CHAPTER 8

AUDIT REPORT

LEARNING OUTCOMES

After studying this chapter, you would be able to understand:

- The objectives of the auditor as per SA 700 (Revised), "Forming an Opinion and Reporting on Financial Statements." Also, whether the auditor has obtained reasonable assurance. Understand the evaluation by the auditor and Qualitative Aspects of the Entity's Accounting Practices. Elements of Auditor's report.
- The basics of Standard on Auditing (SA) 705 "Modifications to the Opinion in the Independent Auditor's Report".
- The basics of SA 701- "Communicating Key Audit Matters in the Independent Auditor's Report".
- The Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report as per SA 706.
- SA 710 - "Comparative Information- Corresponding figures and Comparative financial statements".
- The basics of SA 600 – "Using the work of Another Auditor".
- SA 299 – "Joint Audit of Financial Statements".
- Reporting requirements under the Companies Act, 2013
- Companies (Auditor's Report) Order, 2020.
- Practicality of above concepts by studying through examples and case studies.

CHAPTER OVERVIEW

Audit process culminates in formation of opinion by an auditor and expression of the same by means of audit report. Audit report, therefore, is the final outcome of an audit exercise. It is the document on which reliance is placed by users of financial statements as it contains auditor's opinion. Audit evidence obtained by performing various audit procedures, ultimately, leads to crystallization of opinion by auditor contained in audit report.

Understanding enormous significance of audit report, Sameer was unequivocal in his mind regarding some kind of consistency and comparability in reporting. It logically led him to next question- What are basic elements of an audit report? How does it look like? Is it necessary for an auditor to prepare audit report using these elements?

A counter question struck his mind in no time. If there is consistency and comparability in reporting, how does an auditor report in specific situations?

Shouldn't there be flexibility in reporting in particular situations? How do auditors do that? If an auditor wants to highlight some matters which are necessary to understanding of users of financial statements, how the same can be ensured?

And what about those issues which were identified as significant issues during the audit? Can such issues and manner of addressing such issues be reported? What kind of audit procedures were performed on those significant matters? There must be some sort of reporting mechanism for these issues. In absence of such type of flexibility in reporting, audit report can become too mechanical. He was mulling deeply.

What if auditor wants to express a modified opinion? What are different types of it and under what circumstances different types of modified opinion can be given by auditor? Does auditor have to state basis for such an opinion compulsorily? These were probing thoughts criss-crossing his mind.

He was also considering about reporting requirements if some matters are specifically required to be reported in accordance with law. Particularly, in case of companies, are there some specific matters? How reporting is to be made by auditor in respect of such matters?

Amidst this maze of thoughts, Shekhar called him to inform that, audit of company his team was doing, is now over and audit report has been issued. Wanting to know about outcome, he was asked by Shekhar to go to website of the company and go through audit report himself.

INTRODUCTION

Management is responsible for the preparation of the financial statements. Management also accepts responsibility for necessary internal controls to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The purpose of an audit is to enhance the degree of confidence of intended users of the financial statements. The aforesaid purpose is achieved by the expression of an independent reporting by the auditor as to whether the financial statements exhibit a true and fair view of the affairs of the entity.

Thus, an audit report is an opinion drawn on the entity's financial statements to make sure that the records are true and fair representation of the transactions they claim to represent. This involves considering whether the financial statements have been prepared in accordance with an acceptable financial reporting framework applicable to the entity under audit. It is also necessary to consider whether the financial statements comply with the relevant statutory requirements. The main users of audit report are shareholders, members and all other stakeholders of the company.

1. FORMING AN OPINION AND REPORTING ON FINANCIAL STATEMENTS

SA 700 (Revised)- "Forming an Opinion and Reporting on Financial Statements", deals with the auditor's responsibility to form an opinion on the financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

The requirements of this SA are aimed at addressing an appropriate balance between the need for consistency and comparability in auditor reporting globally and the need to increase the value of auditor reporting by making the information provided in the auditor's report more relevant to users. This SA promotes consistency in the auditor's report, but recognizes the need for flexibility to accommodate particular circumstances of individual jurisdictions. Consistency in the auditor's report, when the audit has been conducted in accordance with SAs, promotes credibility in the global marketplace by making more readily identifiable those audits that have been conducted in accordance with globally recognized standards. It also helps to promote the user's understanding and to identify unusual circumstances when they occur.

1.1 Objective of the Auditor

The objectives of the auditor as per SA 700 (Revised) are:

- **To form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and**
- **To express clearly that opinion through a written report.**

1.2 To Form Opinion – Auditor to Obtain Reasonable Assurance

The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

In order to form that opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error.

That conclusion shall take into account:

(a) Whether sufficient appropriate audit evidence has been obtained;

(b) Whether uncorrected misstatements are material, individually or in aggregate;

(c) The evaluations.

1.3 Evaluations by the Auditor

The auditor shall evaluate whether the financial statements are prepared in accordance with the requirements of the applicable financial reporting framework.

This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgements.

1.3.1 Qualitative Aspects of the Entity's Accounting Practices

1. Management makes a number of judgements about the amounts and disclosures in the financial statements.

2. SA 260 (Revised) contains a discussion of the qualitative aspects of accounting practices.

3. In considering the qualitative aspects of the entity's accounting practices, the auditor may become aware of possible bias in management's judgements. The auditor may conclude that the cumulative effect of lack of neutrality, together with the effect of uncorrected misstatements, causes the financial statements as a whole to be materially misstated. Indicators of a lack of neutrality include the following:

(i) The selective correction of misstatements brought to management's attention during the audit.

Example

- Correcting misstatements with the effect of increasing reported earnings, but not correcting misstatements that have the effect of decreasing reported earnings.

(ii) Possible management bias in the making of accounting estimates.

4. SA 540 addresses possible management bias in making accounting estimates.

Indicators of possible management bias do not constitute misstatements for purposes of drawing conclusions on the reasonableness of individual accounting estimates. They may, however, affect the auditor's evaluation of whether the financial statements as a whole are free from material misstatement.

1.4 Specific Evaluations by the Auditor

In particular, the auditor shall evaluate whether:

(a) The financial statements adequately disclose the significant accounting policies selected and applied;

(b) The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;

(c) The accounting estimates made by management are reasonable;

(d) The information presented in the financial statements is relevant, reliable, comparable, and understandable;

(e) The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and

(f) The terminology used in the financial statements, including the title of each financial statement, is appropriate.

Further, when the financial statements are prepared in accordance with a fair presentation framework, the evaluation mentioned above (Paragraph 1.3 & 1.4) shall also include an evaluation by the auditor as to whether the financial statements achieve fair presentation which shall include consideration of:

(a) The overall presentation, structure and content of the financial statements; and

(b) Whether the financial statements, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation.

The auditor shall evaluate whether the financial statements adequately refer to or describe the applicable financial reporting framework.

An overview of specific evaluations by the auditor

Checkbox	*Specific evaluations by the auditor*
✓	Selected and applied significant accounting policies are adequately disclosed.
✓	Accounting policies are consistent with applicable financial reporting framework.
✓	Accounting estimates by management are reasonable.
✓	Information in financial statement is relevant, reliable, comparable and understandable.
✓	Disclosures in financial statements are adequate to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements.
✓	Terminology used in financial statements is appropriate.

1.5 Definitions

For making the understanding better, the following terms have been defined below:

(a) **General purpose financial statements** – Financial statements prepared in accordance with a general purpose framework.

(b) **General purpose framework** – A financial reporting framework designed to meet the common financial information needs of a wide range of users. The financial reporting framework may be a fair presentation framework or a compliance framework.

The term **"fair presentation framework"** is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

(i) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or

(ii) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term **"compliance framework"** is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (i) or (ii) above.

(c) **Unmodified opinion –** The opinion expressed by the auditor when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

2. FORM OF OPINION

Unmodified Opinion: The auditor shall express an unmodified opinion when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Modified Opinion: If the auditor:

(a) concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or

(b) is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement,

the auditor shall modify the opinion in the auditor's report in accordance with SA 705.

3. AUDITOR'S REPORT

The auditor's report shall be in writing. This SA- 700 requires the use of specific headings, which are intended to assist in making auditor's report more recognizable, where audit is conducted in accordance with the relevant Standards on Auditing.

3.1 Auditor's Report for Audits Conducted in Accordance with Standards on Auditing

- Title
- Addressee
- Auditor's Opinion
- Basis for Opinion
- Going Concern
- Key Audit Matters
- *Other Information*
- Responsibilities for the Financial Statements
- Auditor's Responsibilities for the Audit of the Financial Statements
- Location of the description of the auditor's responsibilities
- Other Reporting Responsibilities
- Signature of the Auditor
- Place of Signature
- Date of the Auditor's Report

Basic Elements of an Audit Report are given below:

1. **Title:** The auditor's report shall have a title that clearly indicates that it is the report of an independent auditor.

For example, "Independent Auditor's Report," distinguishes the independent auditor's report from reports issued by others.

2. **Addressee:** The auditor's report shall be addressed, as appropriate, based on the circumstances of the engagement. Law, regulation or the terms of the engagement may specify to whom the auditor's report is to be addressed.

The auditor's report is normally addressed to those for whom the report is prepared, often either to the shareholders or to those charged with governance of the entity whose financial statements are being audited. In case of a company, the report is addressed to the shareholders of the company.

ILLUSTRATION 1

M/s Smart & Associates are the statutory auditors of Hotmeals Ltd. for the FY 2021-22. How will the auditor address the audit report issued on the financial statements for the FY 2021-22? Also give a title to the report.

SOLUTION

INDEPENDENT AUDITOR'S REPORT

To the Members of Hotmeals Ltd.

ILLUSTRATION 2

Richa International is a partnership firm dealing in export of blankets. The partners of the firm are Richa and Ashish. Explain how the statutory auditor of the firm will address the auditor's report.

SOLUTION

INDEPENDENT AUDITOR'S REPORT

To the Partners of Richa International

3. **Auditor's Opinion:** The first section of the auditor's report shall include the auditor's opinion, and shall have the heading "Opinion."

The Opinion section of the auditor's report shall also:

- 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; and
- Specify the date of, or period covered by, each financial statement comprising the financial statements.

Unmodified Opinion:

When expressing an unmodified opinion on financial statements, the auditor's opinion shall, unless otherwise required by law or regulation, use one of the following phrases, which are regarded as being equivalent:

(a) In our opinion, the accompanying financial statements **present fairly, in all material respects**, […] in accordance with [the applicable financial reporting framework]; or

(b) In our opinion, the accompanying financial statements **give a true and fair view of** […] in accordance with [the applicable financial reporting framework].

The phrases **"present fairly, in all material respects," and "give a true and fair view"** are regarded as being equivalent

When the auditor expresses an unmodified opinion, it is not appropriate to use phrases such as "with the foregoing explanation" or "subject to" in relation to the opinion, as these suggest a conditional opinion or a weakening or modification of opinion.

ILLUSTRATION 3

M/s Amitabh & Associates are the statutory auditors of Ringston Ltd. which is a company engaged in the business of manufacture of pen drives. The auditor has started drafting the audit report for the FY 2021-22. CA Amitabh, the engagement partner is of the view that the financial statements of Ringston Ltd. represent a true and fair view. Give the draft of the opinion paragraph of the audit report.

SOLUTION

Opinion

We have audited the financial statements of Ringston Limited which comprise the Balance Sheet as at 31.03.2022 and the statement of Profit and Loss Account and the notes to the financial statements, including a summary of significant accounting policies and other explanatory information.

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 Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the company as at 31.03.2022 and the Profit & Loss for the year ending on that date.

4. Basis for Opinion: The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion", that:

1. States that the audit was conducted in accordance with Standards on Auditing;
2. Refers to the section of the auditor's report that describes the auditor's responsibilities under the SAs;
3. 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.
4. 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.

   Thus, the Basis for opinion section provides important context about the auditor's opinion.

ILLUSTRATION 4

M/s Kite Rite & Associates are the statutory auditors of Prime Deluxe Limited, for the FY 2021-22. At the time of finalising the audit report, one of the engagement team members, Mr. Robin, asked the engagement partner, CA Kite as to what all should be included in the Basis of Opinion Paragraph. The engagement partner CA Kite, explained the team in detail and asked Mr. Robin to draft such section for the auditor's report of Prime Deluxe Limited. Help Mr. Robin to draft the Basis for opinion section.

SOLUTION

Basis for Opinion

We conducted our audit in accordance with the Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013. Our responsibilities under those Standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Company in accordance with the Code of Ethics issued by the Institute of Chartered Accountants of India together with the ethical requirements that are relevant to our audit of the financial statements under the provisions of the Companies Act, 2013 and the Rules thereunder, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

5. Going Concern: Where applicable, the auditor shall report in accordance with SA 570 (Revised).

- ♦ Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future. General purpose financial statements are prepared using the going concern basis of accounting, unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.
- ♦ When the use of the going concern basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business.
- ♦ The auditor shall evaluate whether sufficient appropriate audit evidence has been obtained regarding, and shall conclude on, the appropriateness of

management's use of the going concern basis of accounting in the preparation of the financial statements.

- Based on the audit evidence obtained, the auditor shall conclude whether, in the auditor's judgement, a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.
- A material uncertainty exists when the magnitude of its potential impact and likelihood of occurrence is such that, in the auditor's judgement, appropriate disclosure of the nature and implications of the uncertainty is necessary for:

  (a) In the case of a fair presentation financial reporting framework, the fair presentation of the financial statements, or

  (b) In the case of a compliance framework, the financial statements not to be misleading.

6. **Key Audit Matters:** For audits of complete sets of general purpose financial statements of listed entities, the auditor shall communicate key audit matters in the auditor's report in accordance with SA 701.

When the auditor is otherwise required by law or regulation or decides to communicate key audit matters in the auditor's report, the auditor shall do so in accordance with SA 701.

Law or regulation may require communication of key audit matters for audits of entities other than listed entities.

Example

Entities characterized in such law or regulation as public interest entities.

The auditor may also decide to communicate key audit matters for other entities, including those that may be of significant public interest, for example because they have a large number and wide range of stakeholders and considering the nature and size of the business.

Examples of such entities may include financial institutions (such as banks, insurance companies, and pension funds), and other entities such as charitable institutions.

7. Other Information: Where applicable, the auditor shall report in accordance with SA 720 (Revised).

8. Responsibilities for the Financial Statements: The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements."

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.**

(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.**

(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;[because of the possible effects of fraud on other aspects of the audit, materiality does not apply to management's acknowledgement regarding its responsibility for the design, implementation, and maintenance of internal control (or for establishing and maintaining effective internal control over financial reporting) to prevent and detect fraud.] 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.

SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Management and, where appropriate, those charged with governance accept responsibility for the preparation of the financial statements. Management also accepts responsibility for such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The description of management's responsibilities in the auditor's report includes reference to both responsibilities as it helps to explain to users the premise on which an audit is conducted.

SA 210 requires the auditor to agree management's responsibilities in an engagement letter or other suitable form of written agreement.

Oversight of the financial reporting process: This section of the auditor's report shall also identify those responsible for the oversight of the financial reporting process, when those responsible for such oversight are different from Management. In this case, the heading of this section shall also refer to "Those Charged with Governance" ***or such term that is appropriate in the context of the legal framework applicable to the entity.***

ILLUSTRATION 5

Diamond Shine Ltd. is a company engaged in the manufacture of detergent. M/s Bright & Associates are the statutory auditors of the company. Explain how the paragraph related to the management's responsibility will come in the auditor's report.

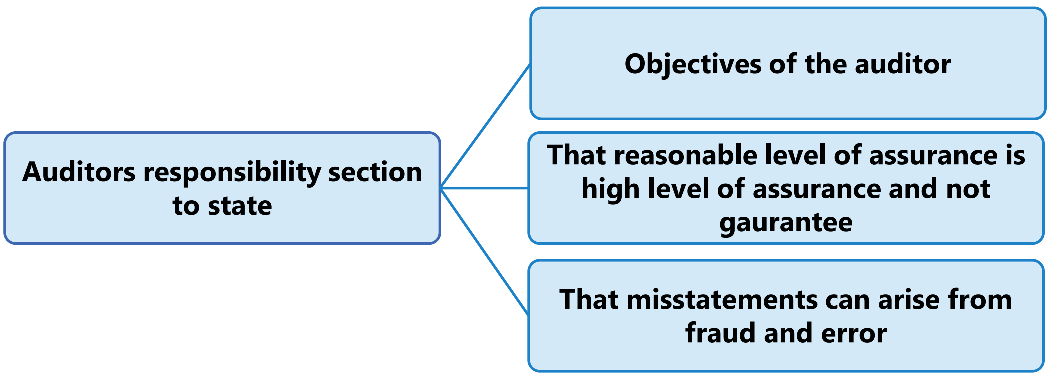
SOLUTION

Management's Responsibility for the Standalone Financial Statements

The Company's Board of Directors is responsible for the matters stated in section 134(5) of the Companies Act, 2013 ("the Act") with respect to the preparation of these standalone financial statements that give a true and fair view of the financial position, financial performance, (changes in equity) and cash flows of the Company in accordance with the accounting principles generally accepted in India, including the accounting Standards specified under section 133 of the Act. This responsibility also includes maintenance of adequate accounting records in accordance with the provisions of the Act for safeguarding of the assets of the Company and for preventing and detecting frauds and other irregularities; selection and application of appropriate accounting policies; making judgements and estimates that are reasonable and prudent; and design, implementation and maintenance of adequate internal financial controls, that were operating effectively for ensuring the accuracy and completeness of the accounting records, relevant to the preparation and presentation of the financial statement that give a true and fair view and are free from material misstatement, whether due to fraud or error. In preparing the financial statements, management is responsible for assessing the Company'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. Those Board of Directors are also responsible for overseeing the Company's financial reporting process.

9. Auditor's Responsibilities for the Audit of the Financial Statements: The auditor's report shall include a section with the heading **"Auditor's Responsibilities for the Audit of the Financial Statements."**

I. This section of the auditor's report shall state:



(a) That the objectives of the auditor are to:

(i) Obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error; and

(ii) Issue an auditor's report that includes the auditor's opinion.

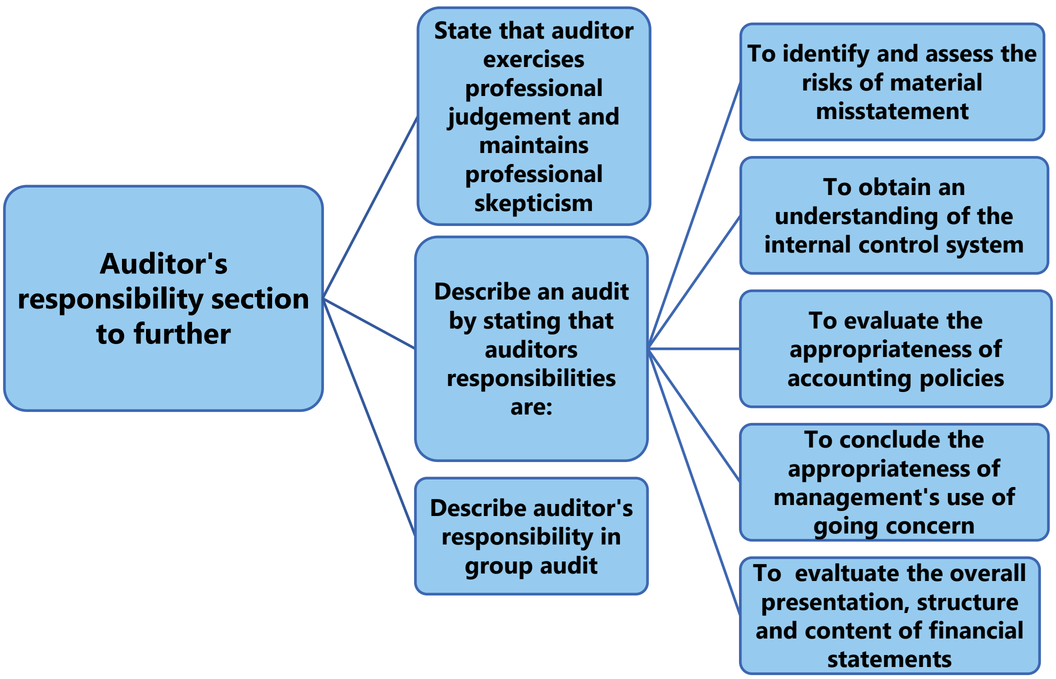
(b) That reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists; and

(c) That misstatements can arise from fraud or error, and either:

(i) Describe that they are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements; or

(ii) Provide a definition or description of materiality in accordance with the applicable financial reporting framework.

II. The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report shall further:



(a) State that, as part of an audit in accordance with SAs, the auditor exercises professional judgement and maintains professional skepticism throughout the audit; and

(b) Describe an audit by stating that the auditor's responsibilities are:

(i) To identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error; to design and perform audit procedures responsive to those risks; and to obtain audit evidence that is sufficient and appropriate to provide a basis for the auditor's opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

(ii) To obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances.

(iii) To evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

(iv) To conclude on the appropriateness of management'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.

(v) When the financial statements are prepared in accordance with a fair presentation framework, to evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

(c) When SA 600 applies, further describe the auditor's responsibilities in a group audit engagement by stating:

The division of responsibility for the financial information of the entity by indicating the extent to which the financial information of components is audited by the other auditors have been included in the financial information of the entity, e.g., the number of divisions /branches/subsidiaries or other components audited by other auditors

III. The Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report also shall:

(a) State that the auditor communicates with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that the auditor identifies during the audit;

(b) For audits of financial statements of listed entities, state that the auditor provides those charged with governance with a statement that the auditor has complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on the auditor's independence, and where applicable, related safeguards; and

(c) For audits of financial statements of listed entities and any other entities for which key audit matters are communicated in accordance with SA 701, state that, from the matters communicated with those charged with governance, the auditor determines those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. The auditor describes these matters in the auditor's report unless law or regulation precludes public disclosure.

10. Location of the description of the auditor's responsibilities for the audit of the financial statements: The description of the auditor's responsibilities for the audit of the financial statements shall be included:

Within the body of the auditor's report

Within an appendix to the auditor's report, in which case the auditor's report shall include a reference to the location of the appendix or

By a specific reference within the auditor's report to the location of such a description on a website of an appropriate authority, where law, regulation or national auditing standards expressly permit the auditor to do so.

ILLUSTRATION 6

M/s Ajay Vijay & Associates are the statutory auditors of Sarovar Ltd. for the FY 2021-22. The company is engaged in the business of manufacture of water bottles. At the time of finalising the auditor's report, one of the audit team members asked CA Ajay, the engagement partner to advise as to how the auditor's responsibilities can be shown in an appendix to the auditor's report. Draft the auditor's responsibility paragraph so as to advise the audit team member.

SOLUTION

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. 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 when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is included in appendix X of this auditor's report. This description, which is located at [*indicate page number or other specific reference to the location of the description*], forms part of our auditor's report.

11. Other Reporting Responsibilities:

- If the auditor addresses other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibilities under the SAs, these other reporting responsibilities shall be addressed in a separate section in the auditor's report with a heading titled

  "Report on Other Legal and Regulatory Requirements" or otherwise as appropriate to the content of the section, unless these other reporting responsibilities address the same topics as those presented under the reporting responsibilities required by the SAs in which case the other reporting responsibilities may be presented in the same section as the related report elements required by the SAs.

- If other reporting responsibilities are presented in the same section as the related report elements required by the SAs, the auditor's report shall clearly differentiate the other reporting responsibilities from the reporting that is required by the SAs.

- If the auditor's report contains a separate section that addresses other reporting responsibilities, the requirements stated above shall be included under a section with a heading "Report on the Audit of the Financial Statements." The "Report on Other Legal and Regulatory Requirements" shall follow the "Report on the Audit of the Financial Statements."

12. Signature of the Auditor: The auditor's report shall be signed. The report is signed by the auditor (i.e. the engagement partner) in his personal name. Where the firm is appointed as the auditor, the report is signed in the personal name of the auditor and in the name of the audit firm.

The partner/proprietor signing the audit report also needs to mention the membership number assigned by the Institute of Chartered Accountants of India. They also include the registration number of the firm, wherever applicable, as allotted by ICAI, in the audit reports signed by them.

13. Place of Signature: The auditor's report shall name specific location, which is ordinarily the city where the audit report is signed.

14. Date of the Auditor's Report: The auditor's report shall be dated no earlier than the date on which the auditor has obtained sufficient appropriate audit evidence on which to base the auditor's opinion on the financial statements, including evidence that:

- **All the statements that comprise the financial statements, including the related notes, have been prepared; and**
- **Those with the recognized authority have asserted that they have taken responsibility for those financial statements**

The date of the auditor's report informs the user of the auditor's report that the auditor has considered the effect of events and transactions of which the auditor became aware and that occurred up to that date. The auditor's responsibility for events and transactions after the date of the auditor's report is addressed in SA 560.

UDIN

It was noticed that financial documents/ certificates attested by third person misrepresenting themselves as CA Members were misleading the Authorities and Stakeholders. ICAI also received number of complaints of signatures of CAs being forged by non CAs. To curb the malpractices, the Professional Development Committee of ICAI implemented in phased manner an innovative concept of UDIN i.e. Unique Document Identification Number. All Certificates were made mandatory with effect from 1st February, 2019 as per the Council decision taken at its 379th Meeting held on 17th – 18th December, 2018.

Chartered Accountants having full-time Certificate of Practice can register on UDIN Portal and generate UDIN by registering the certificates attested/certified by them.

Accordingly, an auditor is required to mention the UDIN with respect to each audit report being signed by him, along with his membership number while signing an audit report. The same is shown in the below illustration.

IILUSTRATION 7

M/s TUV & Associates are the statutory auditors of Venus Ltd. for the FY 2021-22.

At the time of finalising the auditor's report, one of the audit team members asked the engagement partner, CA Tarun, to explain as to how the auditor's report will be signed. Help CA Tarun in explaining the same.

SOLUTION

The following is the correct way of signing an audit report.

M/s TUV & Associates

Chartered Accountants

(Firm's Registration No.)

Signature

(Name of the Member Signing the Audit Report)

(Designation)

(Membership No. XXXXX)

Place of Signature: UDIN: 20037320AAAAAH1111

Date:

Test Your Understanding 1

Maithili Thakur, a CA student, was perusing audit report of a company. Her eyes fell on an 18-digit alpha numeric number stated at end of audit report below the signatures of auditor and membership number. Make her understand objective and significance of such a randomly generated number. Is it required to be stated in case of audit reports only?

Test Your Understanding 2

CA. Maya Memani has conducted audit of a company. She has asked Sana, a CA student undergoing training in her office, to prepare draft audit report. Sana was part of engagement team conducting the audit. She has been further told to prepare draft report expressing unmodified opinion. After drafting para comprising unmodified opinion, Sana feels no need to provide basis for opinion. Discuss why her thinking is not proper.

4. AUDITOR'S REPORT PRESCRIBED BY LAW OR REGULATION

SA 200 explains that the auditor may be required to comply with legal or regulatory requirements in addition to SAs. When the differences between the legal or regulatory requirements and SAs relate only to the layout and wording of the auditor's report, the requirements stated below in points (a)–(m) set out the minimum elements to be included in the auditor's report to enable a reference to the Standards on Auditing. In those circumstances, the requirements stated in paragraph 3.1 above that are not included in points (a)–(m) need not be applied.

For example, the required ordering of the Opinion and the Basis of Opinion sections need not be applied.

Where specific requirements in a particular law or regulation do not conflict with SAs, the layout and wording required by this SA assist users of the auditor's report in more readily recognizing the auditor's report as a report of an audit conducted in accordance with SAs.

If the auditor is required by law or regulation to use a specific layout, or wording of the auditor's report, the auditor's report shall refer to Standards on Auditing only if the auditor's report includes, at a minimum, each of the following elements:

(a) A title.

(b) An addressee, as required by the circumstances of the engagement.

(c) An Opinion section containing an expression of opinion on the financial statements and a reference to the applicable financial reporting framework used to prepare the financial statements.

(d) An identification of the entity's financial statements that have been audited.

(e) 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.

(f) Where applicable, a section that addresses, and is not inconsistent with, the reporting requirements relating to going concern as per SA 570 (Revised).

(g) Where applicable, a Basis for Qualified (or Adverse) Opinion section that addresses, and is not inconsistent with, the reporting requirements relating to going concern as per SA 570 (Revised).

(h) Where applicable, a section that includes the information required by SA 701, or additional information about the audit that is prescribed by law or regulation and that addresses, and is not inconsistent with, the reporting requirements in that SA.

(i) A description of management's responsibilities for the preparation of the financial statements and an identification of those responsible for the oversight of the financial reporting process that addresses, and is not inconsistent with, the requirements as contained in this SA 700.

(j) A reference to Standards on Auditing and the law or regulation, and a description of the auditor's responsibilities for an audit of the financial statements that addresses, and is not inconsistent with, the requirements as contained in this SA 700.

(k) The auditor's signature.

(l) The Place of signature.

(m) The date of the auditor's report.

