

Practical Insights into Company Audit and Audit Trail Reporting Requirements

Presentation at the Two Day National Workshop organised by the Corporate Law & Corporate Governance Committee of ICAI and hosted by the Ernakulam Branch of SIRC of ICAI on 28 June 2024

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Auditors' Responsibility and Accounting Standards

In our opinion and to the best of our information and according to the explanations given to us, the aforesaid financial statements give the information required by the Companies Act, 2013 ('Act') in the manner so required and give a true and fair view in conformity with the Accounting Standards prescribed under section 133 of the Act read with the Companies (Accounting Standards) Rules, 2021, as amended from time to time and other accounting principles generally accepted in India

Accounting Standards specified u/s 133	Other generally accepted accounting principles	True and Fair view
Balance Sheet	Statement of Profit and Loss	Statement of Cash Flows

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Criteria for classification of Companies for applicability of AS

Level	Criteria	Turnover Limits (Excluding Other Income)
SMC	Listing	Whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India
SMC	Nature of business	Which is not a bank, financial institution or an insurance company
SMC	Turnover	whose turnover (excluding other income) does not exceed Rs.50 Crores in the immediately preceding accounting year
SMC	Borrowings	Which does not have borrowings (including public deposits) in, excess of Rs.10 Crores at any time during the immediately preceding accounting year
SMC	Other	Which is not a holding or subsidiary company of a company which is not a small and medium-sized company

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CAR 2021 – an overview

Accounting Standards	Non SMC	SMC
AS 1 to 14 (except AS 3), 15, 16, 18, 19, 20, 22, 24, 25, 26, 28 and 29	✓	✓
AS 3, 17	✓	✗
AS 21, 23 and 27 (Only if regulator requires consolidation or entity prepares consolidated financial statements)	✓	✓

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Auditors' Responsibility and Standards on Auditing

We conducted our audit in accordance with the standards on auditing specified under section 143 (10) of the Act. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement

Standards on Auditing specified u/s 143 (10)	Ethical requirements	Plan audit
Perform audit	Reasonable assurance	FS are free from Material Misstatement


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Auditor's Independence and MCA observations

Auditor's responsibility is not limited to shareholders and Audit report is a public document	Audit Report is relied on to by various stakeholders, including Financial Institutions, Government and general public	Auditor's financial or other interest in client's business inappropriately influence his judgement or behaviour
There is self interest threat due to reliance of auditor on the fee from the client	Income from other services provided by the auditor also effects how far the auditor may be influenced by the management	Audit firms quote competitive prices, not commensurate with amount necessary to undertake quality audit.

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Audit issues are now more complex



Material Uncertainty Relating to Going concern	Auditors' evaluation and reporting of Going Concern Assumption	Compliance with Laws and Regulations
Impairment testing of PPE	Expected credit loss on financial assets	Fair valuation
Inventories	Employee Costs	Accounting for deferred tax assets

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A simple approach




Understanding the client's business and its environment

Understanding the laws and regulations

Understanding the Key risks and responding to the risks

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What additionally is required?



Good understanding of the Accounting Standards	Good understanding of the Standards on Auditing	Good understanding of the Companies Act, 2013
Keeping updated with the changes in SEBI listing requirements	Keeping updated with the changes in auditor's report	Reasonable level of professional skepticism

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We often miss this – Audit Planning



Audit

Understanding The business

Risk Assessment

Responding to assessed risks

Understanding the reporting requirements


Performing audit procedures

Sufficient, appropriate audit evidence

Audit opinion on Financial Statements

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We could do this – Risk assessment




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    graph TD
      A[Understand the entity] --> B[Identify & assess risk of material misstatements]
      C[Design & implement responses to assessed risk] --> D[Reduce risk to acceptably low level]
      E[Entity's environment] --> A
      F[Entity's internal controls] --> A
      G[Fraud] --> B
      H[Error] --> B
      B --> C
      C --> D
      I[Financial statement & Assertion level] --- B
  
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We often miss this – Audit procedures



