

**AUDIT CONCLUSIONS AND REPORTING[INCLUDING
ICFR]
(EMPHASIS ON PRIVATE LIMITED COMPANIES /
SMES)**

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Is Compliance of **Auditing Standards** Mandatory while doing Company Audits?

- **Basic Requirements as to Financial Statements**
- The Auditor shall make the Report after taking into account, the following –
 - the provisions of the Act,
 - **the accounting and auditing Standards,**
 - matters which are required to be included in the Audit Report under the provisions of the Act / Rules / Order u/s 143(11)
 - **best of his information and knowledge.**

- Sec. 143(9) – Every Auditor shall **comply** with the Auditing Standards.

AN OVERVIEW OF ENGAGEMENT AND QUALITY CONTROL STANDARDS

- Framework for Assurance Engagements
- Engagement Standards
- 100 – 999: Standards on Auditing(SAs)
- 100 – 199 : Introductory Matters
- 200 – 299 : General Principles & Responsibilities -9
- 300 – 499 : Risk Assessment & Response to Assessed Risks -6
- 500 – 599 : Audit Evidence -11
- 600 – 699 : Using Work of Other -3
- 700 – 799 : Audit Conclusions & Reporting -6
- 800 – 899 : Specialised Areas -3
- 2000 – 2699 : Standards on Review Engagements (SREs) -2
- 3000 – 3699 : Standards on Assurance Engagements (SAEs) 3
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CONTENTS

- **Audit Conclusion and Reporting Standards (including Going Concern Considerations)**
- **Reporting on Internal Controls**
- **CARO Considerations (for private limited companies)**

AUDIT CONCLUSION AND REPORTING STANDARDS

- SA-700 – Forming an Opinion and Reporting on Financial Statements (Revised)
- SA-705 – Modifications to the Opinion in the Independent Auditor’s Report
- SA-706 – Emphasis of Matter Paragraphs in the Independent Auditor’s Report
- SA-570 – Going Concern

SA-700 – FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS

- Objectives
- Definitions
- Forming an Opinion
- Contents

SA-700 – FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS

Objectives of the auditor :

- Form an opinion on the Financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained.
- Express clearly the above opinion through a written report that also describes the basis for the opinion



SA-700 - DEFINITIONS

- **General Purpose Financial Statements-** *Financial Statements prepared in accordance with a general purpose framework*
- **General Purpose Framework – Fair presentation framework – Compliance Framework**
- **Unmodified Opinion –** *Opinion expressed that the financial statements are prepared in all **material respects** in accordance with the applicable financial reporting framework*

SA-700 – FORMING AN OPINION

- Prepared in accordance with the financial reporting framework
- Whether sufficient appropriate audit evidence has been obtained
- Conclusion whether uncorrected misstatements are material
- Selection, disclosure and consistent application of accounting policies in accordance with the financial reporting framework
- Accounting estimates are reasonable
- Information presented is relevant, reliable, comparable, understandable to achieve a **fair presentation**
- **Type of opinion – modified, unmodified or disclaimer**

SA-700 – Contents

Old Format (Applicable till 31 March 2018)	New Format (Applicable from 1 April 2018)
Title and Addressee	Title and Addressee
Introductory Paragraph	Auditors Opinion
Management Responsibility	Basis of opinion
Auditors Responsibility	Emphasis of matter and / or other matter paragraphs (SA 706) <i>Information other than the Financial Statements and the Auditors Report</i>
Basis of opinion	Key Audit Matters (KAM) Paragraph (SA 701) (Applicable to listed entities only)
Auditors Opinion	Management Responsibilities
Emphasis of matter and / or other matter paragraphs (SA 706)	Auditors responsibilities for the audit of the Financial statements
Report on other legal and regulatory requirements	Report on other legal and regulatory requirements
Signature, date of report and membership number and place of signature	Signature, date of report and membership number, UDIN No. and place of signature

