

## PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS

### PART – I ACADEMIC UPDATE

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

## CHAPTER 9 AUDIT OF BANKS

The Ministry of Corporate Affairs has further amended the Companies (Audit and Auditors) Rules, 2014, through the Companies (Audit and Auditors) Amendment Rules, 2021 vide notification S.O. 206(E) dated 24<sup>th</sup> March, 2021.

As per reporting requirements cast through Rule 11 of the Companies (Audit and Auditors) Rules, 2014 the auditor's report shall also include their views and comments on the following matters, namely:

- (1) whether the bank has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;
- (2) whether the bank has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;
- (3) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the bank.
- (4)
  - (i) ***Whether the management has represented that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been advanced or loaned or invested (either from borrowed funds or share premium or any other sources or kind of funds) by the banks to or in any other person(s) or entity(ies), including foreign entities ("Intermediaries"), with the understanding, whether recorded in writing or otherwise, that the Intermediary shall, whether, directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the bank ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries;***
  - (ii) ***Whether the management has represented, that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been received by the bank from any person(s) or entity(ies), including foreign entities ("Funding Parties"), with the understanding, whether recorded in writing or otherwise, that the bank shall, whether, directly or indirectly, lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Funding Party ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries; and***

- (iii) *Based on such audit procedures that the auditor has considered reasonable and appropriate in the circumstances, nothing has come to their notice that has caused them to believe that the representations under sub-clause (i) and (ii) contain any material mis-statement.*
- (5) *Whether the dividend declared or paid during the year by the bank is in compliance with section 123 of the Companies Act, 2013.*
- (6) *[Whether the bank, in respect of financial years commencing on or after the 1st April, 2022,] has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated throughout the year for all transactions recorded in the software and the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention.]*
- (Note: Students are required to refer Page no. 9.48 of Audit of Banks )

## UNIT 1 OF CHAPTER 12: AUDIT UNDER FISCAL LAWS

### Revision of Tax Audit Report [Notification No.28/2021 dated 1.4.2021]

- Section 44AB lays obligation on certain persons mentioned thereunder carrying on business or profession, to get their accounts audited before the "specified date" by a Chartered Accountant, if their turnover exceeds the stipulated threshold or in cases where they are eligible to declare income on presumptive basis, if they claim that their income is lower than the income so computed.

These persons have to furnish by the specified date, a report of the audit in the prescribed form. For this purpose, the CBDT has prescribed under Rule 6G, Forms 3CA/ 3CB and Form 3CD.

The CBDT has, vide this notification, amended Rule 6G to provide that the audit report furnished may be revised by the person by getting revised report of audit from a chartered accountant, duly signed and verified by such chartered accountant, if there is payment by such person after furnishing of report which necessitates recalculation of disallowance under section 40 or section 43B. The said revised audit report has to be furnished before the end of the relevant assessment year for which the report pertains.

#### 2. In Form 3CD:

- In PART – A for clause 8A, the following clause shall be substituted, namely: - —  
**8A Whether the assessee has opted for taxation under section 115BA/115BAA/115BAB/ 115BAC/ 115BAD?**

- (ii) In PART-B, for clause 17, the following clause shall be substituted, namely: -

Clause 17. Where any land or building or both is transferred during the previous year for a consideration less than value adopted or assessed or assessable by any authority of a State Government referred to in section 43CA or 50C, please

Details of property	Consideration received or accrued	Value adopted or assessed or assessable	Whether provisions of second proviso to subsection (1) of section 43CA or fourth proviso to clause (x) of sub-section (2) of section 56 applicable? [Yes/No] .”;

- (iii) In PART-B, in clause 18, for sub-clauses (ca) and (cb), the following sub-clauses, shall be substituted namely:-

“(ca) Adjustment made to the written down value under section 115BAC/115BAD (for assessment year 2021-2022 only).....

(cb) Adjustment made to written down value of Intangible asset due to excluding value of goodwill of a business or profession.....

(cc) Adjusted written down value.....”;

- (iv) In PART-B, for in clause 32, for sub-clause (a), the following sub-clause shall be substituted, namely:-

(a) Details of brought forward loss or depreciation allowance, in the following manner, to the extent available:

Serial Number	Assessment Year	Nature of loss/ allowance (in rupees)	Amount as returned* (in rupees)	All losses/allowances not allowed under section 115BAA/ 115BAC/ 115BAD	Amount as adjusted by withdrawal of additional depreciation on account of opting for taxation under section 115BAC/115BAD <sup>^</sup>	Amounts as assessed (give reference to relevant order)	Remarks
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)

Note: \*If the assessed depreciation is less and no appeal pending then take assessed.

<sup>^</sup>To be filled in for assessment year 2021-2022 only.”:

- (v) In PART-B, clause 36 shall be omitted.

**Students are required to refer updated chapters applicable for November 2021 examination on the below mentioned link:**

Chapter. No.	Chapter Name	Link
Chapter 5	The Company Audit	<a href="https://resource.cdn.icai.org/65691bos53002cp5.pdf">https://resource.cdn.icai.org/65691bos53002cp5.pdf</a>
Chapter 11	Audit of Non-Banking Financial Companies	<a href="https://resource.cdn.icai.org/65692bos53002cp11.pdf">https://resource.cdn.icai.org/65692bos53002cp11.pdf</a>
Chapter 13	Audit of Public Sector Undertakings	<a href="https://resource.cdn.icai.org/65693bos53002cp13.pdf">https://resource.cdn.icai.org/65693bos53002cp13.pdf</a>
Chapter 14	Liabilities of Auditors	<a href="https://resource.cdn.icai.org/65694bos53002cp14.pdf">https://resource.cdn.icai.org/65694bos53002cp14.pdf</a>

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

## PART – II : QUESTIONS AND ANSWERS

### QUESTIONS

#### PART A: MULTIPLE CHOICE QUESTIONS

##### Integrated Case Scenario 1

Kiwspace Ltd. is an unlisted public company incorporated in the year 2009, having 90 shareholders with an equity share capital of ₹ 27 lakhs. There are total four directors in its board.