ILLUSTRATION 8

Auditor's Report on Financial Statements of a Listed Entity Prepared in Accordance with a Fair Presentation Framework

For purposes of this illustrative auditor's report, the following circumstances are assumed:

- *Audit of a complete set of financial statements of a listed company (registered under the Companies Act, 2013) using a fair presentation framework. The audit is not a group audit (i.e., SA 600 does not apply).*

- *The financial statements are prepared by management of the entity in accordance with the accounting Standards prescribed under section 133 of the Companies Act, 2013.*
- *The terms of the audit engagement reflect the description of management's responsibility for the financial statements in SA 210.*
- *The auditor has concluded an unmodified (i.e., "clean") opinion is appropriate based on the audit evidence obtained.*
- *The relevant ethical requirements that apply to the audit comprise the Code of Ethics issued by ICAI together with the other relevant ethical requirements relating to the audit and the auditor refers to both.*
- *Based on the audit evidence obtained, the auditor has concluded that a material uncertainty does not exist related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern in accordance with SA 570 (Revised).*
- *Key audit matters have been communicated in accordance with SA 701.*
- *Those responsible for oversight of the financial statements differ from those responsible for the preparation of the financial statements.*
- *In addition to the audit of the financial statements, the auditor has other reporting responsibilities required under the Companies Act, 2013.*

INDEPENDENT AUDITOR'S REPORT

To the Members of ABC Company Limited

Report on the Audit of the Standalone Financial Statements [1]

Opinion

We have audited the standalone financial statements of ABC Company Limited ("the Company"), which comprise the balance sheet as at 31st March 20XX, and the statement of Profit and Loss, *(statement of changes in equity)*[2] and statement of cash flows for the year then ended, and notes to the financial statements, including

---

[1] The sub-title "Report on the Audit of the Standalone Financial Statements" is unnecessary in circumstances when the second sub-title "Report on Other Legal and Regulatory Requirements" is not applicable.

[2] Where applicable

a summary of significant accounting policies and other explanatory information [in which are included the Returns for the year ended on that date audited by the branch auditors of the Company's branches located at (location of branches)][3].

In our opinion and to the best of our information and according to the explanations given to us, the aforesaid standalone financial statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as at March 31, 20XX, and profit/loss, *(changes in equity)*[4] and its cash flows for the year ended on that date.

Basis for Opinion

We conducted our audit in accordance with the Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013. Our responsibilities under those Standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the *Code of Ethics* issued by the Institute of Chartered Accountants of India together with the ethical requirements that are relevant to our audit of the financial statements under the provisions of the Companies Act, 2013 and the Rules thereunder, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

[Description of each key audit matter in accordance with SA 701.]

Management's Responsibility for the Standalone Financial Statements

The Company's Board of Directors is responsible for the matters stated in section 134(5) of the Companies Act, 2013 ("the Act")[4] with respect to the preparation of

---

[3] Where applicable

[4] Where applicable

these standalone financial statements that give a true and fair view of the financial position, financial performance, (changes in equity)[5] and cash flows of the Company in accordance with[6] the accounting principles generally accepted in India, including the accounting Standards specified under section 133 of the Act. This responsibility also includes maintenance of adequate accounting records in accordance with the provisions of the Act for safeguarding of the assets of the Company and for preventing and detecting frauds and other irregularities; selection and application of appropriate implementation and maintenance of accounting policies; making judgements and estimates that are reasonable and prudent; and design, implementation and maintenance of adequate internal financial controls, that were operating effectively for ensuring the accuracy and completeness of the accounting records, relevant to the preparation and presentation of the financial statement that give a true and fair view and are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company'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.

Those Board of Directors are also responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. 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 when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

[5] Where applicable

[6] Where management's responsibility is to prepare financial statements that give a true and fair view, this may read: "Management is responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards, and for such ..."

Paragraph 40(b) of this SA explains that the shaded material below can be located in an Appendix to the auditor's report. Paragraph 40(c) explains that when law, regulation or applicable auditing standards expressly permit, reference can be made to a website of an appropriate authority that contains the description of the auditor's responsibilities, rather than including this material in the auditor's report, provided that the description on the website addresses, and is not inconsistent with, the description of the auditor's responsibilities below.

As part of an audit in accordance with SAs, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances. Under section 143(3)(i) of the Companies Act, 2013, we are also responsible for expressing our opinion on whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management'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 Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our

auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Other Matter

We did not audit the financial statements/ information of ………………. (number) branches included in the stand alone financial statements of the Company whose financial statements/financial information reflect total assets of ₹ ……………..as at 31st March 20XX and the total revenue of ₹ ……………….. for the year ended on that date, as considered in the standalone financial statements/information of these branches have been audited by the branch auditors whose reports have been furnished to us, and our opinion in so far as it relates to the amounts and disclosures included in respect of branches, is based solely on the report of such branch auditors.

Our opinion is not modified in respect of these matters.

Report on Other Legal and Regulatory Requirements

As required by the Companies (Auditor's Report) Order, 2020 ("the Order"), issued by the Central Government of India in terms of sub-section (11) of section 143 of the Companies Act, 2013, we give in the Annexure a statement on the matters specified in paragraphs 3 and 4 of the Order, to the extent applicable.

As required by Section 143(3) of the Act, we report that:

(a) We have sought and obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit.

(b) In our opinion, proper books of account as required by law have been kept by the Company so far as it appears from our examination of those books [*and proper returns adequate for the purposes of our audit have been received from the branches not visited by us*[7]*]*

(c) [*The reports on the accounts of the branch offices of the Company audited under Section 143(8) of the Act by branch auditors have been sent to us and have been properly dealt with by us in preparing this report*[8].]

(d) 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 [*and with the returns received from the branches not visited by us*[9]].

(e) In our opinion, the aforesaid standalone financial statements comply with the Accounting Standards specified under Section 133 of the Act, read with Rule 7 of the Companies (Accounts) Rules, 2014.

(f) We do not have any observation or comment on the financial statements or matters which have any adverse effect on the functioning of the company.

(g) On the basis of the written representations received from the directors as on 31st March, 20XX taken on record by the Board of Directors, none of the directors is disqualified as on 31st March, 20XX from being appointed as a director in terms of Section 164 (2) of the Act.

(h) We do not have any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected herewith.

[7] Where applicable
[8] Where applicable
[9] Where applicable

(i) With respect to the adequacy of the internal financial controls over financial reporting of the Company and the operating effectiveness of such controls, refer to our separate Report in "Annexure A".

(j) With respect to the other matters to be included in the Auditor's Report in accordance with Rule 11 of the Companies (Audit and Auditors) Rules, 2014, in our opinion and to the best of our information and according to the explanations given to us:

(1) The Company has disclosed the impact of pending litigations on its financial position in its financial statements – Refer Note XX to the financial statements; *[or the Company does not have any pending litigations which would impact its financial position[10]]*

(2) The Company has made provision, as required under the applicable law or accounting standards, for material foreseeable losses, if any, on long-term contracts including derivative contracts – Refer Note XX to the financial statements; *[or the Company did not have any long-term contracts including derivative contracts for which there were any material foreseeable losses.[11]]*

(3) There has been no delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company {*or, following are the instances of delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the Company or there were no amounts which were required to be transferred to the Investor Education and Protection Fund by the Company[12]*}.

(4) (i) 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 company 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 company

[10] As may be applicable

[11] As may be applicable

[12] As may be applicable

("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries;

(ii) 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 company from any person(s) or entity(ies), including foreign entities ("Funding Parties"), with the understanding, whether recorded in writing or otherwise, that the company 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 we have considered reasonable and appropriate in the circumstances, nothing has come to our notice that has caused us to believe that the representations under sub-clause (i) and (ii) contain any material mis-statement.

(5) The dividend declared or paid during the year by the company is in compliance with section 123 of the Companies Act, 2013.

(6) The company 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.

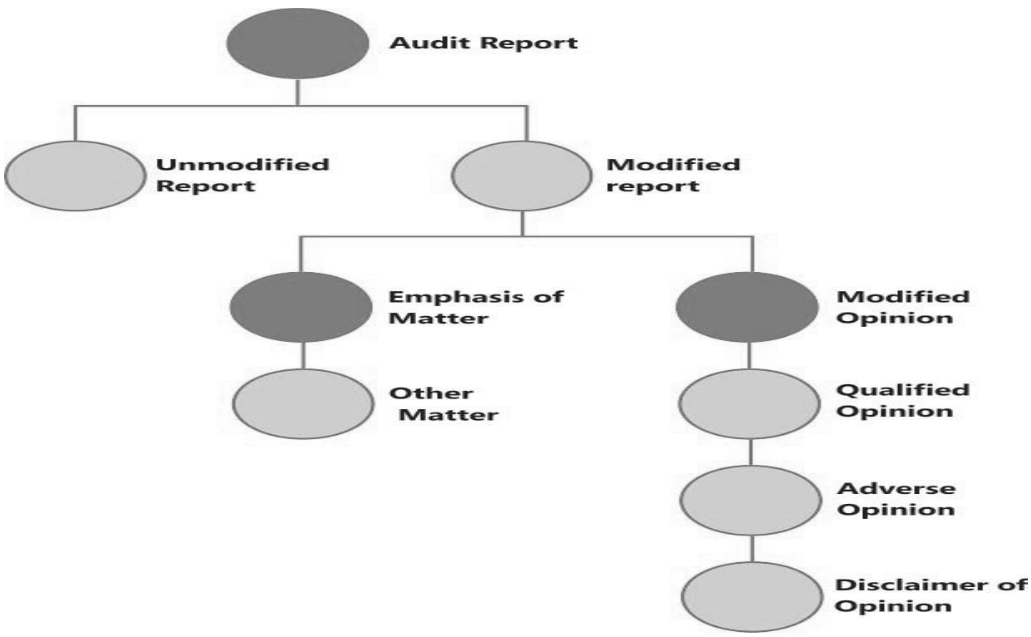
For XYZ & Co
Chartered Accountants
(Firm's Registration No.)
Signature
(Name of the Member Signing the Audit Report)
(Designation[13])
(Membership No. XXXXX)
UDIN: 20037320AAAAAH1111
Place of Signature:

Date:

[13] Partner or Proprietor, as the case may be

5. MODIFICATIONS TO THE OPINION IN THE INDEPENDENT AUDITOR'S REPORT

Standard on Auditing (SA) 705 "Modifications to the Opinion in the Independent Auditor's Report" deals with the auditor's responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with SA 700 (Revised) "Forming an Opinion and Reporting on Financial Statements", the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary.



This SA also deals with how the form and content of the auditor's report is affected when the auditor expresses a modified opinion.

5.1 Circumstances When a Modification to the Auditor's Opinion Is Required

The auditor shall modify the opinion in the auditor's report in the following circumstances:

The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or

The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

5.2 Objective of the Auditor- To Express Clearly an Appropriately Modified Opinion

As per Standard on Auditing (SA) 705 "Modifications To The Opinion In The Independent Auditor's Report", the objective of the auditor is **to express clearly an appropriately modified opinion** on the financial statements that is necessary when:

(a) The auditor concludes, based on the audit evidence obtained, that the financial statements as a whole are not free from material misstatement; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

5.3 Types of Modified Opinions:

There are three types of modified opinions, namely-

1. A qualified opinion
2. An adverse opinion
3. A disclaimer of opinion

Qualified Opinion

The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, are material, but not pervasive or

The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.

Adverse Opinion

The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

Disclaimer of Opinion

The auditor shall disclaim an opinion when he is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and he concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

Qualified Opinion

The auditor shall express a qualified opinion when:

(a) The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.

IILUSTRATION 9

Super Duper Ltd. is a company engaged in the manufacture of office furniture. M/s Young Old & Associates are the statutory auditors of the company for the FY 2021-22. During the year under audit, the engagement partner CA Young noticed that the company has not bifurcated its loans into long term and short term. CA Young understands that such misstatement is not pervasive though the same is material.

Explain the type of opinion that should be given by M/s Young Old & Associates in this case.

SOLUTION

M/s Young Old & Associates should give a qualified opinion as the effect of the misstatement on account of the non-bifurcation of loans into long term and short term loans, is material but not pervasive.

Adverse Opinion

The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

Definition of Pervasive – A term used, in the context of misstatements, to describe the effects on the financial statements of misstatements or the possible effects on the financial statements of misstatements, if any, that are undetected due to an inability to obtain sufficient appropriate audit evidence.

Pervasive effects on the financial statements are those that, in the auditor's judgement:

(i) Are not confined to specific elements, accounts or items of the financial statements;

(ii) If so confined, represent or could represent a substantial proportion of the financial statements; or

(iii) In relation to disclosures, are fundamental to users' understanding of the financial statements.

IILUSTRATION 10

M/s Taj Raj & Associates are the statutory auditors of Polex Ltd. engaged in the manufacture of premium watches, for the FY 2021-22. During the course of audit, CA Taj, the engagement partner found that the stocks and debtors of the company constituting about 80% of the total assets of the company are not realisable. Further, the cashier of the company has committed a fraud during the year under audit. Both the facts are not reflected in the financial statements for the year ending 31.03.2022. Accordingly, CA Taj is of the view that the impact of both the situations on the financial statements is material and pervasive and thus, the financial statements represent a distorted view of the state of affairs of the company. Explain the reporting requirements of CA Taj.

SOLUTION

The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

In the case Polex Ltd., CA Taj found that the stocks and debtors of the company constituting about 80% of the total assets of the company are not realisable. Further, the cashier of the company has committed a fraud during the year under audit. Such situations are not reflected in the financial statements of the company despite having a material and pervasive impact on the financial statements. As such, CA Taj should give an adverse opinion.

Further, CA Taj should also consider the reporting responsibilities under CARO 2020 and section 143(12) of the Companies Act, 2013.

Disclaimer of Opinion The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.

ILLUSTRATION 11

Delightful Ltd. is a company engaged in the production of smiley balls. During the FY 2021-22 the company transferred its accounts to computerised system (SAP) from manual system of accounts. Since the employees of the company were not well versed with the SAP system, there were many errors in the accounting during the transition period. As such the statutory auditors of the company were not able to extract correct data and reports from the system. Such data was not available manually also. Further, the employees and the management of the company were not supportive in providing the requisite information to the audit team. Explain the kind of audit report that the statutory auditor of the company should issue in this case.

SOLUTION

When the statutory auditor of the company is unable to obtain sufficient and appropriate audit evidence, the auditor should give disclaimer of opinion as per SA 705.

In the present case, the statutory auditor of the company is unable to extract correct data and reports from the SAP system for conduct of audit. Also, such data and reports are not available manually. As such, the statutory auditor of Delightful Ltd. should give a disclaimer of opinion.

5.4 Which type of opinion is appropriate?

The decision regarding which type of modified opinion is appropriate depends upon:

(a) The nature of the matter giving rise to the modification, that is, whether the financial statements are materially misstated or, in the case of an inability to obtain sufficient appropriate audit evidence, may be materially misstated; and

(b) The auditor's judgement about the pervasiveness of the effects or possible effects of the matter on the financial statements.

