

Companies Auditors Report Order, 2016



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Introduction

The Auditor of a company has a very important role to perform in light of the opinion he has to provide in relation to the audit of the financial statement of the company. For this, the MCA has issued the Companies (Auditor's Report) Order, 2016 (CARO 2016), on 29th March 2016. This order has been issued in supersession of the Companies (Auditor's Report) Order, 2015, and is applicable for reporting on financial statements of companies whose financial year commences on or after 1st April 2015. CARO 2015 was issued by MCA in supersession of CARO 2003 which was issued earlier in pursuance with the provision of Section 227 (4A) of Companies Act 1956. It contains the various guidelines the auditor must keep in mind while conducting the audit of a company. I have prepared this article to better understand the applicability of CARO, 2016 and further the guidelines provided in it.

Applicability of CARO, 2016:

It shall apply to every company including a foreign company as defined in clause(42) of section 2 of the Companies Act,2013 **except:**

1. A banking company as defined in clause(c) of section 5 of the Banking regulation Act,1949.
2. An insurance company as defined under the Insurance Act,1938.
3. A company licensed to operate under section 8 of the Companies Act;
4. A one person company as defined under clause(62) of section 2 of the Companies Act and a small company as defined under clause (85) of section 2 of the Companies Act
5. A private limited company
 - a) not being a subsidiary or holding company of a public company
 - b) having a paid up share capital and reserve and surplus not more than 1Cr as **on the balance sheet date**
 - c) which does not have a total borrowing exceeding Rs.1Cr from any bank or financial institution **at any point of time during the financial year** and;
 - d) which does not have **a total revenue as disclosed in Schedule III to the Companies Act, 2013 (including revenue from discontinuing operations) exceeding Rs. 10 Cr** as per the financial statements.
6. A small company i.e. having paid up share capital of not more than 50 Lakhs and revenue for operations not more than 1 Crore.

Matters to be included in the auditors report under CARO,2016:

1. Fixed Assets [Clause 3 (i)]

(a) Whether the company is maintain proper records showing full particulars including quantitative details and situation of fixed asset.

(b) Whether these fixed asset have been physically verified by management at reasonable interval.

(c) Whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account.

Notes:

- The records should also contain particulars in respect of fixed assets that have been fully depreciated or amortized or have been retired from active use and held for disposal.
- The records should also contain necessary particulars in respect of item of fixed asset that have been fully impaired during the period covered by the audit report.
- Physical verification of the assets has to be made by the **management** and not by the auditor.
- The auditor should obtain the fixed asset register and reconcile it with the title deeds of immovable properties.

2. Inventory [Clause 3 (ii)]

(a) Whether physical verification of inventory has been conducted at reasonable interval by the management.

(b) Whether any material discrepancies has been noticed on such verification and if so, whether the same has been properly dealt with in the books of account.

3. Loan given by company [Clause 3 (iii)]

Whether the company has granted any loans, secured or unsecured to companies, firms, LLP or other parties covered in the registered maintained under Section 189 of the Companies Act, 2013. If so,

(a) Whether terms and conditions of the grant of such loan are not prejudicial to the company's interest.

(b) Whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments and receipts are regular

(c) If the amount is overdue, state the total amount overdue, state the total amount overdue for more than 90 days and whether reasonable steps have been taken by the company for recovery of principal.

4. Loan to director and investment by the company [Clause 3 (iv)]

In respect of loan, investment, guarantees and security whether provision of Sections 185 and 186 of the Companies Act, 2013 has been complied with. If not, provide the details thereof.

As per section 185 of the Companies Act, 2013, no company shall directly or indirectly:

*a. Advance any loan to a **specified person***

*b. Give any guarantee in connection with a loan taken by a **specified person***

c. Provide any security in connection with a loan taken by a specified person.

Except in certain cases.

As per the provision of section 186 of the Companies Act, 2013, if the loans, investments etc already made by the company exceed the limit specified under section 186(2) approval by special resolution is required.

5 Deposits [Clause 3 (v)]

In case, the company has accepted deposits, whether the following has been complied with: Directives issued by the reserve bank of India:

(a) The provision of sec 73 to 76 or any other relevant provision of Companies Act, 2013 and the rules framed there under

(b) If the order has been passed by company law board (CLB) or National company law tribunal (NCLT) or RBI or any court or any other tribunal.

(c) However, if any of the above not complied with, the nature of contraventions should be stated.

6 Cost Records [Clause 3 (vi)]

Whether maintenance of cost records have been prescribed by the central government under sec 148 (1) of Companies Act, 2013 whether such accounts and records have been made and maintained.

As per section 148(1)

These provisions apply to such class of companies engaged in the

- Production of prescribed goods or,
- Providing prescribed services

If the Central Government is of the opinion, that it is necessary to do so, it may, by order, direct the audit of cost records.