For the financial year 2020-21 as well as for the quarter ended on 30<sup>th</sup> June, 2021, Kiwspace Ltd. had suffered a loss. Despite of such loss, the board of Kiwspace Ltd. declared a total interim dividend of ₹ 20 lakhs for quarter ended March, 2021 on 25<sup>th</sup> April, 2021.

The details of dividends declared by Kiwspace Ltd. during preceding financial years are tabulated, as below:-

Financial Year	Rate of Dividend Declared
2019-20	12%
2018-19	16%

2017-18	10%
2016-17	15%
2015-16	20%
2014-15	14%

The said dividend was paid to the shareholders on 10<sup>th</sup> June, 2021, through account payee cheque, by withdrawing an amount of 5% from the total free reserves available with Kiwspack Ltd. The balance of free reserves after such withdrawal fell to 20% of its paid up share capital as appearing in the latest audited financial statements.

One of the shareholders, Mr. Mahesh, had submitted a transfer deed to the company on 28<sup>th</sup> April, 2021, for registration relating to transfer of all shares held by him in Kiwspack Ltd. in the name of Mr. Govardhan, along with an authorization letter for paying the amount of dividend on his shares to Mr. Govardhan.

However, till 10<sup>th</sup> June, 2020, due to certain reasons, Kiwspack Ltd. could not register the aforesaid transfer of shares in the name of Mr. Govardhan.

The dividend remaining unpaid of ₹ 2 lakhs was transferred to the unpaid dividend account by the company on 15<sup>th</sup> June, 2021.

Kiwspack Ltd. prepared a statement on 30<sup>th</sup> September, 2021, containing the names of shareholders to whom payment of dividend had remained pending, their last known addresses and the amount of dividend to be paid to them. The said statement was placed on the same date on the company's website and also on the website approved by the Central Government for this purpose.

Rao & Co. is the statutory auditor of Kiwspack Ltd. for F.Y. 2020-21 which issued its audit report on 30<sup>th</sup> June, 2021 on the financial statements approved on 20<sup>th</sup> June, 2021.

On the basis of the abovementioned facts, you are required to answer the following MCQs:

**Question No.: (1-5)**

1. At what maximum rate, the board of Kiwspack Ltd. would have declared the interim dividend for quarter ended March, 2021?
  - (a) 10.6%.
  - (b) 12.67%.
  - (c) 14.5%.
  - (d) 15%.
2. How much amount of interest shall be payable by Kiwspack Ltd. for delay in payment of dividend to the shareholders?
  - (a) ₹ 13,151.

- (b) ₹ 8,877.
  - (c) ₹ 10,521.
  - (d) ₹ 15,781.
3. In which account, Kiwspack Ltd. would have transferred the dividend amount in relation to shares which were held by Mr. Mahesh?
- (a) Account of Mr. Mahesh.
  - (b) Account of Mr. Govardhan.
  - (c) Unpaid Dividend Account.
  - (d) Investor Education and Protection Fund.
4. How much maximum amount of fine could be levied on every director of the company who was knowingly a party to the default in payment of dividend to the shareholders?
- (a) ₹ 9,000.
  - (b) ₹ 11,000.
  - (c) ₹ 16,000.
  - (d) ₹ 1,00,000.
5. By what date, the unpaid or unclaimed dividend amount should have been transferred to Unpaid Dividend Account and also by what date, the statement in relation to details of such Unpaid Dividend should have been prepared by Kiwspack Ltd. and placed on its website?
- (a) 01<sup>st</sup> June, 2021 and 13<sup>th</sup> September, 2021, respectively.
  - (b) 25<sup>th</sup> May, 2021 and 15<sup>th</sup> July, 2021, respectively.
  - (c) 01<sup>st</sup> June, 2021 and 15<sup>th</sup> July, 2021, respectively.
  - (d) 25<sup>th</sup> May, 2021 and 13<sup>th</sup> September, 2021, respectively.

### **Integrated Case Scenario 2**

Ulip Ltd. is a public company listed on the National Stock Exchange since the year, 2015, with share capital of ₹ 150 crore.

SRS & Co. is being appointed as its statutory auditor for F.Y. 2020-21 and Mr. Raj is appointed as the engagement partner, on behalf of the firm, to conduct the said audit assignment including conducting of limited reviews and other statutory assignments.

Mr. Raj was conducting limited review for second quarter and during the same while adhering to the responsibilities as conferred upon by SA 250, "Consideration of Laws and Regulations in an Audit of Financial Statements", he evaluated the implications of non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations and concluded that withdrawal from engagement was necessary in the given

circumstances, after seeking legal advice, even though the non-compliance was not material to the financial statements but as the management or those charged with governance refrained from taking the remedial action that he considered appropriate in the circumstances. Such a withdrawal was not prohibited by any law or regulation.

Mr. Raj, on behalf of SRS & Co., brought to the notice of the Audit Committee of Ulip Ltd., all his concerns with respect to the proposed resignation, along with relevant documents.

After issuing the necessary reports, as required in the circumstances, SRS & Co gave its resignation letter to Ulip Ltd. at 1:00 p.m. on 20<sup>th</sup> November, 2021 vide its official email-id, which contained the detailed reasons for such resignation.

Such a letter was forwarded to the stipulated authority by Ulip Ltd. at 4:00 p.m. on 21<sup>st</sup> November, 2021 vide its official email-id.

SRS & Co. filed the statement with respect to its resignation as a statutory auditor in prescribed form with Ulip Ltd. and the Registrar on 15<sup>th</sup> January, 2021, respectively, after receiving a notice from MCA.

For the purpose of filling the casual vacancy in the office of auditor, the Audit Committee of Ulip Ltd. gave recommendation of an audit firm for being appointed as the statutory auditor to which the Board disagreed and it referred back the recommendation to the committee for reconsideration citing reasons for such disagreement.

However, the Audit Committee, after considering the reasons given by the Board, decided not to reconsider its original recommendation, so, the Board of Ulip Ltd. after recording the reasons for its disagreement with the committee appointed Chavda & Co. as its new statutory auditor on 15<sup>th</sup> December, 2021.

Such an appointment of Chavda & Co. was also approved by the members of Ulip Ltd. at a duly convened general meeting on 3<sup>rd</sup> February, 2022.