The table below illustrates how the auditor's judgement about the nature of the matter giving rise to the modification, and the pervasiveness of its effects or possible effects on the financial statements, affects the type of opinion to be expressed.

Nature of Matter Giving Rise to the Modification	Auditor's Judgement about the Pervasiveness of the Effects or Possible Effects on the Financial Statements	
	Material but not Pervasive	Material and Pervasive
Financial statements are materially misstated	Qualified opinion	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion	Disclaimer of opinion

5.5 Consequence of an Inability to Obtain Sufficient Appropriate Audit Evidence Due to a Management-Imposed Limitation after the Auditor Has Accepted the Engagement

- If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers is likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.
- If management refuses to remove the limitation referred above, the auditor shall communicate the matter to those charged with governance, unless all of those charged with governance are involved in managing the entity and determine whether it is possible to perform alternative procedures to obtain sufficient appropriate audit evidence.
- If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall determine the implications as follows:

  (a) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive, the auditor shall qualify the opinion; or

(b) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall:

(i) Withdraw from the audit, where practicable and possible under applicable law or regulation; or

(ii) If withdrawal from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.

- If the auditor withdraws as contemplated by point (b)(i) above, before withdrawing, the auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion.

Test Your Understanding 3

CA. Sarasbhai Patel, while conducting audit of an entity, feels that there is an atmosphere of non-cooperation all around. He has not been provided with necessary support for attending inventory count process of entity as at year end. Besides, CFO is not providing him present addresses of customers as well as suppliers for sending external confirmations. Even mail ids have not been provided on the pretext of business confidentiality.

He was not able to verify revenues of entity due to lack of complete details. For verifying expenses, he has been asking for bills on a sample basis, but staff has been making lame excuses. The matter was brought to knowledge of higher echelons of management, but of no avail. The auditor feels that there could be misstatements and their possible effects would be material and affecting many aspects of financial statements.

Assuming it is not possible to withdraw from engagement, what type of opinion should be expressed by auditor?

- The above matter is depicted in the following diagram:

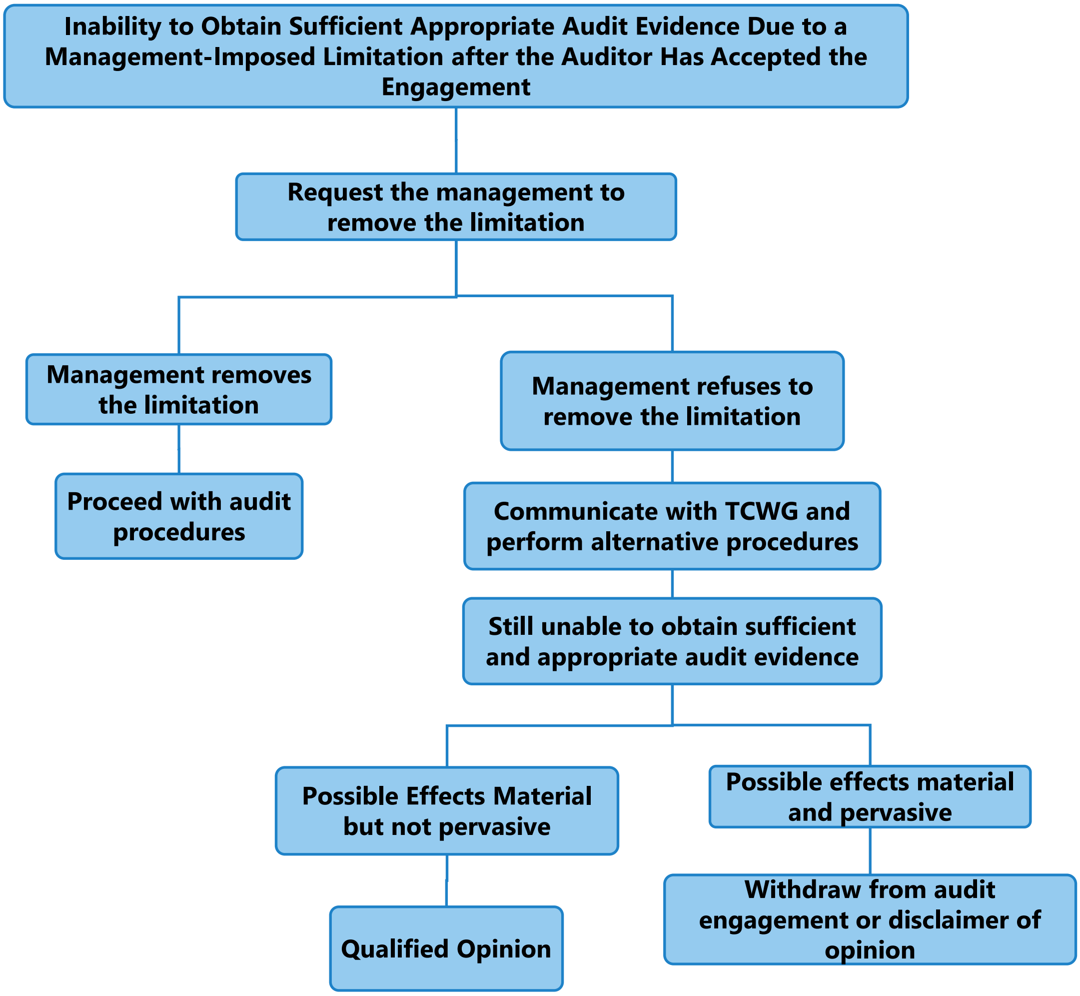


ILLUSTRATION 12

M/s Daisy & Associates are the statutory auditors of Zebra Ltd. for the FY 2021-22. CA Daisy, the engagement partner wants to verify the cash in hand as on 31.03.2022. The cash balance of the company as on 31.03.2022 is ₹ 1,00,000/- and the turnover of the company for the year is ₹ 6 crores. The management of the company informs CA Daisy that such cash verification is not possible as the cashier is on leave for his marriage and no other employee of the company is available as all are busy in year ending activities. Explain the relevant provisions to deal with such a situation.

SOLUTION

If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the scope of the audit that the auditor considers is likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor shall request that management remove the limitation.

In the present case CA Daisy, the statutory auditor is unable to verify the cash in hand of Zebra Ltd. as on 31.03.2022. The same is due to a limitation imposed by the management of Zebra Ltd. which is due to the non availability of the cashier. In such situation, CA Daisy should perform alternate procedures to verify the cash on hand of the company. Further, CA Daisy should consider the impact on the auditor's report and may consider issuing a qualified opinion in this case.

5.6 Form and Content of the Auditor's Report When the Opinion is Modified

Auditor's Opinion

When the auditor modifies the audit opinion, the auditor shall use the heading "Qualified Opinion," "Adverse Opinion," or "Disclaimer of Opinion," as appropriate, for the Opinion section.

Qualified Opinion

When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state that, in the auditor's opinion, **except for the effects of the matter(s) described in the Basis for Qualified Opinion section,**

(a) When reporting in accordance with a fair presentation framework, the accompanying financial statements present fairly, in all material respects (or give a true and fair view of) […] in accordance with [the applicable financial reporting framework]; or

(b) When reporting in accordance with a compliance framework, the accompanying financial statements have been prepared, in all material respects, in accordance with [the applicable financial reporting framework].

When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase "except for the possible effects of the matter(s) …" for the modified opinion.

Adverse Opinion.

When the auditor expresses an adverse opinion, the auditor shall state that, in the auditor's opinion, **because of the significance of the matter(s) described in the Basis for Adverse Opinion section,**

(a) When reporting in accordance with a fair presentation framework, the accompanying financial statements do not present fairly (or give a true and fair view of) […] in accordance with [the applicable financial reporting framework]; or

(b) When reporting in accordance with a compliance framework, the accompanying financial statements have not been prepared, in all material respects, in accordance with [the applicable financial reporting framework].

Disclaimer of Opinion

When the auditor disclaims an opinion due to an inability to obtain sufficient appropriate audit evidence, the auditor shall:

(a) State that the auditor does not express an opinion on the accompanying financial statements;

(b) State that, because of the significance of the matter(s) described in the Basis for Disclaimer of Opinion section, **the auditor has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements;** and

(c) Amend the statement required by SA 700 (Revised), which indicates that the financial statements have been audited, to state that the auditor was engaged to audit the financial statements.

5.7 Basis for Opinion

When the auditor modifies the opinion on the financial statements, the auditor shall, in addition to the specific elements required by SA 700 (Revised):

Amend the heading "Basis for Opinion" required by SA 700 (Revised) to "Basis for Qualified Opinion," "Basis for Adverse Opinion," or"Basis for Disclaimer of Opinion," as appropriate; and

Within this section, include a description of the matter giving rise to the modification.

- If there is a material misstatement of the financial statements that relates to specific amounts in the financial statements (including quantitative disclosures in the notes to the financial statements), the auditor shall include in the Basis for Opinion section a description and quantification of the financial effects of the misstatement, unless impracticable.
- If it is not practicable to quantify the financial effects, the auditor shall so state in this section.
- If there is a material misstatement of the financial statements that relates to narrative disclosures, the auditor shall include in the Basis for Opinion section an explanation of how the disclosures are misstated.
- If there is a material misstatement of the financial statements that relates to the non-disclosure of information required to be disclosed, the auditor shall:
  - (a) Discuss the non-disclosure with those charged with governance;
  - (b) Describe in the Basis for Opinion section the nature of the omitted information; and
  - (c) Unless prohibited by law or regulation, include the omitted disclosures, provided it is practicable to do so and the auditor has obtained sufficient appropriate audit evidence about the omitted information.
- If the modification results from an inability to obtain sufficient appropriate audit evidence, the auditor shall include in the Basis for Opinion section the reasons for that inability.

- When the auditor expresses a qualified or adverse opinion, the auditor shall amend the statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion required by SA 700 (Revised) to include the word "qualified" or "adverse", as appropriate.
- When the auditor disclaims an opinion on the financial statements, the auditor's report shall not include the following elements required by SA 700 (Revised).

  (a) A reference to the section of the auditor's report where the auditor's responsibilities are described; and

  (b) A statement about whether the audit evidence obtained is sufficient and appropriate to provide a basis for the auditor's opinion.

  Even if the auditor has expressed an adverse opinion or disclaimed an opinion on the financial statements, the auditor shall describe in the Basis for Opinion section the reasons for any other matters of which the auditor is aware that would have required a modification to the opinion, and the effects thereof.

5.8 Description of Auditor's Responsibilities for the Audit of the Financial Statements When the Auditor Disclaims an Opinion on the Financial Statements

When the auditor disclaims an opinion on the financial statements due to an inability to obtain sufficient appropriate audit evidence, the auditor shall amend the description of the auditor's responsibilities required by SA 700 (Revised) to include only the following:

(a) A statement that the auditor's responsibility is to conduct an audit of the entity's financial statements in accordance with Standards on Auditing and to issue an auditor's report;

(b) A statement that, however, because of the matter(s) described in the Basis for Disclaimer of Opinion section, the auditor was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements; and

(c) The statement about auditor independence and other ethical responsibilities required by SA 700 (Revised).

5.9 Considerations When the Auditor Disclaims an Opinion on the Financial Statements

Unless required by law or regulation, when the auditor disclaims an opinion on the financial statements, the auditor's report shall not include a Key Audit Matters section in accordance with SA 701.

5.10 Communication with Those Charged with Governance

When the auditor expects to modify the opinion in the auditor's report, the auditor shall communicate with those charged with governance the circumstances that led to the expected modification and the wording of the modification.

ILLUSTRATION 13

M/s Sun Moon & Associates are the statutory auditors of Venus Ltd. for the FY 2021-22. Owing to the pervasive nature of material misstatements in the financial statements of the company, CA Moon, the engagement partner decided to give an adverse opinion. Explain the responsibility of CA Moon with respect to communication with those charged with governance.

SOLUTION

CA Moon, being the statutory auditor of Venus Ltd. should communicate with those charged with governance about the circumstances that led to the expected modification i.e. an adverse opinion. Further the wording of such modification also needs to be discussed.

6. EMPHASIS OF MATTER PARAGRAPHS AND OTHER MATTER PARAGRAPHS IN THE INDEPENDENT AUDITOR'S REPORT.

SA 706 deals with additional communication in the auditor's report when the auditor considers it necessary to:

(a) Draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements; or

(b) Draw users' attention to any matter or matters other than those presented or disclosed in the financial statements that are relevant to user's understanding of the audit, the auditor's responsibilities or the auditor's report.

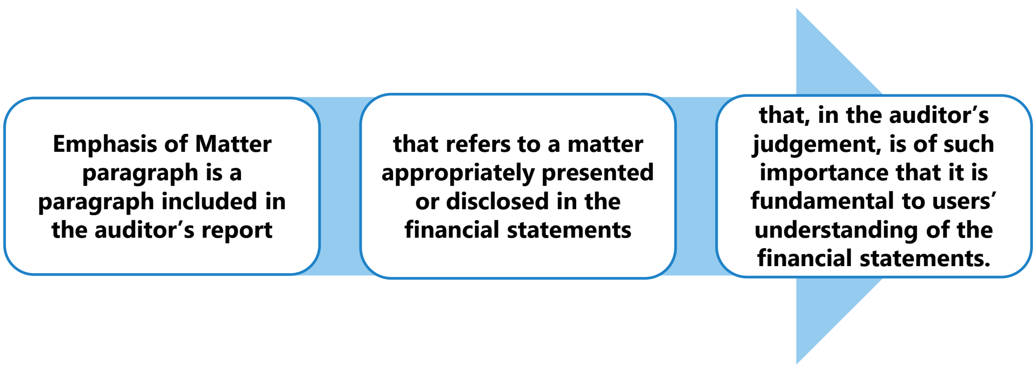
6.1 Objective of the Auditor as per SA 706

As per SA 706 (Revised) on "Emphasis of Matter Paragraphs and Other Matter Paragraphs In The Independent Auditor's Report", the objective of the auditor, having formed an opinion on the financial statements, is to draw users' attention, when in the auditor's judgement it is necessary to do so, by way of clear additional communication in the auditor's report, to:

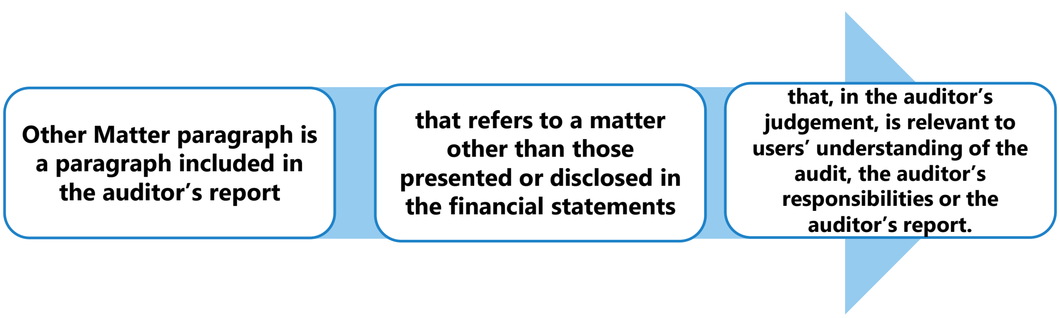
(a) A matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to users' understanding of the financial statements; or

(b) As appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

Definition of Emphasis of Matter Paragraph



Definition of Other Matter paragraph



6.2 Emphasis of Matter Paragraphs in the Auditor's Report

If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements, the auditor shall include an Emphasis of Matter paragraph in the auditor's report provided:

(a) The auditor would not be required to modify the opinion in accordance with SA 705 (Revised) as a result of the matter; and

(b) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.