SA-700 – CONTENTS

- **Title** – Clearly state from an **independent auditor**
- **Addressee** – Depends upon the circumstances, terms of engagement and regulatory requirements
- **Opinion**- Identify the entity whose financial statements have been audited - State that the financial statements have been audited - Identify the title of each statement comprising the financial statements - Refer to the notes, including the summary of significant accounting policies; - Specify the date of, or period covered by, each financial statement comprising the financial statements
- **Basis for opinion**– **audit conducted in accordance with the SAs** - compliance with independence ethical requirements – reasonable assurance whether financial statements are free from material misstatement- use of judgement- risk of material misstatement whether due to fraud or error –opinion not expressed on effectiveness of internal controls
- **Report on Going Concern (wherever applicable in accordance with SA-570 and Key Audit Matters (not discussed)**

SA-700 – CONTENTS

- **Management's Responsibility for the financial statements** – design, implementation and maintenance of internal control – free from material misstatement whether due to fraud or error- preparation in accordance with fair presentation framework – *going concern responsibilities – Specific assertions – discussed later*
- **Auditor's Responsibility** – audit conducted in accordance with the **SAs** - compliance with ethical requirements – reasonable assurance whether financial statements are free from material misstatement- use of judgement- risk of material misstatement whether due to fraud or error –opinion not expressed on effectiveness of internal controls – *going concern appropriateness – Specific assertions – discussed later*
- **Audit Opinion**
- **Other Reporting Responsibilities** (Report on Other legal and Regulatory Requirements) (*Reporting under section 197(16) of the Act; with a specific reference that the same is not applicable to Private Limited Companies*)

KEY AMENDMENTS

- Prominent placement of the “**Auditor’s Opinion**” towards the **beginning** of the Auditor’s Report.
- New descriptions of responsibilities relating to **Going Concern** to be included in the respective sections for Management Responsibility Paragraph and Auditors Responsibilities Paragraph
- Under para “**Basis of Opinion**”; a statement that the auditor is **independent** of the entity in accordance with the **relevant ethical requirements** relating to the audit.
- Report on **Other Information**
- Management Responsibility [**new clauses**]
- Auditors’ Responsibility [**new clauses**]

BASIS OF OPINION (EARLIER UNDER AUDITOR'S RESPONSIBILITY STATEMENT)

- The auditor's report shall include a section, directly following the Opinion Section, with the heading "Basis for Opinion", that:
 - a) States that the audit was conducted in accordance with SAs
 - b) Refers to the section of the auditor's report that describes the auditor's responsibilities under the SAs;
 - c) Includes a statement that the **auditor is independent of the entity in accordance with the relevant ethical requirements** relating to the audit, and has fulfilled the auditor's other ethical responsibilities in accordance with these requirements. The statement shall **refer to the Code of Ethics issued by ICAI**
 - d) States whether the auditor believes that the audit evidence the auditor has obtained is sufficient and appropriate to provide a basis for the auditor's opinion

RESPONSIBILITIES OF THE MANAGEMENT SECTION

- This section of the auditor's report shall describe management's responsibility for:
 - a) Preparing the financial statements in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; and
 - b) Assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate.
- This section shall also identify those responsible for the oversight of the financial reporting process, when those responsible for such oversight are different from those who fulfil the responsibilities described as above.

AUDITOR'S RESPONSIBILITIES SECTION

- Shall state that the objectives of the auditor are to:
 - (a) obtain reasonable assurance about whether the financial statement as a whole are free from material misstatement, whether due to fraud or error.
 - (b) Issue an auditor's report that includes the auditor's opinion.
- State that reasonable assurance is a high level of assurance, but is **not a guarantee** that an audit conducted in accordance with Sas will always detect a material misstatement if it exists
- State that misstatements can arise from fraud or error, and either
 - describe that they are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users or
 - provide a **definition or description of materiality** in accordance with the applicable financial reporting framework.

AUDITOR'S RESPONSIBILITIES SECTION (CONTD)

- Shall state that the auditor exercises professional judgment and maintains **professional scepticism** throughout the audit.
- The auditor shall describe that the auditor's responsibilities are:
 - a) To identify and assess the risk of material misstatement
 - b) To design and perform audit procedures responsive to those risks
 - c) To obtain audit evidence that is sufficient and appropriate to provide basis for the auditor's opinion.
 - d) To obtain an understanding of internal control relevant to the audit
 - e) To evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
 - f) To conclude on the appropriateness of management's use of the going concern basis of accounting
 - g) To evaluate the overall presentation, structure and content of the financial statements, including the disclosures.