On the basis of the abovementioned facts, you are required to answer the following MCQs:

**Question No.: (6-10)**

6. Whether the reasons for withdrawal from the engagement by SRS & Co. can be considered to be justifiable in the light of the fact that the non-compliance was not material to the financial statements?
- (a) Yes, as such a withdrawal was not prohibited by any law or regulation.
  - (b) Yes, as the auditor had obtained legal advice for the same and also such a withdrawal was not prohibited by any law or regulation.
  - (c) Yes, in exceptional cases, the auditor may consider for such withdrawal provided that such a withdrawal is not prohibited by any law or regulation.
  - (d) Yes, as it does not matter whether non-compliance is material or not, management or those charged with governance should not refrain from taking the remedial action

which the auditor has considered necessary, provided that such a withdrawal is not prohibited by any law or regulation.

7. In continuation of Question no. 6, above, if it is assumed that the auditor was prohibited by any law or regulation from such withdrawal from engagement, then how he would have reported the non-compliance in the audit report?
  - (a) In the "Basis for Qualified Opinion" paragraph.
  - (b) In the Other Matter(s) paragraph.
  - (c) In the Emphasis of Matter(s) paragraph.
  - (d) In the "Basis for Disclaimer of Opinion" paragraph.
8. Ulip Ltd. was required to disclose to which authority, the detailed reasons for resignation of the auditor and by what time limit as per LODR 2015?
  - (a) Such reasons were required to be disclosed to MCA till 1:00 p.m. – 21<sup>st</sup> November, 2021.
  - (b) Such reasons were required to be disclosed to NSE & SEBI till 1:00 p.m. – 23<sup>rd</sup> November, 2021.
  - (c) Such reasons were required to be disclosed to NSE till 1:00 p.m. – 21<sup>st</sup> November, 2021.
  - (d) Such reasons were required to be disclosed to the Registrar till 1:00 p.m. – 22<sup>nd</sup> November, 2021.
9. What could be the penalty specified under the Company Act, 2013 that could be levied upon SRS & Co. for failure in filing the statement with respect to its resignation, within the prescribed time limit, with Ulip Ltd. and the Registrar, respectively, if its remuneration was ₹ 40,000?
  - (a) ₹ 62,500.
  - (b) ₹ 50,000.
  - (c) ₹ 40,000.
  - (d) ₹ 52,500.
10. What was the last date available with board of Ulip Ltd. for filing the casual vacancy in the office of the auditor and by what last date, the general meeting for approving the auditor as appointed by the board should have been made in accordance with the provisions of the Companies Act, 2013?
  - (a) 27<sup>th</sup> November, 2021 and 27<sup>th</sup> February, 2022.



- (b) 20<sup>th</sup> December, 2021 and 15<sup>th</sup> February, 2022.
- (c) 20<sup>th</sup> January, 2021 and 20<sup>th</sup> April, 2022.
- (d) 20<sup>th</sup> December, 2021 and 15<sup>th</sup> March, 2022.

## **PART B : DESCRIPTIVE QUESTIONS**

### **Standards on Auditing, Statements and Guidance Notes**

11. The audit report of Kolsi (P) Ltd. for F.Y. 2020-21 was issued by Bishnoi & Co. on 25<sup>th</sup> July, 2021. However, a case was filed against Kolsi (P) Ltd. on 4<sup>th</sup> August, 2021, with the Civil Court, with respect to an incident caused in its factory on 17<sup>th</sup> January, 2021, the outcome of which may result in paying heavy penalty by Kolsi (P) Ltd.

Mr. Raj Bishnoi, the partner of Bishnoi & Co., discussed the said matter with the management and it was determined to amend the financial statements for F.Y. 2020-21. Further, Mr. Raj inquired how the management intended to address the said matter in the financial statements to which he was told that the said matter was going to be disclosed as a "Contingent Liability for a Court case" to the foot note in the balance sheet with no additional disclosures.

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

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

- (a) Whether Mr. Raj on behalf of Bishnoi & Co., has properly adhered to his responsibilities in accordance with SA 560, on becoming aware of the court case filed against Kolsi (P) Ltd.?
  - (b) Whether the contention of management of Kolsi (P) Ltd. is valid with respect to the disclosure of the court case in the financial statements?
12. While formulating the audit plan and responding to the risks of material misstatement identified and assessed in related party transaction and relationships, Ms. K the engagement manager of the audit team of ABC Limited, decided to rely upon the internal controls placed for identification and disclosure of related party relationships and transactions in accordance with the applicable financial reporting framework.

You are requested to guide Ms. K regarding the necessity to test the controls to obtain sufficient and appropriate audit evidence. Also guide, whether Ms. K can use the audit evidence obtained, regarding operative effectiveness of control on identification and disclosure of related party relationships and transactions, in the interim period.

**The Company Audit & Audit Report**

13. AB & Co. were appointed auditors for NOME Limited, a listed company, for the term of two five consecutive years from 2010-11, 2011-12, 2012-13, 2013-14, 2014-15, 2015-16, 2016-17, 2017-18, 2018-19, 2019-20. As per the provision of the section 139(2)(b) "No listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint an audit firm as auditor for more than two terms of five consecutive years".

Hence, Management of NOME Limited reached out (based on the recommendation of Audit Committee) to BCD & Co. for their nomination as the appointment of Statutory Auditor for the financial year 2020-21. However, BCD & Co. did not provide any written consent to such appointment neither they provided a certificate that the appointment, if made, shall be in accordance with the conditions laid in the Act and Rules therein.

Still the management went ahead and proposed an appointment in AGM and BCD & Co. were appointed as an auditor for the financial year 2020-21. Post appointment, those charged with governance identified that majority of the partners in the BCD & Co. are same which were there in AB & Co. Now, fearing the contravention of the provision of Companies Act, 2013. Management, on guidance of those charged with governance, decided to file a complaint with tribunal under section 140(5) of the Companies Act against statutory auditors.

You are required to guide the BCD & Co. regarding the contravention of the provisions of the Companies Act, 2013 with respect to appointment of Auditor.

14. Mr. Hemant Ramsey was appointed as the engagement partner for conducting the audit of Kshetra Lap Ltd. for F.Y. 2020-21, on behalf of Ramsey & Associates. Mr. Vishay Tyagi was appointed as the engagement quality control reviewer by the firm for the said audit.

