

Commonly found Non-compliances in Financial Statements of Companies – Auditor’s Report and CARO, 2016

Observations related to Auditor’s Report

1. **Case:** In the financial statements of a company, the relevant abstract of Independent Auditor’s report read as under:

“Report on Other Legal and Regulatory Requirements

...

(c) The balance sheet, the statement of profit and loss, the statement of cash flows and the statement of changes in equity dealt with by this Report are in agreement with the books of account.

(d) In our opinion, the aforesaid standalone financial statements to comply with the Accounting Standards specified under Section 133 of the Act read with relevant rule issued thereunder;”

Decision: It was viewed that Annexure I to Implementation Guide on auditor’s Report under Ind AS for transition prescribes the following format of reporting:-

Report on Other Legal and Regulatory Requirements

.....

(e) In our opinion, the aforesaid standalone Ind AS financial statements comply with the Indian Accounting Standards prescribed under section 133 of the Act.”

It was noted that the Auditor has reported that the financial statements comply with ‘Accounting Standards’. Since the financial statements have been prepared under Ind AS framework, it was viewed that the auditor should have used the term ‘Indian Accounting Standards’ as per the above stated requirement of Implementation Guide.

Accordingly, it was viewed that the reporting in the auditor’s report is not in line with illustrative format given under Annexure I to Implementation Guide on Auditor’s Report under Ind AS for transition.

2. **Case:** In the financial statements of a company, the relevant abstract of Annexure B to the Auditor’s report read as under:

“Annexure B to the Independent Auditors Report of even date on the standalone Ind AS financial Statement of the (Name of holding company) Report on Internal Financial Control under Clause (i) of Sub-section (3) of Section 143 of Companies Act, 2013

We have audited the internal financial control over financial reporting of ‘Name of Holding Company’ (“The Company”) as of March 31 20XX in conjunction with our

audit of standalone Ind AS financial statement of the Company for the year ended on that date.”

Decision: It was noted that in Annexure B annexed with the Independent Auditors Report pertaining to Internal Financial Controls on Financial Reporting, the name of the holding company has been mentioned there in place of the auditee company. It was viewed that in the title as well as in the opinion paragraph the name of the holding company has been wrongly mentioned which may create confusion in mind of the readers of the financial statements.

Accordingly, it was viewed that such errors should be avoided by the auditors.

3. **Case:** In the financial statements of a company for the financial year 20XX-XX, the relevant abstract of Independent Auditor’s report and Note XX and XY read as under:

“Independent Auditor’s Report

.....

Emphasis of Matter

We draw attention to the following matters in the notes to the standalone financial statements of 31 March 2017. Our opinion is not modified in respect of this matter:

1. Note No. XX of the Financial Statements regarding non provision of interest on ECB Borrowings from XYZ Ltd. consequent to the waiver of interest.
2.
3. Note No. XY of the Financial Statements regarding Impact and Justification on the Assumption of Going Concern.”

“Note No. XX - Taking into consideration the financial health of the company, the Promoter Company has agreed for not to insist for payment till the improvement of the financial health of the Company. Therefore, the interest on ECBs for the period from 1st April 20XX to 31st March, 20XX has been waived off and has not been provided in the books of accounts.”

“Note No. XY - Consequent to the transfer and assignment of AB & CD Fields to the XYZ Limited, all assets, stores and capital work in progress lying at fields has been fully depreciated/written off being zero realizable value and the same have been charged to the Statement of Profit & Loss as Exceptional Item. The company has accumulated losses and its net worth has been fully eroded which indicate the existence of material curtailment of the operations that cast a substantial doubt on the Company’s ability to continue as a going concern.”

Decision: It was noted that section 143(3)(f) of Companies Act, 2013 and paragraph 9 of Guidance Note on Reporting under Section 143(3)(f) of Companies Act, 2013 prescribes as follows:-

“Section 143(3)(f) of Companies Act, 2013

(3) The auditor ‘s report shall also state—

...

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company.”

Paragraph 9 of Guidance Note on Reporting under Section 143 (3)(f) and (h) of the Companies Act, 2013

Auditor will need to apply professional judgement in considering matters of emphasis that may have an adverse effect on the functioning of the company. Ordinarily matters that are pervasive in nature such as going concern or matters that will significantly impact the operations of the company due to its size and nature will need to be reported under clause (f) of sub-section (3) of section 143 of the Act...

