls in the *related services* domain. These are, in the nature, of agreed-upon procedures to be carried out by the auditor. The auditor cannot issue an assurance report while providing such kind of services. He can only issue a report stating facts as they are without providing any sort of assurance. He can report only facts.

Therefore, the auditor *cannot* give a report providing assurance for such type of services. He can only issue a factual report.

13. (a) **As per SA 210** Agreeing the Terms of Audit Engagements The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate.

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

- (i) The objective and scope of the audit of the financial statements;
- (ii) The responsibilities of the auditor;
- (iii) The responsibilities of management;
- (iv) Identification of the applicable financial reporting framework for the preparation of the financial statements; and
- (v) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.

- (b) As per SA 620, Using the work of an Auditor's Expert, the nature, scope and objectives of the auditor's expert's work may vary considerably with the circumstances, as may the respective roles and responsibilities of the auditor and the auditor's expert, and the nature, timing and extent of communication between the auditor and the auditor's expert. It is therefore required that these matters are agreed between the auditor and the auditor's expert.

In certain situations, the need for a detailed agreement in writing is required like -

- The auditor's expert will have access to sensitive or confidential entity information.
- The matter to which the auditor's expert's work relates is highly complex.
- The auditor has not previously used work performed by that expert.
- The greater the extent of the auditor's expert's work, and its significance in the context of the audit.

In the given case, considering the complexity involved in the valuation and volume of derivatives and also due to the fact that the auditor and auditor's expert were new to each other, auditor should have signed a formal agreement/ engagement letter with the auditor's expert in respect of the work assigned to him.

14. (a) Guidance to CA Gautam with well defined set of Standard Operating Procedure is given hereunder:

- (i) Standard Operating Procedures (SOPs): A well defined set of SOPs helps define role, responsibilities, process & controls & thus helps clearly communicate the operating controls to all touch points of a process. The controls are likely to be clearly understood & consistently applied even during employee turnover.
- (ii) Enterprise Risk Management: An organization which has robust process to identify & mitigate risks across the enterprise & its periodical review will assist in early identification of gaps & taking effective control measures. In such organizations, surprises of failures in controls is likely to be few.
- (iii) Segregation of Job Responsibilities: A key element of control is that multiple activities in a transaction/decision should not be concentrated with one individual. Segregation of duties is an important element of control such that no two commercial activities should be conducted by the same person.

A buyer should not be involved in receiving of materials or passing of bills. Similarly bank reconciliation should be prepared by a person other than the one who maintains bank book

- (iv) Job Rotation in Sensitive Areas: Any job carried out by the same person over a long period of time is likely to lead to complacency & possible misuse in sensitive areas. It is therefore important that in key commercial functions, the job rotation

is regularly followed to avoid degeneration of controls. For example, if the same buyer continues to conduct purchase function for long period, it is likely that he gets into comfort zone with existing vendors & hence does not exercise adequate controls in terms of vendor development, competitive quotes etc.

- (v) **Delegation of Financial Powers Document:** As the organization grows, it needs to delegate the financial & other powers to their employees. A clearly defined document on delegation of powers allows controls to be clearly operated without being dependent on individuals.
  - (vi) **Information Technology based Controls:** With the advent of computers & enterprise resource planning (ERP) systems, it is much easier to embed controls through the system instead of being human dependent. The failure rate for IT embedded controls is likely to be low, is likely to have better audit trail & is thus easier to monitor. For example, at the stage of customer invoicing, application of correct rates in invoices or credit control can all be exercised directly through IT system improving control environment.
- (b) In the given case of Acharya Ltd, Auditors, while conducting audit has come across significant deficiency existing in the internal control system and also auditors wanted to ascertain that deficiency.

As per SA 265, “Communicating Deficiencies in Internal Control to Those Charged with Governance and Management “, Indicators of significant deficiencies in internal control include, for example:

- (i) Evidence of ineffective aspects of the control environment, such as:
  - (a) Indications that significant transactions in which management is financially interested are not being appropriately scrutinised by those charged with governance.
  - (b) Identification of management fraud, whether or not material, that was not prevented by the entity's internal control.
  - (c) Management's failure to implement appropriate remedial action on significant deficiencies previously communicated.
- (ii) Absence of a risk assessment process within the entity where such a process would ordinarily be expected to have been established.
- (iii) Evidence of an ineffective entity risk assessment process, such as management's failure to identify a risk of material misstatement that the auditor would expect the entity's risk assessment process to have identified.
- (iv) Evidence of an ineffective response to identified significant risks (e.g., absence of controls over such a risk).
- (v) Misstatements detected by the auditor's procedures that were not prevented, or

detected and corrected, by the entity's internal control.