During F.Y. 2020-21, there was an implementation of ERP system in a phased manner, in Kshetra Lap Ltd. due to which some of its business processes got automated. As a result of the implementation of such a system, there was a significant effect on the auditor's overall audit strategy. Mr. Hemant discussed the implementation of such a system with Mr. Vishay and also told him that such a matter may be a key audit matter to be reported in the audit report.

Mr. Vishay considered the significance of such matter but however he was of the opinion that such a matter did not appear to link with the matters disclosed in the financial statements and so there was no need to disclose such matter as a key audit matter.

Whether the contention of Mr. Vishay is proper with respect to the matters to be communicated as a key audit matter?

**Audit Committee and Corporate Governance**

15. Kayask Ltd. is a public company which got listed on BSE and NSE in the F.Y. 2015-16 and is amongst the top 500 listed entities on the basis of market capitalization. JP Bhuj & Co., a CA firm, has been appointed as its statutory auditor for the F.Y. 2020-21.

Mr. Pankaj Bhuj was assigned its audit as an engagement partner and he was verifying the composition of the Board of Director because of some changes in the same. The present composition of the Board of Kayask Ltd. is as follows: -

- (1) There are 9 directors out of which there are 4 non-executive directors and 3 independent directors. The board has only one woman director and she is an executive director.
- (2) Mr. Madhusudan Mehra has been appointed as the non-executive chairperson of the Board. He is brother in law of the Managing Director of Kayask Ltd.

Whether present composition of the board of Kayask Ltd. complies with the requirement of the provisions of SEBI LODR Regulations?

**Audit of Banks & Insurance Company**

16. (a) Gupta & Co. has been appointed as a statutory auditor of TCB Bank Ltd., a private sector bank, registered with RBI. Mr. Kaival Gupta, the engagement partner, while performing the audit as per the checklist, noted down the following points, which would be part of the audit queries, as tabulated below:

Sr. No.	Queries
1	Interest on State Government Guaranteed advance has been taken to income even though such advance has remained overdue for more than 90 days.
2	There is an account for which an ad hoc limit has not been reviewed for 180 days from the date of such ad hoc sanction and such account has been treated as a performing asset in the books.
3	One of the NPAs was sold for a value higher than the net book value. Profit was not recognized but the excess provision in respect of the same has been reversed.
4	In case of one of the accounts, an additional temporary limit has been sanctioned for 25% of the existing limit and for 120 days tenure.
5	On verification of outstanding forward exchange contracts, the 'net position' in respect of one of the foreign currencies was not squared and was uncovered by a substantial amount.

You are required to provide the reasons due to which such queries would have been raised by Mr. Kaival and describe the actions that may be taken by the person responsible on behalf of TCB Bank Ltd. for solving such queries.

- (b) You have been appointed to carry out the audit of 'The Blue Insurance Company Ltd.' for the year 2019-20. In the course of your audit, you observed that the commission paid to agents constituted a major expense in operating expenses of the Company. Enumerate the audit concerns that address to the assertions required for the Auditor to ensure the continued existence of internal control as well as fairness of the amounts in accounting of commission paid to agents.

#### Audit under Fiscal Laws

17. UT & Co. is a Chartered Accountant Firm, that provides consultancy services. Recently, it got queries from different clients with respect to applicability of tax audit provisions to their businesses.

In response to such queries, UT & Co., asked from them details such as turnover, total receipts and total payments made during the year respectively along with mode of receipt/payment, whether filing return of Income under normal tax provisions or presumptive tax provisions such as section 44AD, 44AE, etc.

So, in the trailing mail, UT & Co., got the aforesaid details from different clients, which it classified into following categories for ease of framing an opinion, as follows:

Client Sr. No.	Turnover (₹ in crore)	% of Cash Receipts in Total Receipts	% of Cash Payments in Total Payments	Remarks
1	4.5	5%	5%	Has been filing return as per the regular provisions of income tax.
2	1.8	7%	4%	Has declared business income as per presumptive taxation under section 44AD of the Income-tax Act, 1961.
3	0.85	6%	4%	Has declared business income as per presumptive taxation under section 44AD of the Income-tax Act, 1961 during last 2 previous years but during current previous year has declared income lower than as per section 44AD and the total

				income is less than basic exemption limit.
4	3.2	8%	6%	Has declared business income as per presumptive taxation under section 44AE of the Income-tax Act, 1961 during last 4 previous years but during current previous year has declared income lower than as per section 44AE and the total income is less than basic exemption limit.

On behalf of UT & Co., please provide your opinion, along with reasons, as a consultant in case of aforesaid clients that whether tax audit is applicable to them or not?

#### PEER REVIEW

18. (a) Roshan, a practicing Chartered Accountant is appointed to conduct the peer review of another practicing unit. What areas Roshan should review in the assessment of independence of the practicing unit?
- (b) You are required to classify the following practice units into Level I entity or Level II entity for the purpose of peer review along with providing the reason for such classification, assuming the services have been undertaken in the period under review by such CA firms:

Name of the Firm	Data of assurance services provided by such firms
MT & Co.	Conducted statutory audit of a private company which is an associate of a company, the net worth of which is ₹ 300 crore.
GBL & Co.	Conducted statutory audit of a Mutual Fund Company.
IML & Associates	Conducted statutory audit of a company registered under Section 8 of the Companies Act, 2013 but is not covered as a public interested entity. However, it has raised a contribution of ₹ 60 crore.
BTS & Co.	Conducted statutory audit of an unlisted public company having net worth of ₹ 4 crore and turnover of ₹ 55 crore. The net worth of its parent company is ₹ 325 crore.

TJK & Associates	Conducted statutory audit of LLP which has raised has a loan of ₹ 35 crore from a bank and a loan of ₹ 10 crore from an NBFC, respectively.
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- (c) Evaluating the professional judgment exercised by the auditor is one of the important aspects under Quality review, please explain the situation with reference to applicable SA.