AUDITOR'S RESPONSIBILITIES SECTION (CONTD)

- State that the auditor communicates with those charged with governance regarding the planned scope and timing of the audit and significant audit findings, including any significant deficiencies identified in internal control.
- State that the auditor provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements

Note: The description of the auditor's responsibilities (in this and the previous slide) shall be located:

- within the body of the auditor's report; or
- Within an appendix to the auditor's report ; or
- By a specific reference within the auditor's report to the location of such a description on a website of an appropriate authority

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION

- The key changes with respect to going concern include :
 - The new requirement to evaluate the adequacy of disclosures when events or conditions have been identified but no material uncertainty exists.
 - Additional guidance to support the auditor's evaluation of the adequacy of disclosures when a material uncertainty exists.
 - New requirements and guidance on how to refer to going concern in the auditor's report , including :
 - A new requirement to describe in the auditor's report the responsibilities of management / those charged with governance and the auditor related to going concern
 - A new material uncertainty related to going concern section in the auditor's report , and
 - A requirement to communicate key audit matters related to going concern , if applicable , in the auditor's report

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Change in management responsibility section** :- *“In preparing the financial statements, management or those charged with governance are responsible for assessing the entity’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.”* [See next slide for factors to be considered by the Management]
- **Change in auditors responsibility section** :- “We are also responsible to conclude on the appropriateness of management’s or those charged with governance’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to **draw attention in the auditor’s report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify the opinion.** Our conclusions are based on the audit evidence obtained up to the date of the auditor’s report. However, future events or conditions may cause an entity to cease to continue as a going concern.”

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Factors to be considered by the Management whilst evaluating the Going Concern Assumption:**
 - a. The period to be considered for taking into account all available information; generally most financial reporting framework considers 12 month as the period to be considered.
 - b. The size and complexity of the entity;
 - c. The nature and condition of its business;
 - d. The degree to which the entity or its business is affected by external factors.
 - e. Any judgment about future is based on information available at the time at which the judgment is made. Subsequent events may result in outcomes that are inconsistent with judgments that were reasonable at the time they were made

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- Factors to be considered by the Auditor to assess the appropriateness of the Going Concern Assumption:
 - a. If *events or conditions that cast significant doubt on the entity's ability to continue as a going concern are identified* [See next slide onwards] after the auditor's risk assessments are made, the auditor *needs to perform additional procedures* [See subsequent slides] and at the same time revise the assessment carried out to identify the risk of material misstatement.
 - b. The existence of such events or conditions may also affect the nature, timing and extent of the auditors' further procedures in response to the assessed risks as per SA 330.
 - c. The auditor to **remain alert throughout the audit** for evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern
 - d. Evaluating the steps taken by Management to *mitigate the*²⁴

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Examples of events or conditions that cast significant doubt on the entity's ability to continue as a going concern:**
 - a. Financial Factors, Events and Considerations**
 - b. Operating Factors and Considerations**
 - c. Regulatory Factors and Considerations**
 - d. Considerations Specific to Smaller Entities**

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

• **Financial Factors:**

- Net liability or net current liability position
- Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment;
- Excessive reliance on short-term borrowings to finance long-term assets (ALM)
- Indications of withdrawal of financial support by creditors.
- Negative operating cash flows indicated by historical or prospective financial statements.
- Adverse key financial ratios.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- Substantial operating losses or significant deterioration in the value of assets used to generate cash flows.
- Arrears or discontinuance of dividends.
- Inability to pay creditors on due dates.
- Inability to comply with the terms of loan agreements.
- Change from credit to cash-on-delivery transactions with suppliers.
- Inability to obtain financing for essential new product development or other essential investments.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Financial Factors [COVID Related Matters]:**
- Risk relating to receivables (delays or failures of counterparties, requests for changes in payment terms).
- Risk of significant business expansion into a new sector that is not sustainable in the future.
- Adverse movement in bond yields leading to deterioration of value of investments and impact on recoverability due to adverse market movements.
- Understanding the sources of available cash – shareholders (including related parties), lenders.
- Position of asset liability mismatch especially in case of financial institutions and the adverse implications of such ALM gap.
- Determination of whether funding facilities are on demand or committed, any representations or warranties required by funding agreements and if there is a risk of funding being withdrawn.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- The impact on funding due to but not limited to: Potential covenant breaches.
Material adverse changes/material adverse event clauses in debt agreements.
Debt maturity profile and impact of COVID-19 on refinancing risk.
- Clarity on how any accounting for exceptional items or adjusting items will be treated in determining covenant compliance.
- Risk of contingent liabilities (bank guarantees, performance guarantees, bonding, etc.).
- Risk that the parent company will no longer support the business
- Quality and timeliness of the financial and operational information used to manage the day to day business.
- Appropriateness of methodology or approach to short-term cash forecasting.
- Management's track record on forecasting expenditure such as cost reductions, plant restarts due to COVID-19.
- Whether management prepared a reverse stress test of liquidity, solvency and where applicable, covenant compliance to consider the maximum downside risk that would need to be managed through.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