- (vi) Disclosure of a material misstatement due to error or fraud as prior period items in the current year's Statement of Profit and Loss.
- (vii) Evidence of management's inability to oversee the preparation of the financial statements.

**15. The data analytics methods used in an audit are known as Computer Assisted Auditing Techniques or CAATs.** There are several steps that should be followed to achieve success with CAATs and any of the supporting tools. A suggested approach to benefit from the use of CAATs is as given below:

- Understand Business Environment including IT
- Define the objectives and criteria
- Identify source and format of data
- Extract Data
- Verify the completeness and Accuracy of Extracted data
- Apply Criteria on data obtained.
- Validate and confirm results.
- Report and document results and conclusions (SA 230)

**16.** As per para 1 of Companies (Auditor's Report) Order 2020, CARO 2020 is applicable to every company, including a foreign company, as defined in clause (42) of section 2 of the Companies Act 2013, except,

- (i). a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);
- (ii). an insurance company as defined under the Insurance Act, 1938 (4 of 1938);
- (iii). a company licensed to operate under section 8 of the Companies Act;
- (iv). a One Person Company as defined under clause (62) of section 2 of the Companies Act and a small company as defined under clause (85) of section 2 of the Companies Act; 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 rupees one crore as on the balance sheet date and which does not have total borrowings exceeding rupees one 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 III to the Companies Act, 2013 (including revenue from discontinuing operations) exceeding rupees ten 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 15<sup>th</sup> December to 17<sup>th</sup> 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.

- (i) As per clause (i) (e) of para 3 of CARO 2020, the auditor shall include a statement on: whether any proceedings have been initiated or pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 (45 of 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, the 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 clause (i) (e) of para 3 of CARO 2020.

- (ii) As per clause (xvii) of para 3 of CARO 2020, the 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, the 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.

17. (a) It is clear from the ageing schedule 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 creditors of the company. Most of key financial ratios are adverse.

Further, bankers have refused further debits in cash credit account due to negative drawing power from March 2022. Cash credit loans are repayable on demand. There

is no other information available how the company plans to run its business without bank finance.

Also, Further, upon inquiry with the management, it was identified that management did not have any major future contracts to boost their revenue and financial position.

All the above factors are indicators that a material uncertainty exists that may cast significant doubt on the company's ability to continue as a going concern. There is no express disclosure of this fact in financial statements.

Therefore, it is a situation where material uncertainty exists, which has cast significant doubt on company's ability to continue as going concern in accordance with SA 570, Going Concern.

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

- (b) If supplementary information that is not required by the applicable financial reporting framework is presented with the audited financial statements, the auditor shall evaluate whether, in the auditor's professional judgment, supplementary information is nevertheless an integral part of the financial statements due to its nature or how it is presented. When it is an integral part of the financial statements, the supplementary information shall be covered by the auditor's opinion.

If supplementary information that is not required by the applicable financial reporting framework is not considered an integral part of the audited financial statements, the auditor shall evaluate whether such supplementary information is presented in a way that sufficiently and clearly differentiates it from the audited financial statements. If this is not the case, then the auditor shall ask management to change how the unaudited supplementary information is presented.

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.

18. A parent which presents consolidated financial statements is required to consolidate all its components in the consolidated financial statements other than those for which exceptions have been provided in the relevant accounting standards under the applicable financial reporting framework.

The auditor should obtain a listing of all the components included in the consolidated financial statements and review the information provided by the management of the parent identifying the components. The auditor should verify that all the components have been included in the consolidated financial statements unless these components meet criterion for exclusion.

In the given case, Brilliant Ltd has provided the list of components included in the consolidated financial statements (CFSs). CA Vishudh shall verify that all the components have been included in the CFSs.