### Professional Ethics

19. The Director (Discipline) of the ICAI received information of alleged misconduct against Mr. Jayprakash, the proprietor of JP & Associates, as follows:-

- (i) Audit of a college was accepted by JP & Associates in which Mr. Jayprakash is working as a part-time lecturer and also, he had not taken permission of the ICAI for working as a part-time lecturer in the college.
- (ii) An event relating to Corporate Social Responsibility was sponsored by JP & Associates, whereby in the sponsorship banner, name of Mr. Jayprakash as 'CA Jayprakash, Proprietor, JP & Associates' was mentioned.

On the basis of above information and along with certain evidence against Mr. Jayprakash, he was found guilty and so he was reprimanded and a fine of ₹ 1 lakh was imposed by an order passed against him dated 12<sup>th</sup> July, 2020.

Against the said order, Mr. Jayprakash preferred an appeal with the Appellate Authority on 17<sup>th</sup> August, 2020 by submitting a statement of appeal along with the application form of appeal. During such appellate proceedings, it was discovered that the said statement of appeal contained some facts which were false to which Mr. Jayprakash admitted it to be false and apologized for it.

- (a) Mr. Jayprakash has violated which of the provisions of the Chartered Accountants Act, 1949?
  - (b) Before which authority, the matter of Mr. Jayprakash would have been placed and what maximum punishment could have been imposed on him by the said authority in accordance with the Chartered Accountant Act, 1949?
20. Write a short note on the following:
- (a) Responsibility of holding company for preparation of Consolidated Financial Statements.
  - (b) Summary Written Report.
  - (c) Direction by Tribunal in case auditor acted in a fraudulent manner.
  - (d) Example of Headings of a Due Diligence Report.

**SUGGESTED ANSWERS/HINTS****PART A : ANSWERS TO MULTIPLE QUESTIONS**

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

**PART B**

11. (a) As per SA 560, 'Subsequent Events', the auditor has no obligation to perform any audit procedures regarding the financial statements after the date of the auditor's report. However, when, after the date of the auditor's report but before the date the financial statements are issued, a fact becomes known to the auditor that, had it been known to the auditor at the date of the auditor's report, may have caused the auditor to amend the auditor's report, the auditor shall:
- (1) Discuss the matter with management and, where appropriate, those charged with governance.
  - (2) Determine whether the financial statements need amendment and, if so,
  - (3) Inquire how management intends to address the matter in the financial statements.

In the given case, on becoming aware of the court case filed against Kolsi (P) Ltd., Mr. Raj discussed the said matter with the management and it was determined to amend the financial statements. Also, he inquired how the management intended to address the said matter in the financial statements.

However, If management does not take the necessary steps to ensure that anyone in receipt of the previously issued financial statements is informed of the situation and does not amend the financial statements in circumstances where Mr. Raj (hereinafter referred as 'the auditor') believes they need to be amended, the auditor shall notify

management and, those charged with governance (unless all of those charged with governance are involved in managing the entity), that the auditor will seek to prevent future reliance on the auditor's report. If despite such notification the management or those charged with governance do not take these necessary steps, the auditor shall take appropriate action to seek to prevent reliance on the auditor's report in accordance with SA 560.

- (b) As per SA 706, 'Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report', an Emphasis of Matter paragraph is not a substitute for:
- (a) A modified opinion in accordance with SA 705 (Revised) when required by the circumstances of a specific audit engagement;
  - (b) Disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation; or
  - (c) Reporting in accordance with SA 570 (Revised) when a material uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern.

In the given case, the management of Kolsi (P) Ltd. has presumed that as the auditor was going to provide a description of the said court case and its outcome in the 'Emphasis of Matter' paragraph in his amended audit report, there was no further need for it to provide additional disclosures about the court case in the financial statements.

The said contention of management of Kolsi (P) Ltd. is not valid as 'Emphasis of Matter' paragraph cannot be used as a substitute for disclosures required to be made in the financial statements as per the applicable financial reporting framework or that is otherwise necessary to achieve fair presentation, which is the responsibility of the management.

12. As per SA 550, "Related Parties", according to para on "Responses to the risks of material misstatement associated with related party relationships and transactions", the auditor should design and performs further audit procedures to obtain sufficient appropriate audit evidence about the assessed risks of material misstatement associated with related party relationships and transactions.

Further, as per SA 330, "The Auditor's Responses to Assessed Risks", the auditor shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls when:



- (a) the auditor's assessment of risks of material misstatement at the assertion level includes an expectation that the controls are operating effectively (i.e., the auditor intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures); or
- (b) Substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.

In designing and performing tests of controls, the auditor shall obtain more persuasive audit evidence the greater the reliance the auditor places on the effectiveness of a control. Moreover, the auditor shall test controls for the particular time, or throughout the period, for which the auditor intends to rely on those controls, subject to when the auditor obtains audit evidence about the operating effectiveness of controls during an interim period, and the timing of test of controls over significant risks, in order to provide an appropriate basis for the auditor's intended reliance.

When the auditor obtains audit evidence about the operating effectiveness of controls during an interim period, the auditor shall:

- (a) Obtain audit evidence about significant changes to those controls subsequent to the interim period; and
- (b) Determine the additional audit evidence to be obtained for the remaining period.

In the current case, Ms. K shall design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of relevant controls as she intends to rely on the operating effectiveness of controls in determining the nature, timing and extent of substantive procedures.

Further, she is also required to obtain the audit evidence about significant changes to those controls subsequent to the interim period along with the additional audit evidence to be obtained for the remaining period in accordance with the requirements of Standards on Auditing as discussed above.

- 13.** As per section 139(1) of the Companies Act, 2013, every company shall, at the first annual general meeting, appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting and the manner and procedure of selection of auditors by the members of the company at such meeting shall be such as may be prescribed.

It may be noted further that before such appointment is made, the written consent of the auditor to such appointment, and a certificate from him or it that the appointment, if made, shall be in accordance with the conditions as may be prescribed, shall be obtained from the auditor.

It may also be noted that the certificate shall also indicate whether the auditor satisfies the criteria provided in section 141 of the Companies Act, 2013.

Further, as per section 139(2), “(2) No listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint (a) an individual as auditor for more than one term of five consecutive years; and (b) an audit firm as auditor for more than two terms of five consecutive years.