Audit Planning

Use of relevant Standards on Auditing

Application of relevant Accounting Standards

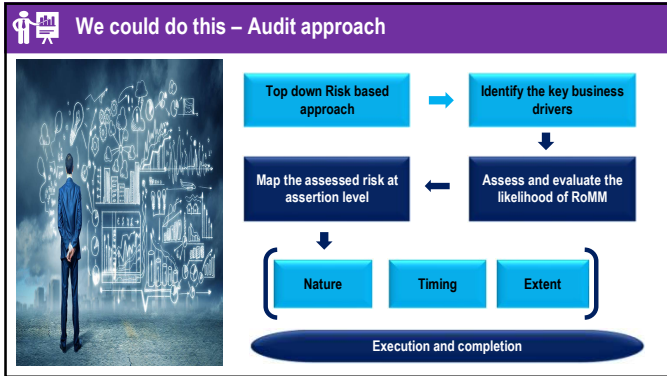
Significant Estimates

Fraud Risk

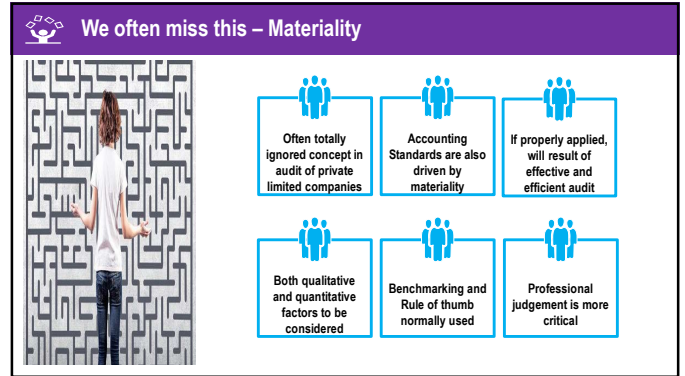
Relying on the work of others

Audit Documentation

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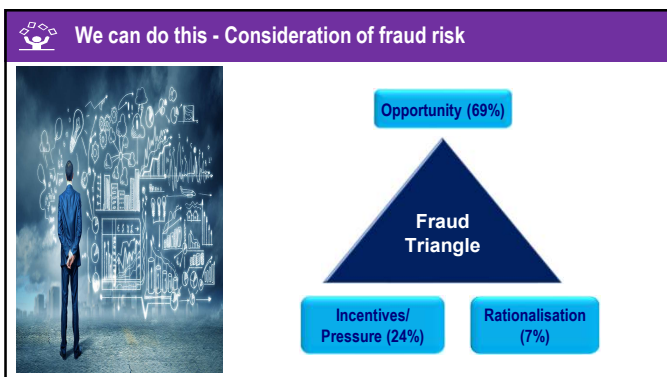
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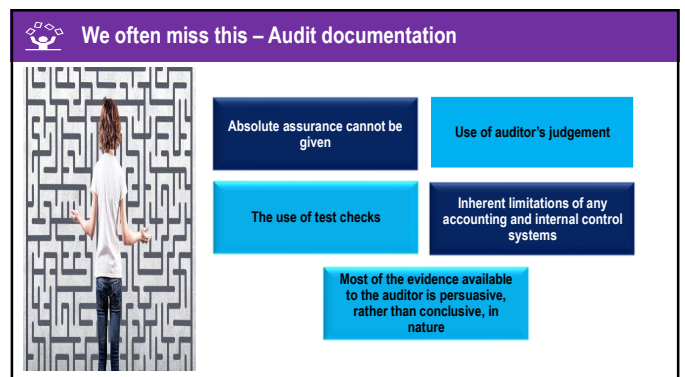
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We could do this – Audit documentation



Contemporaneous documentation	
End to end clear documentation	
Determining test objective	Definition of misstatements
Procedures performed	Exceptions identified
Evaluating exceptions	Audit conclusion and reporting

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Reporting Requirements



Reporting Requirements for a private limited Company

Reporting on audit of financial statements	Reporting on Other Legal and Regulatory Requirements
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Report on Audit of Financial Statements



Compliance with SA 700	Compliance with SA 705
Compliance with SA 706	Special focus on Going Concern Assumption

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Reporting on Other Legal and Regulatory Requirements



Reporting under Companies (Auditor's) Order 2016	Reporting on Internal Financial Controls over financial Reporting
Reporting under Section 143 (3) of the Companies Act, 2013	

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Reporting on Companies (Auditor's) Report Order 2020



Companies (Auditor's) Report Order 2020 is not applicable to a private company, if ALL the following conditions are satisfied

It is not a subsidiary or holding company of a public company	Its paid-up capital and reserves and surplus are not more than Rs.1 Crores as at the balance sheet date
Its total borrowings from banks and financial institutions are not more than Rs.1 Crores at any time during the year	Its turnover for the year is not more than Rs.10 Crores during the year

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Reporting on Internal Financial Controls over financial reporting




Reporting on Internal Financial Controls over financial reporting is not applicable to a private company, if ALL the following conditions are satisfied

Its turnover as per last audited financial statements is less than Rs.50 Crores	Its total borrowings from banks and financial institutions are less than Rs.25 Crores at any time during the year
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Reporting Requirements u/s 143 (3) of the Companies Act, 2013