Further, in respect of completeness of this information, CA Vishudh should perform the following procedures:

- (i) review his working papers for the prior years for the known components;
  - (ii) review the parent's procedures for identification of various components;
  - (iii) make inquiries of the management to identify any new components or any component which goes out of consolidated financial statements;
  - (iv) review the investments of parent as well as its components to determine the shareholding in other entities;
  - (v) review the joint ventures and joint arrangements as applicable;
  - (vi) review the other arrangements entered into by the parent that have not been included in the consolidated financial statements of the group;
  - (vii) review the statutory records maintained by the parent, for example registers under section 186, 190 of the Companies Act, 2013;
  - (viii) Identify the changes in the shareholding that might have taken place during the reporting period.
19. Sometimes, a customer is sanctioned a cash credit limit at one branch but is authorised to utilise such overall limit at several other branches also, for each of which a sub-limit is fixed.

In such a case, the determination of status of the account as NPA or otherwise should be determined at the limit-sanctioning branch with reference to the overall sanctioned limit/drawing power and not by each of the other branches where a sub-limit has been fixed.

The auditor of the limit-sanctioning branch should examine whether it receives particulars of all transactions in the account at sub-limit branches and whether status of the account has been determined considering the total position of operation of the account at all

concerned branches. The standalone matter of no credit transactions for more than 90 days as on 31<sup>st</sup> March, 2022 at Solapur branch is irrelevant.

Hence, keeping in view above, CA. Muni should consider asset classification considering the total position of operation of the account at all concerned branches.

Regarding sub-limit at branches, the classification adopted by the limit-sanctioning branch should be followed. Hence, the Solapur branch has to follow asset classification made by the limit-sanctioning branch.

20. (a) Under Clause 16(b) of Form 3CD, proforma credits, drawbacks, refund of duty of customs or excise or service tax, or refund of sales tax or value added tax, where such credits, drawbacks or refunds are admitted as due by the authorities concerned and not credited to the profit and loss account are to be reported.

The details of the following claims, if admitted as due by the concerned authorities but not credited to the profit and loss account, are to be stated under clause 16(b).

- (i) Pro forma credits
- (ii) Drawback
- (iii) Refund of duty of customs
- (iv) Refund of excise duty
- (v) Refund of service tax
- (vi) Refund of sales tax or value added tax or GST

All relevant correspondence, records and evidence should be examined to determine whether any refund/claim has been admitted as due and accepted during the relevant financial year. The words 'admitted by the concerned authorities' would mean 'admitted by the authorities within the relevant previous year'.

Therefore, the tax auditor may need to scrutinise the relevant files or subsequent records, including copies of shipping bills, etc., relating to such refunds while verifying the particulars.

Besides, appropriate management representation should also be obtained.

- (b) A drawback of ₹5 lac is noticed as admitted by customs authorities, which has not been credited to the Statement of Profit and loss. A company has to maintain accounts on accrual basis in accordance with section 128 of Companies Act, 2013. As admitted drawback has not been credited in the statement of Profit and loss, the same should be reported under clause 16(b) of Form 3CD.
21. Section 2(45) of the Companies Act, 2013, defines a "Government Company" as a company in which not less than 51% of the paid-up share capital is held by the Central Government or by any State Government or Governments or partly by the Central



Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company.

The auditors of these government companies are firms of Chartered Accountants, appointed by the Comptroller & Auditor General, who gives the auditor directions on the manner in which the audit should be conducted by them.

In the given situation, Siddha Ltd is a company wholly owned by central government was disinvested during the previous year, resulting in 40% of the shares being held by public. The shares were also listed on the BSE. The listing of company's shares on a stock exchange is irrelevant for this purpose and hence, Mahavir's opinion is not correct.

22. (a) The activity described in the situation is Due diligence. Due diligence is a measure of prudence activity, or assiduity, as is properly to be expected from, and ordinarily exercised by, a reasonable and prudent person under the particular circumstance, not measured by any absolute standard but depending upon the relative facts of the case. It involves a careful study of financial and non-financial possibilities. It implies a general duty to take care in any transaction.

Due diligence is a process of investigation, performed by investors, into the details of a potential investment such as an examination of operations and management and the verification of material facts. It entails conducting inquiries for the purpose of timely, sufficient and accurate disclosure of all material statements/information or documents, which may influence the outcome of the transaction. Due diligence involves a careful study of the financial as well as non-financial possibilities for successful implementation of restructuring plans.