It may also be noted further that as on the date of appointment no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years:”

In the current case, while appointing the auditors of the company a written consent of the auditor to such appointment was not obtained. Moreover a certificate from him that the appointment if made shall be in accordance with the conditions laid down in the Act and Rules was also not obtained. Further, majority of the partners of AB & Co. were partners in BCD & Co. AB & Co. already served two terms of five consecutive years i.e., from 2010-11 to 2019-20 as a statutory auditor of the company.

Hence, BCD & Co. were not eligible to be appointed as an auditor of NOME Limited as all partners of BCD & Co are partner of AB & Co. who have already served two terms of five consecutive years as an auditor of NOME Limited. Since, before the appointment of Statutory Auditor, the management should have obtained the required certification and written consent from BCD & Co., therefore, in this case both, the management and the auditors have contravened the provision of the Companies Act, 2013 as a result fine as per section 147 of Companies Act will be applicable i.e. if any of the provisions of sections 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees. If an auditor of a company contravenes any of the provisions of section 139, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees, but which may extend to five lakh rupees or four times the remuneration of the auditor, whichever is less.

It may be noted that if an auditor has contravened such provisions knowingly or willfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than fifty thousand rupees, but which may extend to twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less.

14. As per SA 701, 'Communicating Key Audit Matters in the Independent Auditor's Report', the auditor shall determine, from the matters communicated with those charged with governance, those matters that required significant auditor attention in performing the audit. In making this determination, the auditor shall take into account the following:
- (i) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315.
  - (ii) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
  - (iii) The effect on the audit of significant events or transactions that occurred during the period.

The auditor shall determine which of the aforesaid matters considered were of most significance in the audit of the financial statements of the current period and therefore are the key audit matters.

These aforesaid considerations focus on the nature of matters communicated with those charged with governance. Such matters are often linked to matters disclosed in the financial statements and are intended to reflect areas of the audit of the financial statements that may be of particular interest to intended users.

The fact that these considerations are required is not intended to imply that matters related to them are always key audit matters; rather, matters related to such specific considerations are key audit matters only if they are determined to be of most significance in the audit.

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

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

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

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

**15. As per Regulation 17 and 17A of the SEBI LODR Regulations, -**

- ✓ The auditor should ascertain whether, throughout the reporting period, the Board of Directors comprises an optimum combination of executive and non-executive directors, with at least one woman director and not less than 50% of the Board of Directors comprising non-executive directors.

It may be noted that the Board of directors of the top 1000 listed entities shall have at least one independent woman director.

- ✓ The auditor should also verify that where the Chairperson of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors.
- ✓ 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.

As per the term "relative" defined under the Companies Act, 2013 – Brother-in-law i.e. sister's husband is not included.

In the given case, Kayask Ltd. is a public company which got listed on BSE and NSE in the F.Y. 2015-16 and is amongst the top 500 listed entities on the basis of market capitalization. The present composition of the board of Kayask Ltd includes 9 directors out of which there are 4 non-executive directors and 3 independent directors. The board has only one woman director and she is an executive director. In addition, Chairperson of the Board Mr. Madhusudan Mehra is brother in law of the Managing Director of Kayask Ltd. and has been appointed as the non-executive Chairperson.

In view of Regulation 17 and 17A of the SEBI LODR Regulations, there should at least 5 non-executive directors and 3 Independent directors as its Chairperson is a non-executive director.

Further as the company is amongst the top 500 listed entities, at least one independent woman director should be there in its board.

Thus, it can be concluded that the present composition of the board of Kayask Ltd. does not comply with the requirement of the provisions of SEBI LODR Regulations as the woman director should be an independent director and there should be 5 non-executive directors.

16. (a)

Sr. No.	Reason for such Query	Action that may be taken in response to the query
1	A State Government Guaranteed advance has to be treated as NPA even if it remains overdue for more than 90 days and in case of NPA, for the purpose of income recognition, interest on such advance should not be taken to income unless interest is realized.	Interest income recognized on such advance would be reversed and would be taken to income only when it is realized.
2	Accounts for which an ad hoc limit has not been reviewed for 180 days from the date of such ad hoc sanction, should be considered as NPA.	It's treatment in the books would be changed from performing asset to a non-performing asset from the date when such change in the treatment was required.
3	In case of sale of NPA, where the sale is for a value higher than the NBV, the auditor is required to ensure that no profit is recognized, and the excess provision has not been reversed but retained to meet the shortfall/ loss that may arise because of the sale of other non-performing financial assets.	The entry for reversal of the excess provision would be cancelled in the books and such excess provision would be retained to meet the shortfall/ loss that may arise because of the sale of other non-performing financial assets.
4	Additional temporary limit may be sanctioned, for a maximum of 20% of the existing limit and 90 days maximum tenure.	The terms of additional temporary limit in case of such account would be revised to 20% of the existing limit and for 90 days maximum tenure.
5	Net position in respect of each of the foreign currencies should be generally squared and should not be uncovered by a substantial amount.	The net "position" of the branch in relation to each foreign currency should be squared off and get covered by a substantial amount.

- (b) **Commission/Brokerage:** The commission is the consideration payable for getting the insurance business. The term 'commission' is used for the payment of consideration to get Direct business. Commission received on amount of premium paid to a re-insurer is termed 'Commission on reinsurance accepted' and is reduced from the amount of commission expenditure. The internal control with regard to commission is aimed at ensuring that commission is paid in accordance with the rules

and regulations of the company and in accordance with the agreement with the agent, commission is paid to the agent who brought the business and the legal compliances, for example, tax deduction at sources, GST on reverse charge mechanism and provisions of the Insurance Act, 1938 have been complied with.

It is a well-known fact that insurance business is solicited by insurance agents. The remuneration of an agent is paid by way of commission which is calculated by applying a percentage to the premium collected by him. Commission is payable to the agents for the business procured through them and is debited to Commission on Direct Business Account. There is a separate head for commission on reinsurance accepted which usually arise in case of Head Office. It may be noted that under section 40 of Insurance Act, 1938, no commission can be paid to a person who is not an agent of the insurance company. Commission cannot be paid in excess of the maximum rates of commission as framed by IRDAI. The rates of commission/brokerage are agreed and documented with the agent and filed with IRDAI.