- Sought and obtained all the information and explanations necessary for the purposes of our audit
- Proper books of account as required by law have been kept by the Company
- The balance sheet, the statement of profit and loss, and the cash flow statement dealt with by this report are in agreement with the books of account
- Financial statements comply with the accounting standards specified under section 133 of the Act

Directors' disqualification u/s 164 (2)	Reporting on IFC	Reporting u/s 197(16)	Matters to be reported as per Rule 11	Audit Trail (a new requirement)
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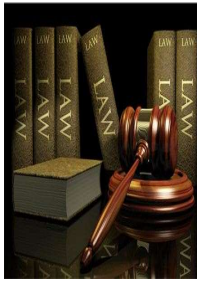
Audit Trail – what is new?



- New proviso to rule 3 (1) of the Companies (Accounts) Rules, 2014
- Implementation of Audit Trail and reporting by auditors applicable from financial year commencing on or after the April 1, 2023
- Audit Report for accounting period commencing on or after April 1, 2023 to have comment on audit trail on the face of the report
- Maintenance of Audit Trail is management responsibility but auditors all responsible for testing the same and reporting
- Increased audit procedures and time may be required

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Audit Trail - What is New?

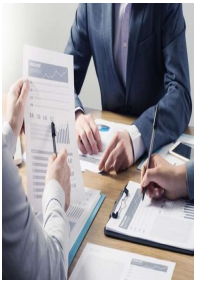


For the financial year commencing on or after April 1, 2023, every company which uses accounting software for maintaining its books of account, shall use only such accounting software which has a feature of recording audit trail of each and every transaction, creating an edit log of each change made in books of account along with the date when such changes were made and ensuring that the audit trail cannot be disabled

Every Company	Uses accounting software	For maintaining books of account
Audit Trail of each and every transaction	Edit Log of each change	Ensuring that Audit Trail cannot be disabled

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What can be traced using Edit Log



Tracking of back dated entries	Deleted Entries
Modified entries	Cash balance changes
Changes to inventory valuation	Any other changes

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Management Responsibility



Responsibility	Penalty for non compliance
<ul style="list-style-type: none"> Every company which uses an Accounting software for maintaining its books of account, should use only such accounting software which has the following features Records an Audit Trail of each and every transaction, creating an edit log of each change made in the books of account along with the date when such changes are made; and Ensuring that the Audit Trail is not disabled 	<ul style="list-style-type: none"> MD, Director in charge of Finance, CFO or any other person identified by Board Fine for non-compliance with a minimum of Rs.50,000/- to a maximum Rs.5,00,000/-

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Auditor's reporting requirements under of Rule 11 (g)




Whether the company, in respect of financial years commencing on or after the 1st April 2023, 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

Used such accounting software for maintaining books	Feature of recording audit trail (edit log) facility	Operated throughout the year for all transactions
The audit trail feature has not been tampered with	The audit trail has been preserved by the Company	As per the statutory requirements for record retention

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Frequently Asked Questions



- Whether applicable only to SFS or also applicable to CFS?
- Whether additions/ deletions made in the entries automatically results in audit qualification
- What happens if a company is recording the transaction only at the yearend in one go or using a part time accountant?
- Whether passing audit JVs will have any impact on audit trail reporting?
- What are the reporting requirements in the case of correction of a mistake?
- Whether the audit trail is required only for transactions but also for the Master Data?

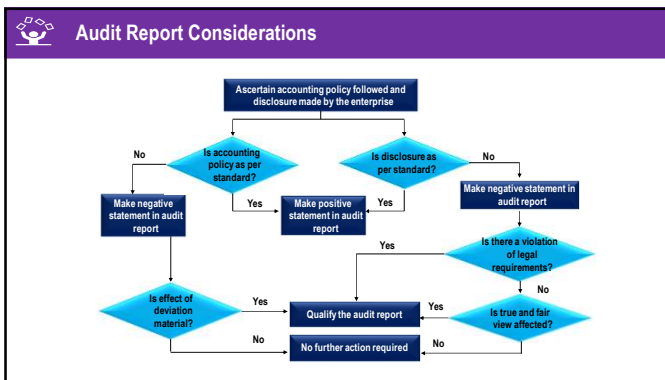
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Frequently Asked Questions



- Data corrupted/ cyber attacks and all data are recreated to maintain books of account on a full fledged basis. What is auditors reporting requirement?
- Can I rely on the work performed by an ISA auditors?
- Can I rely on the management representation and issue my audit opinion stating that I do not possess the required technical knowledge?

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Questions?



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Thank you



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