Due diligence involves an analysis carried out before acquiring a controlling interest in a company to determine that the conditions of the business conform with what has been presented about the target business. Also, due diligence can apply to recommendation for an investment or advancing a loan/credit.

- (b) There would be no difference in answer if above activity was to be performed by a person who is not a Chartered Accountant. The activity would remain due diligence. Due diligence can be performed by any person. It is not necessary that due diligence can only be carried out by a Chartered Accountant. As due diligence involves exercise of prudence and general duty to take care in any transaction, it can be undertaken by any person.
- (c) The areas where due diligence may be undertaken are: -
- (i) Corporate restructuring
  - (ii) Venture capital financing
  - (iii) Public offerings

23. Rule 3 (1) of National Financial Reporting Authority Rules, 2018 inter alia, provides that the Authority (NFRA) shall have power to monitor and enforce compliance with accounting standards and auditing standards, oversee the quality of service under sub-section (2) of section 132 or undertake investigation under sub-section (4) of such section of the auditors of the following class of companies and bodies corporate, namely: -
- (a) companies whose securities are listed on any stock exchange in India or outside India;
  - (b) unlisted public companies having paid-up capital of not less than rupees five hundred crores or having annual turnover of not less than rupees one thousand crores or having, in aggregate, outstanding loans, debentures and deposits of not less than rupees five hundred crores as on the 31<sup>st</sup> March of immediately preceding financial year;
  - (c) insurance companies, banking companies, companies engaged in the generation or supply of electricity, companies governed by any special Act for the time being in force or bodies corporate incorporated by an Act in accordance with clauses (b), (c), (d), (e) and (f) of sub-section (4) of section 1 of the Act;
  - (d) any body corporate or company or person, or any class of bodies corporate or companies or persons, on a reference made to the Authority by the Central Government in public interest; and
  - (e) a body corporate incorporated or registered outside India, which is a subsidiary or associate company of any company or body corporate incorporated or registered in India as referred to in clauses (a) to (d), if the income or net-worth of such subsidiary or associate company exceeds twenty percent of the consolidated income or consolidated net-worth of such company or the body corporate, as the case may be, referred to in clauses (a) to (d).

The Ministry of Corporate Affairs has vide their letter dated 30th January, 2019, has clarified to the Quality Review Board that in view of Sec.132 (2) of the Companies Act, 2013 r/w Rule 9(4) of NFRA Rules, 2018, the issue of QRB reviewing audits of the companies/bodies corporate specified under Rule 3 of the NFRA Rules, 2018 will only arise in case a reference is so made to QRB by NFRA, and not otherwise.

Considering the above, in the case of auditors of XYZ Ltd., PQR Ltd. and X Insurance Ltd., NFRA has power to oversee quality of services of these audit firms. However, QRB can undertake review of the quality of services of auditors of AAZ Ltd.

Therefore, inclusion of names of auditors of XYZ Ltd, PQR Ltd and X insurance Ltd. in the draft panel for consideration by QRB is not proper.

Only the inclusion of the name of the auditor of AAZ Ltd in the draft panel is proper.

24. Given situation can be visualised in following parts:

- (A) **Mr S used to involve himself in equity research and used to advise his friends, relatives and other known people:** As per the recent decisions taken by the Ethical Standards Board of ICAI, a Chartered Accountant in practice may be an equity research adviser, but he cannot publish a retail report, as it would amount to other business or occupation.

In the given case, though Mr S is involved in doing equity research and in advising people, it is clear that he does not publish any retail report of his research. Hence, this act of Mr S shall not make him guilty of professional misconduct.

- (B) Mr S is involved in paper-setting for the Accountancy subject in the school where he studied. He also owns agricultural land and does agriculture activities: As per Clause 11 of Part I of First Schedule of Chartered Accountants Act and regulation 190A of Chartered Accountants Regulations, a Chartered Accountant in practice is deemed to be guilty of professional misconduct if he engages in any business or occupation other than the profession of chartered accountant unless permitted by the Council so to engage.

Further, Regulation 190A mentions the 'Permissions granted Generally' to engage in a certain category of occupations, for which no specific permission of Council is required. Those cases include:

- Valuation of papers, acting as paper-setter, head examiner or a moderator, for any examination.
- Owning agricultural land and carrying out agricultural activities.

Therefore, in the given case, the activities of Mr S as a paper-setter and involvement in agricultural activities do not make him guilty of professional misconduct.