6.2.1 Separate section for Emphasis of Matter paragraph

When the auditor includes an Emphasis of Matter paragraph in the auditor's report, the auditor shall:

(a) Include the paragraph within a separate section of the auditor's report with an appropriate heading that includes the term "Emphasis of Matter";

(b) Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph shall refer only to information presented or disclosed in the financial statements; and

(c) Indicate that the auditor's opinion is not modified in respect of the matter emphasized.

Some examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph.

- An uncertainty relating to the future outcome of exceptional litigation or regulatory action.
- A significant subsequent event that occurs between the date of the financial statements and the date of the auditor's report.
- Early application (where permitted) of a new accounting standard that has a material effect on the financial statements.
- A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position.

6.3 The inclusion of an Emphasis of Matter paragraph in the auditor's report does not affect the auditor's opinion

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.

ILLUSTRATION 14

Lomaxe Ltd. is a company engaged in the business of manufacture of candles. CA Kamalnath is the statutory auditor of the company for the FY 2021-22. During the year under audit, there was a fire in the company's factory as a result of which, some of the company's plant and machinery was destroyed. The same was disclosed by the company in the notes to accounts annexed to the financial statements for the year ending 31.03.2022. CA Kamalnath decided to communicate this matter in the auditor's report as he is of the view that the matter is of such importance that it is fundamental to the user's understanding of the financial statements. Help CA Kamalnath to deal with this situation in the auditor's report.

SOLUTION

In the present case there is a need to add Emphasis on Matter Paragraph in the Auditor's Report. The draft of the same is as under:

Emphasis of Matter – Effects of Fire in Company's Factory

We draw attention to Note Y of the financial statements, which describes the effects of a fire in the Company's factory. Our opinion is not modified in respect of this matter.

6.4 Other Matter Paragraphs in the Auditor's Report

If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report, the auditor shall include an Other Matter paragraph in the auditor's report, provided:

(a) This is not prohibited by law or regulation; and

(b) When SA 701 applies, the matter has not been determined to be a key audit matter to be communicated in the auditor's report.

6.4.1 Separate section for Other Matter paragraph

When the auditor includes an Other Matter paragraph in the auditor's report, the auditor shall include the paragraph within a separate section with the heading "Other Matter," or other appropriate heading.

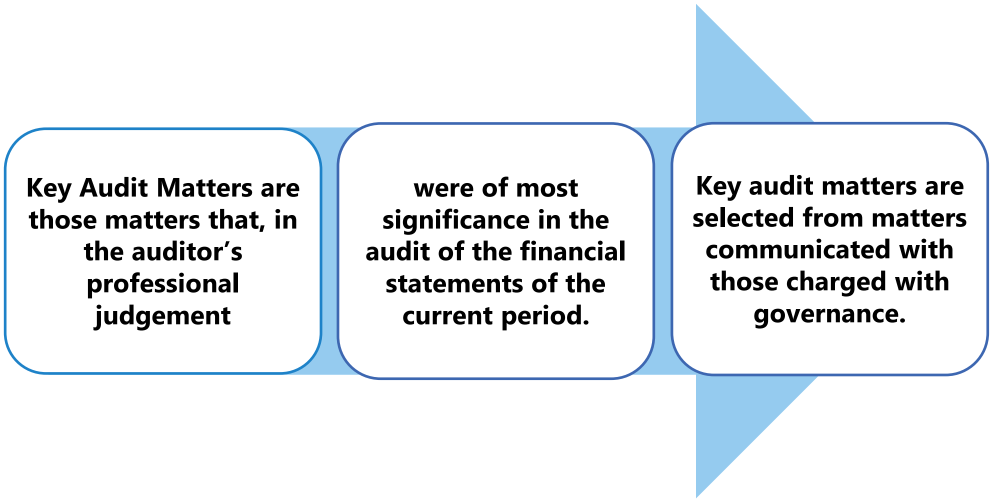
6.5 Communication with Those Charged with Governance

If the auditor expects to include an Emphasis of Matter or an Other Matter paragraph in the auditor's report, the auditor shall communicate with those charged with governance regarding this expectation and the wording of this paragraph.

7. COMMUNICATING KEY AUDIT MATTERS IN THE INDEPENDENT AUDITOR'S REPORT (SA 701)

SA 701 deals with the auditor's responsibility to communicate key audit matters in the auditor's report. It is intended to address both the auditor's judgement as to what to communicate in the auditor's report and the form and content of such communication.

Definition of Key Audit Matter



7.1 Purpose of Communicating Key Audit Matters

As per SA 701, "Communicating Key Audit Matters in the Auditor's Report", the purpose of communicating key audit matters is to enhance the communicative value of the auditor's report by providing greater transparency about the audit that was performed. Communicating key audit matters provides additional information to intended users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial statements of the current period. Communicating key audit matters may also assist intended users in understanding the entity and areas of significant management judgement in the audited financial statements.

7.2 Objectives of the Auditor regarding Key Audit Matters

As per SA 701, "Communicating Key Audit Matters in The Independent Auditor's Report", the objectives of the auditor are to determine key audit matters and, having formed an opinion on the financial statements, communicate those matters by describing them in the auditor's report.

7.3 Determining Key Audit Matters

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:

Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315.

Significant auditor judgements relating to areas in the financial statements that involved significant management judgement, including accounting estimates that have been identified as having high estimation uncertainty.

The effect on the audit of significant events or transactions that occurred during the period.

The auditor shall determine which of the matters determined, as stated above, were of most significance in the audit of the financial statements of the current period and therefore are the key audit matters.

7.4 Communicating Key Audit Matters

The auditor shall describe each key audit matter, using an appropriate subheading, in a separate section of the auditor's report under the heading "Key Audit Matters". The introductory language in this section of the auditor's report shall state that:

(a) Key audit matters are those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial statements [of the current period]; and

(b) These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.

7.5 Communicating Key Audit Matters- not a substitute for disclosure in the Financial Statements etc.

Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not:

(a) A substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;

(b) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised);

(c) A substitute for reporting in accordance with SA 570 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; or

(d) A separate opinion on individual matters.

7.6 Communication with Those Charged with Governance

The auditor shall communicate with those charged with governance:

(a) Those matters the auditor has determined to be the key audit matters; or

(b) If applicable, depending on the facts and circumstances of the entity and the audit, the auditor's determination that there are no key audit matters to communicate in the auditor's report.

Example:

The following illustrates the presentation in the auditor's report if the auditor has determined there are no key audit matters to communicate:

Key Audit Matters

[Except for the matter described in the Basis for Qualified (Adverse) Opinion section or Material Uncertainty Related to Going Concern section,] We have determined that there are no [other] key audit matters to communicate in our report.

SA 701 AT A GLANCE

APPLICABILITY OF SA 701	➢ It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication ➢ This SA applies to audits of complete sets of general purpose financial statements of : ✎ listed entities and ✎ circumstances when the auditor otherwise decides to communicate key audit matters in the auditor's report and ✎ required by law or regulation to communicate key audit matters in the auditor's report However, SA 705 (Revised) prohibits the auditor from communicating key audit matters when the auditor disclaims an opinion on the financial statements, unless such reporting is required by law or regulation

DETERMINING KEY AUDIT MATTERS: 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:

(a)Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with SA 315

(b) 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.

(c) The effect on the audit of significant events or transactions that occurred during the period.

COMMUNICATING KEY AUDIT MATTERS:	The introductory language in this section of the auditor's report shall state that: **(a) Key audit matters are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements [of the current period]; and.** **(b) These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditor's opinion thereon, and the auditor does not provide a separate opinion on these matters.**

AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS- A BIRD'S EYE VIEW

The following table gives a summary of the Standards on Auditing related to audit reporting:

Standard on Auditing	Name of SA	Matters dealt with (Scope)
SA 700 (Revised)	Forming an Opinion and Reporting on Financial Statements	• The auditor's responsibility to form an opinion on financial statements. • The form and content of the Auditor's Report.

SA 705 (Revised)	Modifications to the Opinion in the Independent Auditor's Report	• Auditor's responsibility to issue an appropriate report in circumstances when auditor concludes that a modification to auditor's opinion is necessary.
		• Three types of modified opinion
		  • A Qualified Opinion
		  • An adverse opinion
		  • A disclaimer of opinion

SA 701	Communicating Key Audit Matters in the Independent Auditor's Report	• The auditor's responsibility to communicate key audit matters in the auditor's report.

		• What to communicate and the form and content of such communication.
SA 706 (Revised)	Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report	• Additional communication in the auditor's report when the auditor considers it necessary to draw users' attention to a matter: • Presented or disclosed in the financial statements and which is fundamental for the user's understanding. • Not presented or disclosed in the financial statements and which are relevant for the user's understanding.

8. STANDARD ON AUDITING - 710, "COMPARATIVE INFORMATION - CORRESPONDING FIGURES AND COMPARATIVE FINANCIAL STATEMENTS"

This Standard on Auditing (SA) deals with the auditor's responsibilities regarding comparative information in an audit of financial statements. When the financial statements of the prior period have been audited by a predecessor auditor or were not audited, the requirements and guidance in SA 510 regarding opening balances also apply.

8.1 The Nature of the Comparative Information

The nature of the comparative information that is presented in an entity's financial statements depends on the requirements of the applicable financial reporting framework. There are two different broad approaches to the auditor's reporting responsibilities in respect of such comparative information: corresponding figures and comparative financial statements. The approach to be adopted is often specified by law or regulation but may also be specified in the terms of engagement.

The essential audit reporting differences between the approaches are:

(a) For corresponding figures, the auditor's opinion on the financial statements refers to the current period only; whereas

(b) For comparative financial statements, the auditor's opinion refers to each period for which financial statements are presented.

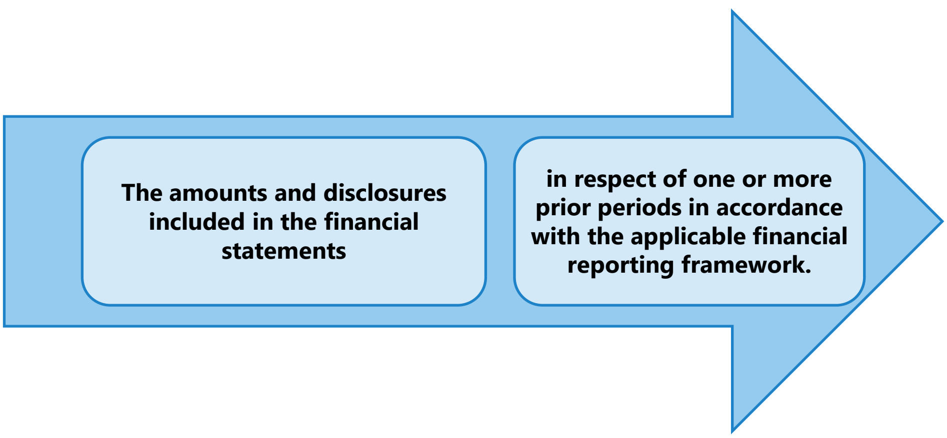
Objectives

As per SA 710, the objectives of the auditor are:

(a) To obtain sufficient appropriate audit evidence about whether the comparative information included in the financial statements has been presented, in all material respects, in accordance with the requirements for comparative information in the applicable financial reporting framework; and

(b) To report in accordance with the auditor's reporting responsibilities.

Definition of Comparative Information:



8.2 Audit Procedures regarding comparative information

- The auditor shall determine whether the financial statements include the comparative information required by the applicable financial reporting framework and whether such information is appropriately classified. For this purpose, the auditor shall evaluate whether:

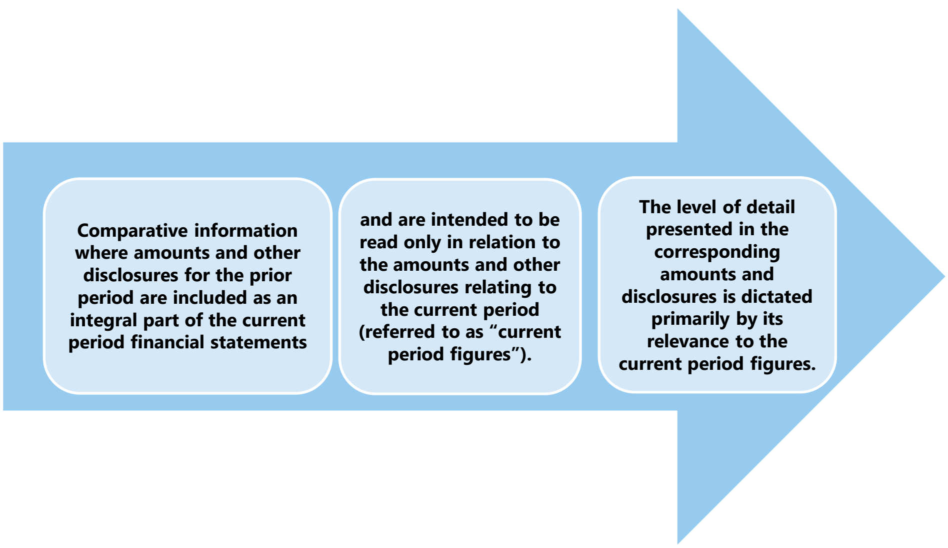
(a) The comparative information agrees with the amounts and other disclosures presented in the prior period; and

(b) The accounting policies reflected in the comparative information are consistent with those applied in the current period or, if there have been changes in accounting policies, whether those changes have been properly accounted for and adequately presented and disclosed.

- If the auditor becomes aware of a possible material misstatement in the comparative information while performing the current period audit, the auditor shall perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists. If the auditor had audited the prior period's financial statements, the auditor shall also follow the relevant requirements of SA 560.
- As required by SA 580, the auditor shall request written representations for all periods referred to in the auditor's opinion. The auditor shall also obtain a specific written representation regarding any prior period item that is separately disclosed in the current year's statement of profit and loss.