• Operating Factors:

- a. Management intentions to liquidate the entity or to cease operations.
- b. Loss of key management without replacement
- c. Loss of a major market, key customer(s), franchise, license, or principal suppliers(s)
- d. Labour difficulties
- e. Shortages of important supplies
- f. Emergence of a highly successful competitor
- g. Uninsured or underinsured catastrophes when they occur

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Operating Factors (COVID Related Matters):**
- The level of lost revenue and cash flows including the effect of rebates, refunds and allowances and volume volatility.
- The risks relating to delivering products and services (e.g., workforce being ill / plant and facilities being inaccessible / inventory unable to reach end markets).
- Significant deterioration in the value of current assets – particularly inventory and whether management has considered possible write downs or write-offs of inventory.
- Loss of existing contracts and future contracts, particularly if facilities are being repurposed to support restructuring or recover losses arising due to COVID-19.
- Inability to honour certain terms of contracts leading to³¹

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- Customers finding other sources of supply during the COVID-19 pandemic and not returning.
- The ability of the business model to operate under current COVID-19 restrictions and whether the business model will be sustainable post COVID-19 (e.g., travel and leisure industry).
- Raw material pricing due to sourcing challenges and the related impact to projected gross margin levels.
- Increase in operating costs or cost of supplies due to restrictions related to COVID-19 and anticipated additional costs on account of adjusting to post COVID-19 scenario.
- Supply chains interruptions due to delays in overseas supplies (no longer just-in-time).
- Grants and other relief provided by governments (such as relief in the form of deferral of payments).

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Regulatory Factors:**

- a. Non-compliance with capital or other statutory or regulatory requirements, such as solvency or liquidity requirements for financial institutions.
- b. Pending legal or regulatory proceeding against the entity that may, if successful result in claims that the entity is unlikely to be able to satisfy.
- c. Changes in law or regulations or government policy expected to adversely affect the entity.

- **COVID Related Matters:**

- a. The impact of measures taken by governments in all the countries where the entity operates.
- b. Changes to the entity's access to capital impacted by measures taken by regulators (industry and/or financial) or banks.
- c. The entity's ability to prepare timely financial statements or other required information/filings, including delays in receiving financial data from operations in other countries or material investees for consolidated financial statements.
- d. The entity's ability to meet regulatory ratios.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Considerations specific to Smaller Entities:**
 - a. Banks and other lenders may cease to support the entity;
 - b. Loss of a principal Suppliers;
 - c. Loss of a major customers;
 - d. Loss of key employee;
 - e. Loss of the right to operate under a license, franchise or other legal agreement

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Examples of Steps to be taken By Management to Mitigate the Effect of Adverse Events or Consequences:**
 - a. Maintaining adequate cash flows by liquidating investments or disposing off non core assets
 - b. Rescheduling loan payments
 - c. Raising additional Debt or Equity Capital
 - d. Negotiating for alternative sources of supply
 - e. Changing the target market
 - f. Recruiting new talent or changing the terms of employment of key management personnel

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Examples of Steps to be taken By Management to Mitigate the Effect of Adverse Events or Consequences [COVID Related Matters]:**
 - a. Capital expenditure reductions
 - b. Reduction in dividends
 - c. Suspension of non-performance based bonuses
 - d. Deferral of payments of principal and interest
 - e. Cost reduction actions
 - f. Working capital reduction
 - g. Taxation payment holidays or deferrals or COVID-19 driven government funding
 - h. Asset liquidation
 - i. Government supported staff retention schemes and other governmental measures