**Role of Auditor:** The auditor should, *inter alia*, do the following for verification of commission:

- Ensure that commission/brokerage is not paid in excess of the limits specified by IRDAI
- Ensure that commission/brokerage is paid as per rates with the agent and rates filed with IRDAI
- Ensure that commission/brokerage is paid to the agent/broker who has solicited the business
- Ensure that the agent/broker is not blacklisted by IRDAI and is not terminated for fraud etc.
- Vouch disbursement entries with reference to the disbursement vouchers with copies of commission bills and commission statements.
- Check whether the vouchers are authorised by the officers-in-charge as per rules in force and income tax is deducted at source, as applicable.
- Test check correctness of amounts of commission allowed.
- Scrutinise agents' ledger and the balances, examine accounts having debit balances, if any, and obtain information on the same. Necessary rectification of accounts and other remedial actions have to be considered.
- Check whether commission outgo for the period under audit been duly accounted.

**17. Applicability of Tax Audit:**

Client Sr. No.	Opinion (Tax Audit applicable or not)	Reason
1	No	As the turnover is upto ₹ 5 crore, Cash Receipts and Cash Payments are upto 5% of total receipts & total payments, respectively, and has been filing return as per the regular provisions of income tax, so tax audit is not applicable.
2	No	Even though turnover exceeds ₹ 1 crore and Cash Receipts are greater than 5% of Total Receipts but as the business income has been declared as per presumptive taxation under section 44AD of the Income-tax Act, 1961, so tax audit is not applicable.
3	No	Even though business income as per presumptive taxation under section 44AD of the Income-tax Act, 1961 has been declared during last 2 previous years but has not been declared during the current previous year but as the total income is less than basic exemption limit, so tax audit is not applicable.
4	Yes	Has been declaring total income as per presumptive taxation under section 44AE of the Income-tax Act, 1961 during last 4 previous years but during current previous year has declared income lower than as per section 44AE, so tax audit is applicable.

- 18. (a) Review in the Assessment of Independence of the Practicing Unit** – The reviewer should carry out the compliance review of the five general controls, i.e., independence, maintenance of professional skills and standards, outside consultation, staff supervision and development and office administration and evaluate the degree of reliance to be placed upon them. The degree of reliance will, ultimately, affect the attestation service engagements to be reviewed.

Independence is the main quality expected of an auditor. That is the very basis for the existence of the profession of auditing. Independence is a condition of mind as well a personal character of a person. It is difficult to define but very easy to perceive. Guidance Note on Independence of Auditors clarifies that independence is of two types, viz. independence of mind and independence of appearance. The Guidance Note further states that there are certain threats to independence which are classified as self interest threats, self review threats, advocacy threats, familiarity threats and intimidation threats.

The responsibility of the Peer Reviewer, therefore, is to ascertain the existence of independence and the absence of threats to independence.

The reviewer should, therefore, check the following aspects in respect of assessment of independence of the practicing unit:

- (i) Does the practice unit have a policy to ensure independence, objectivity and integrity, on the part of partners and staff? Who is responsible for this policy?
- (ii) Does the practice unit communicate these policies and the expected standards of professional behaviour to all staff?
- (iii) Does the practice unit monitor compliance with policies and procedures relating to independence?
- (iv) Does the practice unit periodically review the practice unit's association with clients to ensure objectivity and independence?
- (v) How does the practice unit deal with the threats to independence ?

**(b) Classification of Entity as per Statement of Peer Review**

Name of Entity	Type of Entity	Reason for such classification based on the Statement of Peer Review
MT & Co.	Level I entity	A Practice Unit which has undertaken Statutory Audit of a company which is an associate of an entity having net worth of more than ₹ 250 Crores at any time during the period under Review, shall be treated as a Level I entity.
GBL & Co.	Level I entity	A Practice Unit which has undertaken Statutory Audit of a mutual fund shall be treated as a Level I entity.
IML & Associates	Level I entity	A Practice Unit which has undertaken Statutory Audit of an Entity which has raised donations and / or contributions over ₹ 50 crore during the period under Review, shall be treated as a Level I entity.
BTS & Co.	Level I entity	A Practice Unit which has undertaken Statutory Audit of a company which is a subsidiary of an entity having net worth of more than ₹ 250 Crores at any time during the period under Review, shall be treated as a Level I entity.



TJK & Associates	Level II entity	A Practice Unit which has undertaken Statutory Audit of an entity which has raised funds from public or banks or financial institutions of more than ₹ 25 crore but less than ₹ 50 crore during the period under Review, shall be treated as a Level II entity.
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- (c) **Evaluating the professional judgment exercised by the auditor:** It is also important for the Technical Reviewer (hereinafter referred as TR) to understand that “professional judgment”, as defined in SA 200, “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing” is an integral concept in the context of an audit and application of SAs in real life audit scenarios. SA 200 defines professional judgment as “the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the course of action that is appropriate in the circumstances of the audit engagement.”

The concept of “professional judgment” underscores the fact that Standards, particularly, Standards on Auditing are written to lay down the fundamental principles that would apply to an audit situation. Hence, no Standard can have straight jacketed application/solutions for all audit scenarios. Above all, the Standards on Auditing issued by the Institute of Chartered Accountants of India are principle based rather than rule based. Hence, almost all the SAs envisage exercise of professional judgment by the auditor in their application in real life audit scenarios.

The TR would need to appreciate that the exercise of professional judgment in any particular case is based on the facts and circumstances that are known to the auditor as at the time of exercising that professional judgment. Normally, exercise of professional judgement by an auditor is preceded by consultation on the relevant matters both within the engagement team and between the engagement team and others at the appropriate level within or outside the firm.

In evaluating the professional judgment exercised by the auditor, the TR should consider the following factors:

- whether the judgment reached reflects a due consideration and application of the relevant auditing and accounting principles; and
- whether the judgment is appropriate in the light of, and consistent with, the facts and circumstances that were known to the auditor up to the date of the auditor’s report. Hence, the TR and the QR Team should not, under any circumstance, use “hindsight” (i.e. perception or retrospection) in their evaluation of exercise of professional judgment by the auditor.