8.3 Audit Reporting regarding Corresponding Figures

Definition of Corresponding figures:



When corresponding figures are presented, the auditor's opinion shall not refer to the corresponding figures except in the following circumstances:

1. **If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion** and the matter which gave rise to the modification is unresolved, the auditor shall modify the auditor's opinion on the current period's financial statements. In the Basis for Modification paragraph in the auditor's report, the auditor shall either:

   (a) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or

   (b) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

2. **If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements** on which an unmodified opinion has been previously issued, the auditor shall verify whether the misstatement has been dealt with as required under the applicable financial reporting framework and, if that is not the case, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein.

3. **Prior Period Financial Statements Not Audited-** If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph in the auditor's report that the corresponding figures are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.

   Prior Period Financial Statements Audited by a Predecessor Auditor

   If the financial statements of the prior period were audited by a predecessor auditor and the auditor is permitted by law or regulation to refer to the predecessor auditor's report on the corresponding figures and decides to do so, the auditor shall state in an Other Matter paragraph in the auditor's report:

(a) That the financial statements of the prior period were audited by the predecessor auditor;

(b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefore; and

(c) The date of that report.

8.4 Comparative Financial Statements

Definition: Comparative information where amounts and other disclosures for the prior period are included for comparison with the financial statements of the current period but, if audited, are referred to in the auditor's opinion. The level of information included in those comparative financial statements is comparable with that of the financial statements of the current period.

Auditor's opinion- to refer each period: When comparative financial statements are presented, the auditor's opinion shall refer to each period for which financial statements are presented and on which an audit opinion is expressed.

When reporting on prior period financial statements in connection with the current period's audit, if the auditor's opinion on such prior period financial statements differs from the opinion the auditor previously expressed, the auditor shall disclose the substantive reasons for the different opinion in an Other Matter paragraph in accordance with SA 706.

Prior Period Financial Statements Audited by a Predecessor Auditor

If the financial statements of the prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period's financial statements, the auditor shall state in an Other Matter paragraph:

(a) That the financial statements of the prior period were audited by a predecessor auditor;

(b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefor; and

(c) The date of that report,

unless the predecessor auditor's report on the prior period's financial statements is revised with the financial statements.

If the auditor concludes that a material misstatement exists that affects the prior period financial statements on which the predecessor auditor had previously reported without modification, the auditor shall communicate the misstatement with the appropriate level of management and those charged with governance and request that the predecessor auditor be informed. If the prior period financial statements are amended, and the predecessor auditor agrees to issue a new auditor's report on the amended financial statements of the prior period, the auditor shall report only on the current period.

Prior Period Financial Statements Not Audited

If the prior period financial statements were not audited, the auditor shall state in an Other Matter paragraph that the comparative financial statements are unaudited. Such a statement does not, however, relieve the auditor of the requirement to obtain sufficient appropriate audit evidence that the opening balances do not contain misstatements that materially affect the current period's financial statements.

9. AUDIT OF BRANCH OFFICE ACCOUNTS

As per **section 128(1)** of the Companies Act, 2013, every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year which give a true and fair view of the state of the affairs of the company, including that of its branch office or offices, if any, and explain the transactions effected both at the registered office and its branches and such books shall be kept on accrual basis and according to the double entry system of accounting.

It may be noted that all or any of the books of account aforesaid and other relevant papers may be kept at such other place in India as the Board of Directors may decide and where such a decision is taken, the company shall, within 7 days thereof, file with the Registrar a notice in writing giving the full address of that other place.

Students may also note that the company may keep such books of account or other relevant papers in electronic mode in such manner as may be prescribed.

Sub-section (2) provides that where a company has a branch office in India or outside India, it shall be deemed to have complied with the provisions of sub-section (1), if proper books of account relating to the transactions effected at the branch office are kept at that office and proper summarised returns periodically are sent by the branch office to the company at its registered office or the other place referred in (1).

Further, sub-section (8) of section 143 of the Companies Act, 2013, prescribes the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor. Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company (herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section 139, or where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country and the duties and powers of the company' s auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as may be prescribed:

It may be noted that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

Further as per **rule 12 of the Companies (Audit and Auditors) Rules, 2014,** the branch auditor shall submit his report to the company's auditor and reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.

For better understanding, let us now have a look at the following definitions:

- **Principal auditor** means the auditor with responsibility for reporting on the financial information of an entity when that financial information includes the financial information of one or more components audited by another auditor.
- **Other auditor** means an auditor, other than the principal auditor, with responsibility for reporting on the financial information of a component which is included in the financial information audited by the principal auditor.

- **Component** means a division, branch, subsidiary, joint venture, associated enterprises or other entity whose financial information is included in the financial information audited by the principal auditor.

Using the Work of another Auditor*:* When the accounts of the branch are audited by a person other than the company's auditor (or principal auditor), there is need for a clear understanding of the role of such other auditor and the company's auditor in relation to the audit of the accounts of the branch and the audit of the company as a whole; also, there is great necessity for a proper rapport between these two auditors for the purpose of an effective audit. In recognition of these needs, the Council of the Institute of Chartered Accountants of India has dealt with these issues in **SA 600, "Using the Work of another Auditor**". It makes clear that in certain situations, the statute governing the entity may confer a right on the principal auditor to visit a component and examine the books of account and other records of the said component, if he thinks it necessary to do so. Where another auditor has been appointed for the component, the principal auditor would normally be entitled to rely upon the work of such auditor unless there are special circumstances to make it essential for him to visit the component and/or to examine the books of account and other records of the said component. Further, it requires that the principal auditor should perform procedures to obtain sufficient appropriate audit evidence, that the work of the other auditor is adequate for the principal auditor's purposes, in the context of the specific assignment. When using the work of another auditor, the principal auditor should ordinarily perform the following procedures:

(a) advise the other auditor of the use that is to be made of the other auditor's work and report and make sufficient arrangements for co-ordination of their efforts at the planning stage of the audit. The principal auditor would inform the other auditor of matters such as are as requiring special consideration, procedures for the identification of inter -component transactions that may require disclosure and the time-table for completion of audit; and

(b) advise the other auditor of the significant accounting, auditing and reporting requirements and obtain representation as to compliance with them.

The principal auditor might discuss with the other auditor the audit procedures applied or review a written summary of the other auditor's procedures and findings which may be in the form of a completed questionnaire or check-list. The principal auditor may also wish to visit the other auditor. The nature, timing and extent of procedures will depend on the circumstances of the engagement and the principal auditor's knowledge of the professional competence of the other auditor. This knowledge may have been enhanced from the review of the previous audit work of the other auditor.

Test Your Understanding 4

CA. Dicky Yadav is auditor of a company having four branches. The four branches are audited by another auditor CA. Yamini Jain. The reports in respect of accounts of branches examined by her have already been sent to company auditor. During the course of audit, CA Dicky Yadav asks the branch auditor to share with her summary of audit procedures and findings in respect of accounts of branches examined. CA. Yamini Jain feels it as encroachment of her domain. Discuss the issue.

10. JOINT AUDIT

The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Joint audit basically implies pooling together the resources and expertise of more than one firm of auditors to render an expert job in a given time period which may be difficult to accomplish acting individually. It essentially involves sharing of the total work. This is by itself a great advantage.

In specific terms the **advantages** that flow may be the following:

(i) Sharing of expertise.

(ii) Advantage of mutual consultation.

(iii) Lower workload.

(iv) Better quality of performance.

(v) Improved service to the client.

(vi) In respect of multi-national companies, the work can be spread using the expertise of the local firms which are in a better position to deal with detailed work and the local laws and regulations.

(vii) Lower staff development costs.

(viii) Lower costs to carry out the work.

(ix) A sense of healthy competition towards a better performance.

The general **disadvantages** may be the following:

(i) The fees being shared.

(ii) Psychological problem where firms of different standing are associated in the joint audit.

(iii) General superiority complex of some auditors.

(iv) Problems of co-ordination of the work.

(v) Areas of work of common concern being neglected.

(vi) Uncertainty about the liability for the work done.

The Institute of Chartered Accountants of India has issued Standard on Auditing (SA) 299 (Revised), "Joint Audit of Financial Statements" which lays down the principles for effective conduct of joint audit to achieve the overall objectives of the auditor as laid down in SA 200 "Overall Objectives of the Independent Auditor and the conduct of an audit in accordance with Standards on Auditing". This Standard deals with the special considerations in carrying out audit by joint auditors. It requires that–

(i) the engagement partner and other key members of the engagement team from each of the joint auditors should be involved in planning the audit.

(ii) the joint auditors should jointly establish an overall audit strategy which sets the scope, timing and direction of the audit, and also guides the development of the audit plan.

(iii) before the commencement of the audit, the joint auditors should discuss and develop a joint audit plan. In developing the joint audit plan, the joint auditors should:

  (a) identify division of audit areas and common audit areas;

  (b) ascertain the reporting objectives of the engagement;

  (c) consider and communicate among all joint auditors the factors that are significant in directing the engagement team's efforts;

  (d) consider the results of preliminary engagement activities, or similar engagements performed earlier.

(e) ascertain the nature, timing and extent of resources necessary to accomplish the engagement.

(iv) each of the joint auditors should consider and assess the risks of material misstatement and communicate to other joint auditors.

(v) the joint auditors should discuss and document the nature, timing, and the extent of the audit procedures for (I) common and (II) specific allotted areas of audit to be performed.

(vi) the joint auditors should obtain common engagement letter and common management representation letter.

(vii) the work allocation document should be signed by all the joint auditors and communicated to those charged with governance.

It further states that, in respect of audit work divided among the joint auditors, each joint auditor shall be responsible only for the work allocated to such joint auditor including proper execution of the audit procedures. On the other hand, all the joint auditors shall be jointly and severally responsible for:

(i) the audit work which is not divided among the joint auditors and is carried out by all joint auditors;

(ii) decisions taken by all the joint auditors under audit planning in respect of common audit areas;

(iii) matters which are brought to the notice of the joint auditors by any one of them and there is an agreement among the joint auditors on such matters;

(iv) examining that the financial statements of the entity comply with the requirements of the relevant statutes;

(v) presentation and disclosure of the financial statements as required by the applicable financial reporting framework;

(vi) ensuring that the audit report complies with the requirements of the relevant statutes, applicable Standards on Auditing and other relevant pronouncements issued by ICAI.

In case a joint auditor comes across matters which are relevant to the areas of responsibility of other joint auditors and which deserve their attention, or which require disclosure or require discussion with, or application of judgment by other joint auditors, the said joint auditor shall communicate the same to all the other joint auditors in writing prior to the completion of the audit.

It may be noted that the joint auditors are required to issue **common audit report.** However, where the joint auditors are in disagreement with regard to the opinion or any matters to be covered by the audit report, they shall express their opinion in a **separate audit report.** In such circumstances, the audit report(s) issued by the joint auditor(s) shall make a reference to each other's audit report(s).

[Note: Student may refer SA 299 (revised) "Joint Audit of Financial Statements" for comprehensive knowledge.]

11. REPORTING REQUIREMENTS UNDER THE COMPANIES ACT, 2013

Section 143 of the Companies Act, 2013 contains, inter alia, reporting requirements of auditor of a company in form of duties.

(1) Reporting requirement relating to matters stated in section 143(1)

Under section 143(1), auditor shall inquire into following matters given as under: -

(a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;

(b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;

(c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company;

(d) whether loans and advances made by the company have been shown as deposits;

(e) whether personal expenses have been charged to revenue account;

(f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading.

However, the auditor is not required to report on the matters specified in sub-section (1) unless he has any special comments to make on any of the items referred to therein. If he is satisfied as a result of the inquiries, he has no further duty to report that he is so satisfied. Therefore, it could be said that the auditor should make a report to the members in case he finds answer to any of these matters in adverse.

(2) Reporting on accounts examined

Under provisions of Section 143(2), the auditor shall make a report to the members of the company on the accounts examined by him and on every financial statements which are required by or under this Act to be laid before the company in general meeting and the report shall after taking into account the provisions of this Act, the accounting and auditing standards and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under sub-section (11).

Further, auditor has to report whether to best of his information and knowledge, the said accounts, financial statements give a true and fair view of ***the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year and such other matters as prescribed under Rule 11 of the*** **Companies (Audit and Auditors) Rules, 2014.**

Further, in terms of section 143(3), the auditor's report shall also state

(a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;

(b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;

(c) whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditors has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

(d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

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

(g) whether any director is disqualified from being appointed as a director under sub- section (2) of the section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate internal financial controls ***with reference to financial statements*** in place and the operating effectiveness of such controls;

However, it may be noted that the reporting requirement on adequacy of internal financial controls (IFCs) with reference to financial statements shall **not** be applicable to a private company which is a–

(i) One person company; or

(ii) Small company; or

(iii) Company having turnover less than ₹ 50 crore as per latest audited financial statement and having aggregate borrowings from banks or financial institutions or any body corporate at any point of time during the financial year less than ₹ 25 crore.

(j) such other matters as are prescribed **in Rule 11 of the Companies (Audit and Auditors) Rules, 2014** which are as under:-

(a) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

(b) whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;

(c) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

[(d) (i) Whether the management has represented that, to the best of it's 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 company 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 company ("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 it's knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been received by the company from any person(s) or entity(ies), including foreign entities ("Funding Parties") with the understanding, whether recorded in writing or otherwise, that the company 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 (1) and (2) contain any material misstatement.

(e) Whether the dividend declared or paid during the year by the company is in compliance with section 123 of the Companies Act, 2013.

(f) Whether the company 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.

While reporting, where any of the matters required to be included in the audit report is answered in the negative or with a qualification, the report shall state the reasons therefor in terms of Section 143(4). Further, every auditor shall comply with the auditing standards as required under section 143(9).

(3) Reporting on any other matter specified by Central Government: As per **section 143(11)**, the Central Government may, in consultation with the National Financial Reporting Authority, by general or special order, direct, in respect of such class or description of companies, as may be specified in the order, that the auditor's report shall also include a statement on such matters as may be specified therein.

[Note: Students may note that Companies (Auditor's Report) Order, 2020 has been notified in this perspective which is discussed later in this chapter as Reporting under Companies (Auditor's Report) Order, 2020]

(4) Reporting on frauds:

A. Reporting to the Central Government- As per **section 143(12)** of the Companies Act, 2013 read with **Rule 13** of the Companies (Audit and Auditors) Rules, 2014, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of ₹ 1 crore or above, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as prescribed.

B. **Reporting to the Audit Committee or Board-** In case of a fraud involving lesser than the specified amount [i.e. less than ₹ 1 crore], the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as prescribed.