- (C) **Mr. S was discharged insolvent: Disabilities for the Purpose of Membership :** Section 8 of the Chartered Accountants Act, 1949 enumerates the circumstances under which a person is debarred from having his name entered in or borne on the Register of Members, If he, being a discharged insolvent, has not obtained from the court a certificate stating that his insolvency was caused by misfortune without any misconduct on his part. Here it may be noted that a person who has been removed from membership for a specified period shall not be entitled to have his name entered in the Register until the expiry of such period.

In addition, failure on the part of a person to disclose the fact that he suffers from any one of the aforementioned disabilities would constitute professional misconduct. The name of the person, who is found to have been subject at any time to any of the disabilities discussed in section 8, can be removed from the Register of Members by the Council.

In the given case, it is clearly stated that Mr S was discharged insolvent, and he has also obtained from the court a certificate stating that his insolvency was caused by misfortune without any misconduct on his part. Hence, Mr S has not violated the provisions of Section 8, and he is not debarred from having his name entered in the Register of Members.

- 25. (a) Categorisation of NBFCs carrying out specific activity:** As the regulatory structure envisages scale based as well as activity-based regulation, the following prescriptions shall apply in respect of the NBFCs
- (i) NBFC-P2P, NBFC-AA, NOFHC and NBFCs without public funds and customer interface will always remain in the Base Layer of the regulatory structure.
  - (ii) NBFC-D, CIC, IFC and HFC will be included in Middle Layer or the Upper Layer (and not in the Base layer), as the case may be. SPD and IDF-NBFC will always remain in the Middle Layer.
  - (iii) The remaining NBFCs, viz., Investment and Credit Companies (NBFC-ICC), Micro Finance Institution (NBFC-MFI), NBFC-Factors and Mortgage Guarantee Companies (NBFC-MGC) could lie in any of the layers of the regulatory structure depending on the parameters of the scale based regulatory framework.
  - (iv) Government owned NBFCs shall be placed in the Base Layer or Middle Layer, as the case may be. They will not be placed in the Upper Layer till further notice.
- (b) Role of the Risk Management Committee:** The role of the Risk Management Committee shall, inter alia, include the following:
- (i) To formulate a detailed risk management policy which shall include: (a) A framework for identification of internal and external risks specifically faced by the listed entity, in particular including financial, operational, sectoral, sustainability (particularly, ESG related risks), information, cyber security risks or any other risk as may be determined by the Committee. (b) Measures for risk mitigation including systems and processes for internal control of identified risks. (c) Business continuity plan.
  - (ii) To ensure that appropriate methodology, processes and systems are in place to monitor and evaluate risks associated with the business of the Company.
  - (iii) To monitor and oversee implementation of the risk management policy, including evaluating the adequacy of risk management systems.
  - (iv) To periodically review the risk management policy, at least once in two years, including by considering the changing industry dynamics and evolving complexity.
  - (v) To keep the board of directors informed about the nature and content of its discussions, recommendations and actions to be taken.

- (vi) The appointment, removal and terms of remuneration of the Chief Risk Officer (if any) shall be subject to review by the Risk Management Committee. The Risk Management Committee shall coordinate its activities with other committees, in instances where there is any overlap with activities of such committees, as per the framework laid down by the board of directors.
- (c) **Qualities of Operation Auditor:** The operational auditor should possess some very essential personal qualities to be effective in his work:
  - (i) In areas beyond accounting and finance, his knowledge ordinarily would be rather scanty, and this is a reason which should make him even more inquisitive.
  - (ii) He should ask the who, why, how of everything. He should try to visualise whether simpler alternative means are available to do a particular work.
  - (iii) He should try to see everything as to whether that properly fits in the business frame and organisational policy. He should be persistent and should possess an attitude of skepticism.
  - (iv) He should imbibe a collaborative and constructive approach rather than a fault-finding approach and should give a feeling that his efforts are to help to attain an improved operation and not merely fault finding.
  - (v) If the auditor succeeds in giving a feeling of help and assistance through constructive criticism, he will be able to obtain the co-operation of the persons who are involved in the operations. This will itself be a tremendous achievement of the operational auditor. He should try to develop a team comprised of people of different backgrounds. The involvement of technical people in operational auditing is generally helpful.