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

• **Additional Audit Procedures:**

- Analyzing and discussing cash flow, profit and other relevant forecasts / interim financial statements with management.
- Reading the terms of debentures and loan agreements and determining whether any have been breached.
- Reading minutes of the meetings of shareholders, those charged with governance and relevant committees for reference to financing difficulties.
- Inquiring of the entity's legal counsel regarding the existence of litigation and claims and the reasonableness of management's assessments of their outcome and the estimate of their financial implications.
- Confirming the existence, legality and enforceability of arrangements to provide or maintain financial support with related and third party and assessing the financial ability of such parties to provide additional funds.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- Evaluating the entity's plans to deal with unfulfilled customer orders.
- Performing audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity's ability to continue as a going concern.
- Confirming the existence, terms and adequacy of borrowing facilities.
- Obtaining and reviewing reports of regulatory actions.
- Determining the adequacy of support for any planned disposals of assets.
- Evaluating management's plans for future actions which may include inquiries of management as to its plans for future action, including, for example, its plans to liquidate assets, borrow money or restructure debt, reduce or delay expenditures, or increase capital.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- Reporting Considerations:
 - a. To determine whether there is a “*material uncertainty*”
 - b. *Adequacy of disclosure* when events or conditions regards ability to continue as a going concern have been identified and a *material uncertainty exists*
 - c. *Adequacy of disclosure* when events or conditions regards ability to continue as a going concern have been identified but *no material uncertainty exists*
 - d. *Inadequate disclosures or no disclosures* of events or conditions regards ability to continue as a going concern have been identified and a *material uncertainty exists*

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Material Uncertainty:**

- a. Uncertainties related to events or conditions which may cast significant doubt on the entity's ability to continue as a going concern that should be disclosed in the financial statements
- b. When the magnitude of the potential impact of the events or conditions and the likelihood of occurrence is such that appropriate disclosure is necessary to achieve fair presentation (for fair presentation frameworks) or for the financial statements not to be misleading (for compliance frameworks)

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

Adequacy of Disclosure and Material Uncertainty Exists:

• Factors to consider Adequacy of Disclosure:

- a. Management's evaluation of the significance of the events or conditions relating to the entity's ability to meet its obligations; or
- b. Significant judgments made by management as part of its assessment of the entity's ability to continue as a going concern.
- c. Disclosures about the magnitude of the potential impact of the principal events or conditions, and the likelihood and timing of their occurrence.

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Manner of Reporting:**

- a. Express an **unmodified opinion** and include a separate section under the heading “**Material Uncertainty Related to Going Concern**”
- b. Draw attention to the note in the financial statements that discloses the events or conditions: and
- c. State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity’s ability to continue as a going concern and that the **auditors opinion is not modified** in respect of the matter.
- d. In addition to the above disclosures, the auditor may provide additional information to supplement the required statements for e.g. to explain: • That the existence of a material uncertainty is fundamental to user’s understanding of the financial statements; Or • How the matter was addressed in the audit [**Refer to Illustration 1 of the Appendix to the SA**]

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

Adequacy of Disclosure and Material Uncertainty Exists:

- **Factors to consider Adequacy of Disclosure:**
 - a. Principal Events or conditions
 - b. Management's evaluation of the significance of the events or conditions relating to the entity's ability to meet its obligations;
 - c. Management's Plan to mitigate the effect of these events and circumstances;
 - d. Significant judgments made by management as part of its assessment of the entity's ability to continue as a going concern.
 - e. Disclosures about the magnitude of the potential impact of the principal events or conditions, and the likelihood and timing of their occurrence.

- **No specific disclosures required in the audit report**

SA 570 – EVALUATING THE GOING CONCERN ASSUMPTION (CONTD...)

- **Inadequate Disclosures and Material Uncertainty Exists:**

- a. Express a qualified opinion or adverse opinion, as appropriate, in accordance with SA 705;and
- b. In the basis of qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not adequately disclose this matter.

[Illustration 2 of the appendix to this SA is an example of auditor's report containing qualified opinion.]