Besides, auditor has also to report matters pertaining to fraud at point (xi) of paragraph 3 of CARO,2020 which is discussed subsequently.

12. REPORTING UNDER COMPANIES AUDITOR'S REPORT ORDER, 2020 [CARO, 2020]

In exercise of the powers conferred by sub-section (11) of section 143 of the Companies Act, 2013 (18 of 2013) and in supersession of the Companies (Auditor's Report) Order, 2016, published in the Gazette of India, Extraordinary, Part II, Section 3, Sub-section (ii), vide number S.O. 1228 (E), dated the 29th March, 2016, except as respects things done or omitted to be done before such supersession, the Central Government, after consultation with the National Financial Reporting Authority constituted under section 132 of the Companies Act, 2013, hereby makes the following Order, namely:—

Short title, application and commencement. –

Short title: This Order may be called the Companies (Auditor's Report) Order, 2020.

Application: It shall apply to every company including a foreign company as defined in clause (42) of section 2 of the Companies Act, 2013 (18 of 2013) [hereinafter referred to as the Companies Act], except–

(i) a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);

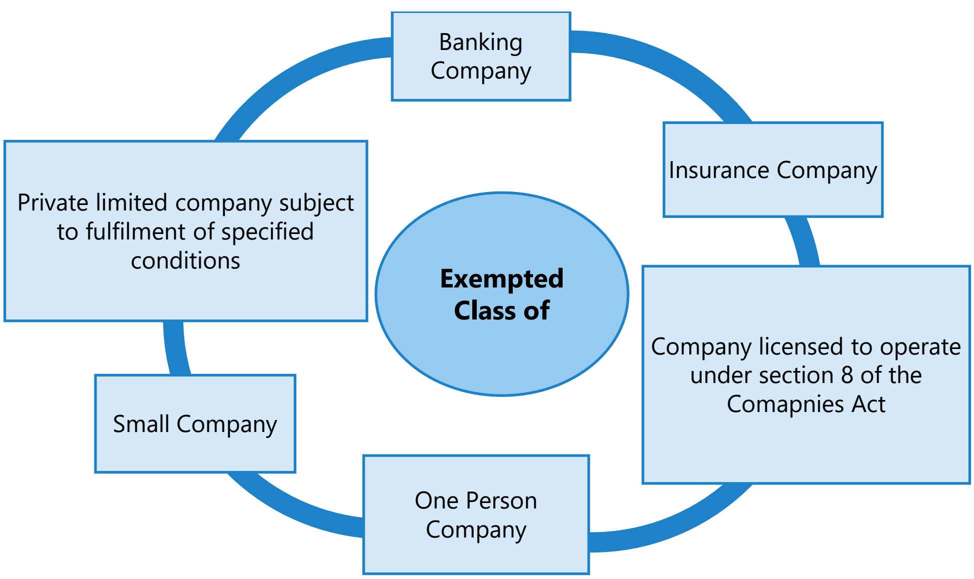
(ii) an insurance company as defined under the Insurance Act,1938 (4 of 1938);

(iii) a company licensed to operate under section 8 of the Companies Act, 2013;

(iv) a One Person Company as defined in clause (62) of section 2 of the Companies Act, 2013 and a small company as defined in clause (85) of section 2 of the Companies Act, 2013; and

(v) a private limited company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than one crore rupees as on the balance sheet date and which does not have total borrowings exceeding one crore rupees from any bank or financial institution at any point of time during the financial year and which does not have a total revenue as disclosed in Scheduled III to the Companies Act (including revenue from discontinuing operations) exceeding ten crore rupees during the financial year as per the financial statements.

Commencement: It shall come into force on the date of its publication in the Official Gazette.



Example

'Educating Child' is a limited company registered under section 8 of the Companies Act, 2013.

In the given case, 'Educating Child' is licensed to operate under section 8 of the Companies Act, 2013. Therefore, CARO, 2020 shall not be applicable to 'Educating Child' accordingly.

Auditor's report to contain matters specified in paragraphs 3 and 4. - Every report made by the auditor under section 143 of the Companies Act, 2013 on the accounts of every company audited by him, to which this Order applies, for the financial years commencing on or after the 1st April, 2019, shall in addition, contain the matters specified in paragraphs 3 and 4, as may be applicable: Provided this Order shall not apply to the auditor's report on consolidated financial statements except clause (xxi) of paragraph 3.

Paragraph 3

Matters to be included in auditor's report. - The auditor's report on the accounts of a company to which this Order applies shall include a statement on the following matters, namely:-

(i) (a) (A) whether the company is maintaining proper records showing full particulars, including quantitative details and situation of Property, Plant and Equipment;

(B) whether the company is maintaining proper records showing full particulars of intangible assets;

(b) whether these Property, Plant and Equipment have been physically verified by the management at reasonable intervals; 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;

(c) whether the title deeds of all the immovable properties (other than properties where the company is the lessee and the lease agreements are duly executed in favour of the lessee) disclosed in the financial statements are held in the name of the company, if not, provide the details thereof in the format below:-

Description of property	Gross carrying value	Held in name of	Whether promoter, director or their relative or employee	Period held –indicate range, where appropriate	Reason for not being held in name of company*
					*also indicate if in dispute

(d) whether the company has revalued its Property, Plant and Equipment (including Right of Use assets) or intangible assets or both during the year and, if so, whether the revaluation is based on the valuation by a Registered Valuer; specify the amount of change, if change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment or intangible assets;

(e) whether any proceedings have been initiated or are pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 (45 of 1988) and rules made thereunder, if so, whether the company has appropriately disclosed the details in its financial statements;

(ii) (a) whether physical verification of inventory has been conducted at reasonable intervals by the management and whether, in the opinion of the auditor, the coverage and procedure of such verification by the management is appropriate; whether any discrepancies of 10% or more in the aggregate for each class of inventory were noticed and if so, whether they have been properly dealt with in the books of account;

(b) whether during any point of time of the year, the company has been sanctioned working capital limits in excess of five crore rupees, in aggregate, from banks or financial institutions on the basis of security of current assets; whether the quarterly returns or statements filed by the company with such banks or financial institutions are in agreement with the books of account of the Company, if not, give details;

(iii) whether during the year the company has made investments in, provided any guarantee or security or granted any loans or advances in the nature of loans, secured or unsecured, to companies, firms, Limited Liability Partnerships or any other parties, if so,-

(a) whether during the year the company has provided loans or provided advances in the nature of loans, or stood guarantee, or provided security to any other entity [not applicable to companies whose principal business is to give loans], if so, indicate-

  (A) the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to subsidiaries, joint ventures and associates;

  (B) the aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to parties other than subsidiaries, joint ventures and associates;

(b) whether the investments made, guarantees provided, security given and the terms and conditions of the grant of all loans and advances in the nature of loans and guarantees provided are not prejudicial to the company's interest;

(c) in respect of loans and advances in the nature of loans, whether the schedule of repayment of principal and payment of interest has been stipulated and whether the repayments or receipts are regular;

(d) if the amount is overdue, state the total amount overdue for more than ninety days, and whether reasonable steps have been taken by the company for recovery of the principal and interest;

(e) whether any loan or advance in the nature of loan granted which has fallen due during the year, has been renewed or extended or fresh loans granted to settle the overdues of existing loans given to the same parties, if so, specify the aggregate amount of such dues renewed or extended or settled by fresh loans and the percentage of the aggregate to the total loans or advances in the nature of loans granted during the year [not applicable to companies whose principal business is to give loans];

(f) whether the company has granted any loans or advances in the nature of loans either repayable on demand or without specifying any terms or period of repayment, if so, specify the aggregate amount, percentage thereof to the total loans granted, aggregate amount of loans granted to Promoters, related parties as defined in clause (76) of section 2 of the Companies Act, 2013;

(iv) in respect of loans, investments, guarantees, and security, whether provisions of sections 185 and 186 of the Companies Act have been complied with, if not, provide the details thereof;

(v) in respect of deposits accepted by the company or amounts which are deemed to be deposits, whether the directives issued by the Reserve Bank of India and the provisions of sections 73 to 76 or any other relevant provisions of the Companies Act and the rules made thereunder, where applicable, have been complied with, if not, the nature of such contraventions be stated; if an order has been passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any court or any other tribunal, whether the same has been complied with or not;

(vi) whether maintenance of cost records has been specified by the Central Government under sub-section (1) of section 148 of the Companies Act and whether such accounts and records have been so made and maintained;

(vii) (a) whether the company is regular in depositing undisputed statutory dues including Goods and Services Tax, 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;

(b) where statutory dues referred to in sub-clause (a) have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned (a mere representation to the concerned Department shall not be treated as a dispute);

(viii) whether any transactions not recorded in the books of account have been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act, 1961 (43 of 1961), if so, whether the previously unrecorded income has been properly recorded in the books of account during the year;

(ix) (a) whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, the period and the amount of default to be reported as per the format below:-

Nature of borrowing, including debt securities	Name of lender	Amount not paid on due date	Whether principal or interest	No. of days delay or unpaid	Remarks, if any
	lender wise details to be provided in case of defaults to banks, financial institutions and Government.				

(b) whether the company is a declared wilful defaulter by any bank or financial institution or other lender;

(c) whether term loans were applied for the purpose for which the loans were obtained; if not, the amount of loan so diverted and the purpose for which it is used may be reported;

(d) whether funds raised on short term basis have been utilised for long term purposes, if yes, the nature and amount to be indicated;

(e) whether the company has taken any funds from any entity or person on account of or to meet the obligations of its subsidiaries, associates or joint ventures, if so, details thereof with nature of such transactions and the amount in each case;

(f) whether the company has raised loans during the year on the pledge of securities held in its subsidiaries, joint ventures or associate companies, if so, give details thereof and also report if the company has defaulted in repayment of such loans raised;

(x) (a) whether moneys raised by way of initial public offer or further public offer (including debt instruments) during the year were applied for the purposes for which those are raised, if not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported;

(b) whether the company has made any preferential allotment or private placement of shares or convertible debentures (fully, partially or optionally convertible) during the year and if so, whether the requirements of section 42 and section 62 of the Companies Act, 2013 have been complied with and the funds raised have been used for the purposes for which the funds were raised, if not, provide details in respect of amount involved and nature of noncompliance;

(xi) (a) whether any fraud by the company or any fraud on the company has been noticed or reported during the year, if yes, the nature and the amount involved is to be indicated;

(b) whether any report under sub-section (12) of section 143 of the Companies Act has been filed by the auditors in Form ADT-4 as prescribed under rule 13 of Companies (Audit and Auditors) Rules, 2014 with the Central Government;

(c) whether the auditor has considered whistle-blower complaints, if any, received during the year by the company;

(xii) (a) whether the Nidhi Company has complied with the Net Owned Funds to Deposits in the ratio of 1:20 to meet out the liability;

(b) whether the Nidhi Company is maintaining ten per cent. unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability;

(c) whether there has been any default in payment of interest on deposits or repayment thereof for any period and if so, the details thereof;

(xiii) whether all transactions with the related parties are in compliance with sections 177 and 188 of the Companies Act, 2013 where applicable and the details have been disclosed in the financial statements, etc., as required by the applicable accounting standards;

(xiv) (a) whether the company has an internal audit system commensurate with the size and nature of its business;

(b) whether the reports of the Internal Auditors for the period under audit were considered by the statutory auditor;

(xv) whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether the provisions of section 192 of the Companies Act, 2013 have been complied with;

(xvi) (a) whether the company is required to be registered under section 45-IA of the Reserve Bank of India Act, 1934 (2 of 1934) and if so, whether the registration has been obtained;

(b) whether the company has conducted any Non-Banking Financial or Housing Finance activities without a valid Certificate of Registration (CoR) from the Reserve Bank of India as per the Reserve Bank of India Act, 1934;

(c) whether the company is a Core Investment Company (CIC) as defined in the regulations made by the Reserve Bank of India, if so, whether it continues to fulfil the criteria of a CIC, and in case the company is an exempted or unregistered CIC, whether it continues to fulfil such criteria;

(d) whether the Group has more than one CIC as part of the Group, if yes, indicate the number of CICs which are part of the Group;

(xvii) whether the company has incurred cash losses in the financial year and in the immediately preceding financial year, if so, state the amount of cash losses;

(xviii) whether there has been any resignation of the statutory auditors during the year, if so, whether the auditor has taken into consideration the issues, objections or concerns raised by the outgoing auditors;

(xix) on the basis of the financial ratios, ageing and expected dates of realisation of financial assets and payment of financial liabilities, other information accompanying the financial statements, the auditor's knowledge of the Board of Directors and management plans, whether the auditor is of the opinion that no material uncertainty exists as on the date of the audit report that company is capable of meeting its liabilities existing at the date of balance sheet as and when they fall due within a period of one year from the balance sheet date;

(xx) (a) whether, in respect of other than ongoing projects, the company has transferred unspent amount to a Fund specified in Schedule VII to the Companies Act, 2013 within a period of six months of the expiry of the financial year in compliance with second proviso to sub-section (5) of section 135 of the said Act;

(b) whether any amount remaining unspent under subsection (5) of section 135 of the Companies Act, 2013 pursuant to any ongoing project, has been transferred to special account in compliance with the provision of sub-section (6) of section 135 of the said Act;

(xxi) whether there have been any qualifications or adverse remarks by the respective auditors in the Companies (Auditor's Report) Order (CARO) reports of the companies included in the consolidated financial statements, if yes, indicate the details of the companies and the paragraph numbers of the CARO report containing the qualifications or adverse remarks.

Paragraph 4. Reasons to be stated for unfavourable or qualified answers. –

(1) Where, in the auditor's report, the answer to any of the questions referred to in paragraph 3 is unfavourable or qualified, the auditor's report shall also state the basis for such unfavourable or qualified answer, as the case may be.

(2) 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.

Test Your Understanding 5

CA. Ravi Patnaik is conducting audit of a company for which reporting requirements under CARO, 2020 are applicable. He finds that cash credit facilities amounting to ₹ 4 crores were released to the company by branch of a bank for meeting its working capital requirements. He finds that out of above funds, ₹ 1 crore have been used by company for installing effluent treatment plant to meet State pollution control Board requirements.

Is there any reporting obligation upon him under CARO,2020?

Example

The company has dispensed with the practice of taking inventory of their inventories at the year-end as in their opinion the exercise is redundant, time consuming and intrusion to normal functioning of the operations. Explain reporting requirement under CARO, 2020.