7 Statutory Dues [Clause 3 (vii)]

(a) Whether the company is regular in depositing undisputed statutory dues with the appropriate authorities including Provident fund, Employees State Insurance fund, income tax, sales tax, service tax, duty of custom, duty of excise, value added tax, cess or any other statutory dues. If the company is not regular in depositing such statutory dues, the extent of arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than six months from the date they become payable, shall be indicated by the auditor.

(b) In case dues of income tax and sales tax or service tax or duty of custom or duty of excise or value added tax have not been deposited on account of any dispute, then the amount involved and the forum where dispute is pending shall be disclosed.

8 Repayment of Loan [Clause 3 (viii)]

Whether the company has defaulted in repayment of loans and borrowing to a financial institution, banks, government or dues to debenture holders. If yes, the period and the amount of default to be reported.

Notes:

- The term government here doesnot include government company.
- The auditor should report the period and amounts of all defaults existing at the balance sheet data irrespective of when those defaults have occurred.

9 Utilization of IPO and further public offer [Clause 3 (ix)]

Whether money raised by way of initial public offer or further public offer and the term loans were applied for the purpose for which those are raised.

If not, the details together with delays and defaults and subsequent rectification, if any, as may be applicable, be reported

10 Reporting of Fraud [Clause 3 (x)]

Whether any fraud by the company or any fraud on the company by its officers and employees has been noticed or reported during the year: if yes, the nature and the amount involved is to be indicated.

11 Approval of managerial remuneration [Clause 3 (xi)]

Whether managerial remuneration has been paid or provided in accordance with the requisite approvals mandated by the provision of

Section 197 read with schedule 5 to the Companies Act, 2013. If not, state the amount involved and step taken by the company for securing refund of the same.

Notes:

- As per the provisions of section 197 of the Companies Act, 2013 remuneration of directors and managers of a company shall be maximum 11% of net profit.
- Calculation of net profit shall be made as per section 198 except that remuneration of directors shall not be deducted.

12 Nidhi Company [Clause 3 (xii)]

Whether the Nidhi company has complied with the net owned funds to deposit in the ratio of 1:20 to meet out the liability and whether the Nidhi company is maintain 10% unencumbered term deposit as specified in the Nidhi rules 2014 to meet out the liability.

Nidhi means a company which has been incorporated as a Nidhi with **the OBJECT** of

- Cultivating the habit of thrift and
- Savings amongst its members,
- Receiving deposits from, and
- Lending to, its members only, for their mutual benefit, and Which complies with rules of Chapter XXVI of Companies Rules, 2014.

13 Related Party Transaction [Clause 3 (xiii)]

Whether all transaction with the related party is in compliance with Section 177 and 188 of the Companies Act, 2013 where applicable and the details have been disclosed in the financial statement etc., as required by the applicable accounting standard.

- As per requirements of section 188 all related party transactions (which are not arm's length transactions) require board resolution.
- If such transactions exceeds the limit as provided, approval by members is also obtained in general meeting.

14 Private Placement of Preferential Issues [Clause 3 (xiv)]

Whether the company has made any preferential allotment or private placement of shares or fully or partly convertible debentures during the year under review and if so, as to whether the requirement of Section 42 of Companies Act, 2013 have been complied with and the amount raised has been used for the purpose for which the funds were raised. If not, provide the detail in respect of the amount involved and the nature of non compliance.

Relevant extract of section 142(1) is as under:

(1) A company may, subject to the provisions of this section, make a private placement of securities.

(2) A private placement shall be made only to a select group of persons who have been identified by the Board (herein referred to as "identified persons"), whose number shall not exceed fifty or such higher number as may be prescribed [excluding the qualified institutional buyers and employees of the company being offered securities under a scheme of employees stock option in terms of provisions of clause (b) of sub-section (1) of section 62], in a financial year subject to such conditions as may be prescribed.

(3) A company making private placement shall issue private placement offer and application in such form and manner as may be prescribed to identified persons, whose names and addresses are recorded by the company in such manner as may be prescribed:

**Provided that the private placement offer and application shall not carry any right of renunciation.*

15 Non Cash Transaction [Clause 3 (xv)]

Whether the company has entered into any non-cash transaction with the director or person concerned with his and if so, whether the provision of Section 192 of Companies Act, 2013 has been complied with.

16 Register under RBI Act 1934 [Clause 3 (xvi)]

Whether the company is required to be registered under Section 45 IA of Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained.

Reasons to be stated for unfavorable and qualified answers

a. Where, in the auditors report the answer to any of the questions referred as above is unfavorable or qualified, the auditors report shall also state the basis for such unfavorable or qualified answer as the case may be.

b. Where the auditor is unable to express any opinion on any specified matter, his report shall indicate such fact together with the reasons as to why it is not possible for him to give his opinion on the same.

Conclusion:

After going through the above article, it can be understood regarding the applicability and reporting of Company Auditor Report Order, 2016. The auditor should have professional skepticism while preparing the auditor report i.e. his attitude should include a questioning mind, being alert to the conditions which may indicate possible misstatement due to error and fraud and a critical assessment of audit evidence.