[Illustration 3 of the appendix to this SA is an example of auditor's reports containing adverse opinion]

SA-705 – MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT

- Qualified Opinion
- Adverse Opinion
- Disclaimer of Opinion

SA-705 – CIRCUMSTANCES RESULTING IN MODIFICATION OF OPINION

- Financial statements as a whole are not free from material misstatement – appropriateness of accounting policies – application of selected accounting policies – appropriateness or adequacy of disclosures
- Inability to obtain sufficient appropriate audit evidence – circumstances beyond control (destruction or seizure of records) – nature and timing of auditors work – Limitations imposed by management

SA-705 – QUALIFIED OPINION AND ADVERSE OPINION

- Misstatements individually or in aggregate are material but **not pervasive**
- Inability to obtain sufficient appropriate audit evidence – conclusion that possible undetected misstatements, if any, could be material but **not pervasive**
- **Adverse Opinion** – possible effect of undetected misstatements is pervasive
 - Not confined to specific elements, accounts or items of the financial statements
 - Represent a substantial portion of the financial statements
 - Disclosures which are omitted / misstated are fundamental to the users understanding of the financial statements
- Communicate to management and TCWG

SA-705 – DISCLAIMER OF OPINION

- Unable to obtain sufficient appropriate audit evidence to base his opinion
- Conclusion that potential effects on financial statements are both material and pervasive
- Communicate to management and TCWG

SA-706 – EMPHASIS OF MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT

- Draw attention to a matter disclosed in the financial statements
- Is of such importance that it is fundamental to the users understanding of the financial statements
- ***Auditor is in agreement and has obtained sufficient appropriate audit evidence***
- Reference should only be to information presented or disclosed in the financial statements

SA-706 – EMPHASIS OF MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT

- **Include immediately after the opinion para**
- Indicate that the opinion is not modified
- Communicate to management and TCWG
- **Examples**
 - a. uncertainties relating to future outcome of exceptional litigation, regulatory action,
 - b. *estimates (to take care),***
 - c. early application of new accounting standards which has a pervasive effect,
 - d. A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position
- Should be used very selectively
- **Also Refer to earlier slides for Going Concern considerations**

SA-706 – EMPHASIS OF MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT

Extracts from the Notes to Accounts of a Manufacturing Co:

"Since December, 2019 Covid-19, a new strain of coronavirus, has spread globally, including India. This event significantly affects economic activity worldwide and, as a result, could affect the operations and results of the group. The impact of coronavirus on our business will depend on future developments that cannot be reliably predicted, including actions to contain or treat the disease and mitigate its impact on the economies of the affected countries, among others.

The impact of the global health pandemic might be different from that estimated as at the date of approval of these financial results and the company will closely monitor any material changes to future economic conditions."

Extracts of EOM in the Audit Report:

"We draw your attention to note 8 to the Statement of Standalone and Consolidated unaudited results for the quarter ended 31st march, 2020 which describes the impact of the outbreak of coronavirus (Covid-19) on the business operations of the company. In view of the highly uncertain economic environment, a definitive assessment of the impact on the subsequent periods is highly dependent upon circumstances as they evolve".

SA-706 – EMPHASIS OF MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT

Extracts from the Notes to Account of a Service Sector Company:

"In assessing the impact of Covid-19 on recoverability of trade receivables including unbilled receivables, contract assets and contract costs, inventories, intangible assets, investments and margins of on-going projects, the company has considered internal and external information up to the date of approval of these financial results. Further, revenue for some on-going agreements has been considered based on management's best estimates. Based on current indicators of future economic conditions, the company expects to recover the carrying amount of these assets and revenue recognised. The impact of the Covid-19 pandemic may be different from that estimated as at the date of approval of these (consolidated) financial results and the company will continue to closely monitor any material changes to future economic conditions."

Extracts of EOM in the Audit Report:

"We draw attention to Note No. 3 of the standalone financial results, which describes that based on current indicators of future economic conditions the company expects to recover the carrying amount of all its assets and revenue recognised. The impact of the Covid-19 pandemic may be different from that estimated as at the date of approval of these financial results and the company will continue to closely monitor any material changes to future economic conditions. Our opinion is not modified in respect of this matter."

SA-706 – EMPHASIS OF MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT

Extracts from the Notes to Account of a Service Sector Company:

"During the previous year, on account of fire at the warehouse on-----, the company has recognised insurance claim of-----. The company has submitted all required information to insurance surveyor and final report is pending due to lockdown on account of Covid-19. The management estimates that the insurance claim amount is fully recoverable".