Since the auditor needs to exercise professional judgment throughout the audit, the latter also needs to be appropriately documented. Hence, the TR can expect to find such audit documentation as a part of the audit engagement file. It is important to note that professional judgment cannot be used by an auditor as a justification for decisions that are not otherwise supported by the facts and circumstances of the engagement or sufficient appropriate audit evidence.

**19. (a)** Mr. Jayprakash has violated following provisions of the Chartered Accountants Act, 1949:

- (i) As per Clause (4) of Part I of the Second Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he expresses his opinion on financial statements of any business or enterprise in which he, his firm, or a partner in his firm has a substantial interest.

In this connection, as per the decision of the Council of the ICAI, a Chartered Accountant should not by himself or in his firm name accept the audit of a college, if he is working as a part-time lecturer in the college.

Thus, by accepting audit of a college in which he is working as a part-time lecturer, Mr. Jayprakash has violated the restriction imposed under Clause (4) of Part I of the Second Schedule to the Chartered Accountants Act, 1949.

- (ii) As per Clause (11) of Part I of the First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be 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.

Members of the Institute in practice may engage in a part-time or full-time tutorship under any educational institution other than the coaching organization of the Institute, after obtaining the specific and prior approval of the Council in each case.

Mr. Jayprakash had not taken permission of the ICAI for working as a part-time lecturer in the college and so has violated the restriction imposed under Clause (11) of Part I of the First Schedule to the Chartered Accountants Act, 1949.

- (iii) As per Clause (6) of Part I of the First Schedule to the Chartered Accountants Act, 1949, a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he solicits clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means.

In this connection, members sponsoring activities relating to Corporate Social Responsibility may mention their individual name with the prefix “CA”. However, mentioning a firm’s name or CA Logo is not permitted.

An event relating to Corporate Social Responsibility was sponsored by JP & Associates, whereby in the sponsorship banner, name of Mr. Jayprakash as ‘CA Jayprakash, Proprietor, JP & Associates’ was mentioned. Thus, firm’s name was mentioned which is not allowed and thus, Mr. Jayprakash has violated the restriction imposed under Clause (6) of Part I of the First Schedule to the Chartered Accountants Act, 1949.

- (iv) As per Clause (3) of Part II of the Second Schedule to the Chartered Accountants Act, 1949, a member of the ICAI shall be deemed to be guilty of professional misconduct, if he includes in any information, statement, return or form to be submitted to the Institute, Council or any of its Committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority, any particulars knowing them to be false.

Mr. Jayprakash in the statement of appeal submitted with the Appellate Authority mentioned some facts knowing them to be false and thus, he has violated the restriction imposed under Clause (3) of Part II of the Second Schedule to the Chartered Accountants Act, 1949.

- (b) As Mr. Jayprakash has been alleged of misconduct falling in First as well as Second Schedule, so the matter would be placed before the Disciplinary Committee.

The maximum punishment which could have been imposed on him by the said authority would be:-

- (i) reprimanding the member.
- (ii) removing name of the member permanently or for any duration, it thinks fit.
- (iii) imposing fine upto ₹ 5,00,000.

20. (a) **Responsibility of holding company for preparation of Consolidated Financial Statements:** The responsibility for the preparation and presentation of consolidated financial statements, among other things, is that of the management of the parent. This includes:

- (a) identifying components, and including the financial information of the components to be included in the consolidated financial statements;
- (b) where appropriate, identifying reportable segments for segmental reporting;
- (c) identifying related parties and related party transactions for reporting;

- (d) obtaining accurate and complete financial information from components;
- (e) making appropriate consolidation adjustments;
- (f) harmonization of accounting policies and accounting framework; and
- (g) GAAP conversion, where applicable.

Apart from the above, the parent ordinarily issues instructions to the management of the component specifying the parent's requirements relating to financial information of the components to be included in the consolidated financial statements. The instructions ordinarily cover the accounting policies to be applied, statutory and other disclosure requirements applicable to the parent, including the identification of and reporting on reportable segments, and related parties and related party transactions, and a reporting timetable.

- (b) **Summary Written Report:** These summary reports are also referred to as '**flash reports**'. In a number of companies, the practice has developed of issuing an annual (or sometimes more frequent) report summarising the various individual reports issued and describing the range of their content. These summary reports in some cases are primarily for audit committees of Boards of Directors, but in other cases for higher level management. They are especially useful to top level managers who do not actively review the individual reports. They are also useful to the general auditor in seeing his total reporting effort with more perspective and on an integrated basis.
- (c) **Direction by Tribunal in case auditor acted in a fraudulent manner:** As per sub-section (5) of the section 140, the Tribunal either *suo motu* or on an application made to it by the Central Government or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors.

However, if the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall within fifteen days of receipt of such application, make an order that he shall not function as an auditor and the Central Government may appoint another auditor in his place.

It may be noted that an auditor, whether individual or firm, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of any company for a period of five years from the date of passing of the order and the auditor shall also be liable for action under section 447.

It is hereby clarified that the case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

**(d) Example of Headings of a Due Diligence Report**

- ◆ Executive Summary
- ◆ Introduction
- ◆ Background of Target company
- ◆ Objective of due diligence
- ◆ Terms of reference and scope of verification
- ◆ Brief history of the company
- ◆ Share holding pattern
- ◆ Observations on the review
- ◆ Assessment of management structure
- ◆ Assessment of financial liabilities
- ◆ Assessment of valuation of assets
- ◆ Comments on properties, terms of leases, lien and encumbrances.
- ◆ Assessment of operating results
- ◆ Assessment of taxation and statutory liabilities
- ◆ Assessment of possible liabilities on account of litigation and legal proceedings against the company
- ◆ Assessment of net worth
- ◆ Interlocking investments and financial obligations with group / associates companies, amounts receivables subject to litigation, any other likely liability which is not provided for in the books of account
- ◆ SWOT Analysis
- ◆ Comments on future projections
- ◆ Status of charges, liens, mortgages, assets and properties of the company
- ◆ Suggestion on ways and means including affidavits, indemnities, to be executed to cover unforeseen and undetected contingent liabilities
- ◆ Suggestions on various aspects to be taken care of before and after the proposed merger/acquisition.