It was noted that in the ‘Emphasis of Matter’ paragraph of Independent Auditor’s Report, auditor has reported there regarding impact of non-provision of interest on going concern assumption, however, the auditor has not reported on the requirements of section 143(3)(f) under the heading of ‘Report on Other legal and Regulatory Requirements’ of the Audit Report.

Accordingly, it was viewed that the requirements of section 143(3) (f) of Companies Act, 2013 read with Guidance Note on Reporting under Section 143 (3) (f) and (h) of the Companies Act, 2013 have not been complied with.

Observations related to CARO, 2016

4. **Case:** In the financial statements of a company, the relevant abstract of paragraph (iv) of Annexure A to the Independent Auditor’s Report (reporting under CARO, 2016) reads as under:

“According to the information and explanation given to us, the Company has not made any loan, investment, and guarantees to any person specified under section 185 and section 186 of the Companies Act, 2013. Therefore, the provisions of paragraph 3(iv) of the Order are not applicable to the Company.”

Decision: It was noted that paragraph 3(iv) of the Companies (Auditor’s Report) order, 2016 requires the auditor to report as per the following:

Paragraph 3 (iv)

“In respect of loans, investments, guarantees, and security whether provisions of section 185 and 186 of the Companies Act, 2013 have been complied with. If not, provide the details thereof.”

It was noted that in paragraph (iv) of Annexure A to the Auditor’s Report, the auditor reported that the company has not made any loan, investment, and guarantees to any person specified under section 185 and section 186 of the Companies Act, 2013. It was viewed that although the auditor has reported about loans, investments and

guarantees under said paragraph but the auditor has not reported on 'security', as required under clause 3 (iv) of CARO, 2016.

Accordingly, it was viewed that the auditor has not appropriately reported on paragraph 3 (iv) of CARO, 2016.

5. **Case:** In the financial statements of a Company, the relevant abstract of the Auditor's Report under CARO, 2016 reads as under:

"vii.a) The Company is generally regular in depositing undisputed statutory dues, including Provident fund, Employees' State Insurance, Income-tax, Sales Tax, Service Tax, Customs Duty, Value Added Tax, Cess, and other material statutory dues applicable to it to the appropriate authorities except GST."

Decision: It was noted that paragraph 3(vii)(a) of the Companies (Auditor's Report) Order, 2016 requires the auditor to report as per the following:

"whether the company is regular in depositing undisputed statutory dues including provident fund, employees' state insurance, income-tax, sales-tax, service tax, duty of customs, duty of excise, value added tax, cess and any other statutory dues to the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as on the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated;"

It was noted from paragraph (vii) (a) as reproduced above that the auditor has reported that the company is regular in depositing statutory dues except GST. It was viewed that the auditor's comment under paragraph (vii)(a) of CARO, 2016 is not complete as he has not commented on other part relating to the extent of the arrears of statutory dues (GST) outstanding as on the last day of the financial year for a period of more than six months from the date, they became payable.

Accordingly, it was viewed that the requirements of CARO, 2016 have not been complied with.

6. **Case:** In the financial statements of a Company, the relevant abstract of paragraph (ix) Annexure 1 to the Auditor's Report under CARO, 2016 reads as under:

"In our opinion and according to the information and explanations given by the management and on an overall examination of the balance sheet, the monies raised by way of debt instruments in the nature of foreign currency bonds and term loans were applied for the purposes for which those were raised, though idle/surplus funds which were not required for immediate utilization have been temporarily invested in fixed deposits / mutual funds."

Decision: It was noted that paragraph 45(s) of Guidance Note on CARO , 2016 prescribes following reporting format under paragraph 3 (ix) of CARO ,2016:

“In our opinion and according to the information and explanations given to us, the Company has utilized the money raised by way of initial public offer/ further public offer (including debt instruments) and the term loans during the year for the purposes for which they were raised, except for:

Nature of the fund raised	Details of default (Reason /Delay)	Amount (Rs.)	Subsequently rectified (Yes/No) and details
.....	---”

It was noted from the auditor’s comment in aforesaid paragraph of CARO reporting that monies were raised by the company through debt instruments and term loans and some of these funds were applied for the purpose for which they were raised, however, there were certain idle funds which were not so utilized and have been temporarily invested in fixed deposits / mutual funds. It was viewed that though auditor has reported on funds not utilized for intended purposes which they were raised for, in line with paragraph 3 (ix) of CARO, 2016, however, he has not adhered to the suggested reporting format as prescribed under 45(s) of Guidance Note on CARO, 2016.

Accordingly, it was viewed that the requirements of Guidance Note on CARO, 2016 have not been complied with by the auditor.