Extracts of EOM in the Audit Report:

"We draw attention to Note No. 4 of the standalone financial results, wherein it is stated that during the previous year on account of a fire at the warehouse on-----, the company has recognised insurance claim of-----. The company has submitted all required information to the insurance surveyor and the final report is pending due to the lockdown on account of Covid-19. The management estimates that the insurance claim amount is fully recoverable. Our opinion is not modified in respect of this matter".

REPORTING ON INTERNAL CONTROLS

Is reporting on IFC over FR also required in unlisted companies?

- As per the Companies Act, Directors' statement of responsibility over existence of adequate IFC and their operating effectiveness is required only for listed companies.
- Sec 143(3)(i) based on which the auditor has to report, however, does not restrict such reporting only to listed companies
- **Rule 10A notified on 7th May, 2018** provides that the *Statutory Auditors Report should instead of adequate financial statements state about existence of "Internal Financial Controls with reference to Financial Statements"*
- Does it therefore mean that directors are not responsible in such companies for IFC over FR, but only auditors' are responsible (See next slide)

REPORTING ON INTERNAL CONTROLS

- For such companies, management does have the primary responsibility for designing, implementation and maintenance of IC relevant for preparation of FS that give T&F view free from material misstatements whether due to fraud or error.
- Hence designing, implementing and maintaining adequate IFC also rests with the management.
- Rule 8(5)(viii) of Companies (Accounts) Rules, 2014 also requires the board in all companies to state adequacy of IFC w.r.t. FS
- Hence even if a specific statement is not required for unlisted companies, ensuring adequacy and operating effectiveness of IFC still remains with management and TCWG.
- The GN therefore equally applies to reporting on IFC in respect of unlisted, small companies and OPCs

REPORTING

- Assess impact on audit opinion
- Forming an opinion

(Depends upon evaluation of the identified deficiencies – see next slide)

EVALUATING THE DEFICIENCIES

- Deficiency
- Significant Deficiency
- Material Weakness

EVALUATING THE DEFICIENCIES

- A **'deficiency'** in internal financial control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.

EVALUATING THE DEFICIENCIES

- A '**significant deficiency**' is a deficiency, or a combination of deficiencies, in internal financial control over financial reporting that is important enough to merit attention of those charged with governance since there is a reasonable possibility that a **misstatement** of the company's annual or interim financial statements will not be prevented or detected on a timely basis.
- A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met.
- A deficiency in operation exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

EVALUATING THE DEFICIENCIES

- A '**material weakness**' is a deficiency, or a combination of deficiencies, in internal financial control over financial reporting, such that there is a reasonable possibility that a **material misstatement** of the company's annual or interim financial statements will not be prevented or detected on a timely basis.

OTHER REPORTING CONSIDERATIONS

- Elements of the Audit Report
- Separate Report on IFC and on the Financial Statements
- Modified Opinion – Definition of material weakness – statement that a material weakness has been identified – Description thereof together with its actual and potential impact on the financial statements
- Guidance provided in IG -20 – Reporting Considerations

ELEMENTS OF THE AUDIT REPORT

- Title including the word *Independent*
- Management's responsibility for assessing adequacy and effectiveness based on the definition as per the Act.
- Identification of the benchmark criteria adopted by the Management
- Statement that the audit was conducted in accordance with GN which requires planning and performing to obtain reasonable assurance about adequacy and operating effectiveness based on the assessed risk and other procedures performed
- Reasonable basis for opinion and inherent limitations for future periods reporting due to changes in conditions or in the deterioration of degree of compliance with policies or procedures
- Opinion on whether the Company has maintained in all material respects adequate IFC and operating effectiveness of the same.

COVID RELATED CONSIDERATIONS

- Companies may need to implement new internal controls or modify existing internal controls over financial reporting.
- Evaluate whether any of the controls are not operating effectively on account of absence of concerned person due to illness/quarantine/working from home/isolation/travel inaccessibility.
- Identify alternate controls.

COVID RELATED CONSIDERATIONS

- Company's ability to close financial reporting process in time.
- Company's ability to design and implement controls related to selection and application of Generally Accepted Accounting Principles (GAAP) for accounting and disclosure issues arising from COVID-19.
- Non participation in physical verification of inventory

ANY QUESTIONS?

- *When we are no longer able to change a situation,
we are challenged to change ourselves.*

Viktor E Frankl

- **THANKS**