Reporting for Physical Verification of Inventory:

Clause (ii) of Para 3 of CARO, 2020, requires the auditor to report (a) whether physical verification of inventory has been conducted at reasonable intervals by the management and whether, in the opinion of the auditor, the coverage and procedure of such verification by the management is appropriate; whether any discrepancies of 10% or more in the aggregate for each class of inventory were noticed and if so, whether they have been properly dealt with in the books of account;

(b) whether during any point of time of the year, the company has been sanctioned working capital limits in excess of five crore rupees, in aggregate, from banks or financial institutions on the basis of security of current assets; whether the quarterly returns or statements filed by the company with such banks or financial institutions are in agreement with the books of account of the Company, if not, give details;

In the given case, the above requirement of physical verification of inventory by the management has not been taken place and therefore the auditor should point out the same under CARO, 2020. He may consider the impact on financial statement and report accordingly.

CASE STUDY

M/s AB & Company is a firm of Chartered Accountants based in Mumbai. Mr. A and Mr. B are the Partners of the Firm. The Firm is engaged in various assignments including Audits. The partners are taking a summary of their work in order to prepare themselves to finalize the Audit and issue the audit report to various clients. You are requested to go through the following and answer the questions that follow:

- During the audit of M/s Persistent & Co, Mr. A found that the firm has changed the method of Depreciation from WDV to SLM but has not given the retrospective effect. Mr. A has calculated the difference of depreciation but M/s Persistent & Co. has stated that they don’t want to change the financial statements and if auditor persists they may give the effect in the next financial year.

- During the audit of M/s Dubious Brothers, Mr B observed that the firm had a very large amount of cash sales and there were no details of the customers to whom the sales were made. Further, cash generated was not even deposited into bank regularly. When Mr. B asked the firm to give him an opportunity to count cash, the manager of the firm said that the cash is with the owner and it cannot be made available to the auditor for the checking purpose. The manager also declined to give an opportunity for stock verification to Mr B.
- During the audit of M/s Honest & Associates, Mr. A came to know that the firm has changed its method of valuation of stock. This change has a material impact on the financial statement of the firm. The firm has made relevant disclosures in the financial statements and has given proper accounting treatment to this exercise.

Based on above, answer following questions:

1. *In case of M/s Persistent & Company, what would be an ideal Audit Opinion?*

   (a) *Unmodified*

   (b) *Qualified*

   (c) *Mention the fact in Emphasis of Matter Paragraph*

   (d) *Disclaimer*

2. *In case of M/s Dubious Brothers, what Audit Opinion should the Auditor give?*

   (a) *Qualified*

   (b) *Adverse*

   (c) *Disclaimer*

   (d) *Unmodified*

3. *According to you, what would be appropriate course to take in case of M/s Honest & Associates?*

   (a) *Issue Qualified Opinion*

   (b) *Issue Adverse Opinion*

(c) *Mention the fact of change in method in Emphasis of Matter Paragraph*

(d) *Issue Disclaimer of Opinion*

4. *When the Auditor, after conclusion of an Audit exercise, is of the opinion that there are material misstatements in the Financial Statements, but they are not pervasive, then what should an Auditor do?*

(a) *Issue Unmodified Opinion*

(b) *Issue Qualified Opinion*

(c) *Issue Disclaimer of Opinion*

(d) *Mention it in Emphasis of Matter Paragraph*

5. *When the Auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework, Auditor shall give:*

(a) *Modified Opinion*

(b) *Qualified Opinion*

(c) *Disclaimer of Opinion*

(d) *Unmodified Opinion*

Answers to Questions involving case study

1.	**(b)**	2.	**(c)**	3.	**(c)**	4.	**(b)**	5.	**(d)**

SUMMARY

- Management is responsible for the preparation of the financial statements. The purpose of an audit is to enhance the degree of confidence of intended users of the financial statements. The aforesaid purpose is achieved by the expression of an independent reporting by the auditor.
- The objectives of the auditor as per SA 700 (Revised), "Forming An Opinion And Reporting On Financial Statements" are to form an opinion on the financial statements based on an evaluation of the conclusions drawn from the audit evidence obtained; and to express clearly that opinion through a written report.

- The auditor shall modify the opinion in the auditor's report when the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or the auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.
- There are three types of modified opinions, namely-a qualified opinion, an adverse opinion, and a disclaimer of opinion.
- As per SA 706 (Revised) on "Emphasis of Matter Paragraphs and Other Matter Paragraphs In The Independent Auditor's Report", the objective of the auditor is to draw users' attention by way of clear additional communication in the auditor's report, to a matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to users' understanding of the financial statements; or as appropriate, any other matter that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.
- As per SA 701, "Communicating Key Audit Matters in The Independent Auditor's Report", the objectives of the auditor are to determine key audit matters and, having formed an opinion on the financial statements, communicate those matters by describing them in the auditor's report.
- As per SA 710, there are two different broad approaches to the auditor's reporting responsibilities in respect of comparative information: corresponding figures and comparative financial statements. The approach to be adopted is often specified by law or regulation but may also be specified in the terms of engagement.
- As per SA 600, when the principal auditor uses the work of another auditor, the principal auditor should determine how the work of the other auditor will affect the audit.
- SA 299 "Joint Audit of Financial Statements" deals with the professional responsibilities which the auditors undertake in accepting appointments as joint auditors.
- CARO 2020, - Every report made by the auditor under section 143 of the Companies Act on the accounts of every company audited by him, to which CARO, 2020 applies, for the financial years commencing on or after the 1st April, 2019, shall in addition, contain the matters specified in paragraphs 3 and 4, as may be applicable.

TEST YOUR KNOWLEDGE

MCQs based Questions

1. *While expressing an unmodified opinion on financial statements, the auditor shall not use which of the following phrases?*

    (a) *present fairly in all material respects*

    (b) *give a true and fair view*

    (c) *with the foregoing explanation*

    (d) *All of the above*

2. *…………………… is a paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to the user's understanding of the financial statements.*

    (a) *Emphasis of Matter Paragraph*

    (b) *Other Matter Paragraph*

    (c) *Key Audit Matter*

    (d) *Management Responsibility Paragraph.*

3. *Statement 1: Communicating key audit matter in the auditor's report constitutes a substitute for disclosure in the financial statements.*

    Statement 2: Instead of modifying an opinion in accordance with SA 705, the statutory auditor can use Key Audit Matter paragraph in the audit report with an unmodified opinion.

    (a) *Only Statement 1 is correct*

    (b) *Only Statement 2 is correct*

    (c) *Both the statements are correct*

    (d) *None of the statement is correct*

4. *Which of the following is not correct?*

    (a) *SA 700 - Forming an Opinion and Reporting on the Financial Statements*

    (b) *SA 701- Key Audit Matters in the Independent Auditor's Report*

(c) *SA 705- Comparative Information- Corresponding figures and Comparative Financial Statements*

(d) *SA 706- Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

5. *Responsibilities of Joint Auditors are governed by:*

(a) *SA 200*

(b) *SA 229*

(c) *SA 299*

(d) *SA 230*

Correct/Incorrect

State with reasons (in short) whether the following statement is correct or incorrect:

(i) *The auditor shall express a qualified opinion when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.*

(ii) *There is no need of addressee in the Auditor's report.*

(iii) *The auditor shall modify the opinion in the auditor's report only when the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement.*

(iv) *The auditor shall express a disclaimer of opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.*

(v) *Communicating key audit matter in the auditor's report constitutes a substitute for disclosure in the financial statements.*

(vi) *When the auditor has to express an adverse opinion, he need not communicate with those charged with governance as this may have an impact on payment of his audit fees.*

(vii) *Instead of modifying an opinion in accordance with SA 705, the statutory auditor can use Key Audit Matter paragraph in the audit report with an unmodified opinion.*

(viii) *The concept of "joint audit" has legal foothold under the Companies Act, 2013.*

Theoretical Questions

1. *"The auditor shall form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework." Explain*

2. *"The auditor shall evaluate whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework. This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgements." Discuss stating clearly qualitative aspects of the entity's accounting practices*

3. *Discuss the factors affecting the decision of the auditor regarding which type of modified opinion is appropriate.*

4. *Discuss the objective of the auditor as per Standard on Auditing (SA) 705 "Modifications to The Opinion in The Independent Auditor's Report".*

5. *In considering the qualitative aspects of the entity's accounting practices, the auditor may become aware of possible bias in management's judgements. The auditor may conclude that lack of neutrality together with uncorrected misstatements causes the financial statements to be materially misstated. Explain and analyse the indicators of lack of neutrality with examples, wherever required.*

6. *The first section of the auditor's report shall include the auditor's opinion, and shall have the heading "Opinion." The Opinion section of the auditor's report shall also identify the entity whose financial statements have been audited. Apart from the above, explain the other relevant points to be included in opinion section.*

7. *Define Emphasis of Matter Paragraph and how it should be disclosed in the Independent Auditor's Report?*

8 *"An auditor is required to make specific evaluations while forming an opinion in an audit report." State those evaluations.*

9. *The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements." SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Explain*

10. *Communicating Key Audit Matter is not a substitute for disclosure in the Financial Statements rather Communicating key audit matters in the auditor's report is in the context of the Auditor having formed an opinion on the financial statements as a whole. Analyse.*

11. *The auditor's report shall include a section, directly following the Opinion section, with the heading "Basis for Opinion". Explain what is included in this "Basis for Opinion" section.*

12. *Distinguish between an adverse opinion and a qualified opinion. Also draft an opinion paragraph for both types of opinion.*

13. *ABC Ltd is a company incorporated in India. It has branches within and outside India. Explain who can be appointed as an auditor of these branches within and outside India. Also explain to whom branch auditor is required to report.*

14. *Before the commencement of the audit, the joint auditors should discuss and develop a joint audit plan. In developing the joint audit plan, the joint auditors should identify division of audit areas and common audit areas. Explain stating the other relevant considerations in this regard.*

15. *The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Explain stating the advantages of the joint audit.*

16. *Discuss the reporting requirements under CARO 2020, with respect to the moneys raised by the company by way of initial public offer or further public offer and where the company has made any preferential allotment or private placement of shares.*

17. *Discuss which class of companies are specifically exempt from the applicability of CARO 2020?*

ANSWERS/SOLUTIONS

Answers to the MCQs based Questions

1.	**(c)**	2.	**(a)**	3.	**(d)**	4.	**(c)**	5.	**(c)**

Answers to Correct/Incorrect

(i) **Incorrect:** The auditor shall express an unmodified opinion when the auditor concludes that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

(ii) **Incorrect:** The auditor's report shall be addressed, as appropriate, based on the circumstances of the engagement. Law, regulation or the terms of the engagement may specify to whom the auditor's report is to be addressed. The auditor's report is normally addressed to those for whom the report is prepared, often either to the shareholders or to those charged with governance of the entity whose financial statements are being audited.

(iii) **Incorrect:** The auditor shall modify the opinion in the auditor's report when:

(a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or

(b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

(iv) **Incorrect:** The auditor shall express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

(v) **Incorrect:** Communicating key audit matters in the auditor's report is in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor's report is not a substitute for disclosures in the financial statements that the applicable financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation.

(vi) Incorrect: When the auditor expects to modify the opinion in the auditor's report, the auditor shall communicate with those charged with governance the circumstances that led to the expected modification and the wording of the modification.

(vii) Incorrect: Communicating key audit matters in the auditor's report is not a substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised).

(viii) Correct: Under provisions of section 139(3), the members of a company may resolve to provide that audit shall be conducted by more than one auditor. Hence, the concept of "joint audit" has legal foothold also under Companies Act, 2013.

Answers to Theoretical Questions

1. Refer Para 1.2
2. Refer Para 1.3.
3. Refer Para 5.4
4. Refer Para 5.2
5. In considering the qualitative aspects of the entity's accounting practices, the auditor may become aware of possible bias in management's judgements. The auditor may conclude that lack of neutrality together with uncorrected misstatements causes the financial statements to be materially misstated. Indicators of a lack of neutrality include the following:

   (i) The selective correction of misstatements brought to management's attention during the audit.

   Example

   - Correcting misstatements with the effect of increasing reported earnings, but not correcting misstatements that have the effect of decreasing reported earnings.
   - The combination of several deficiencies affecting the same significant account or disclosure (or the same internal control component) could amount to a significant deficiency (or material

weakness if required to be communicated in the jurisdiction). This evaluation requires judgement and involvement of audit executives.

(ii) Possible management bias in the making of accounting estimates.

6. The first section of the auditor's report shall include the auditor's opinion, and shall have the heading "Opinion."

The Opinion section of the auditor's report shall also:

(a) Identify the entity whose financial statements have been audited;

(b) State that the financial statements have been audited;

(c) Identify the title of each statement comprising the financial statements;

(d) Refer to the notes, including the summary of significant accounting policies; and

(e) Specify the date of, or period covered by, each financial statement comprising the financial statements.

7. **Emphasis of Matter paragraph:** A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial statements.

When the auditor includes an Emphasis of Matter paragraph in the auditor's report, the auditor shall:

(i) Include the paragraph within a separate section of the auditor's report with an appropriate heading that includes the term "Emphasis of Matter";

(ii) Include in the paragraph a clear reference to the matter being emphasized and to where relevant disclosures that fully describe the matter can be found in the financial statements. The paragraph shall refer only to information presented or disclosed in the financial statements; and

(iii) Indicate that the auditor's opinion is not modified in respect of the matter emphasized.

8. **Specific Evaluations by the auditor:** In particular, the auditor shall evaluate whether :

   (i) The financial statements adequately disclose the significant accounting policies selected and applied;

   (ii) The accounting policies selected and applied are consistent with the applicable financial reporting framework and are appropriate;

   (iii) The accounting estimates made by management are reasonable;

   (iv) The information presented in the financial statements is relevant, reliable, comparable, and understandable;

   (v) The financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements; and

   (vi) The terminology used in the financial statements, including the title of each financial statement, is appropriate.

9. **Responsibilities for the Financial Statements:** The auditor's report shall include a section with a heading "Responsibilities of Management for the Financial Statements."

   SA 200 explains the premise, relating to the responsibilities of management and, where appropriate, those charged with governance, on which an audit in accordance with SAs is conducted. Management and, where appropriate, those charged with governance accept responsibility for the preparation of the financial statements. Management also accepts responsibility for such internal control as it determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The description of management's responsibilities in the auditor's report includes reference to both responsibilities as it helps to explain to users the premise on which an audit is conducted.

   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;[because of the possible effects of fraud on other aspects of the audit, materiality does not apply to management's acknowledgement regarding its responsibility for the design, implementation, and maintenance of internal control (or for establishing and maintaining effective internal control over financial reporting) to prevent and detect fraud.] 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.

10. **Communicating key audit matters in the auditor's report is not:**

(i) A substitute for disclosures in the financial statements that the applicable

Financial reporting framework requires management to make, or that are otherwise necessary to achieve fair presentation;

(ii) A substitute for the auditor expressing a modified opinion when required by the circumstances of a specific audit engagement in accordance with SA 705 (Revised);

(iii) A substitute for reporting in accordance with SA 570 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; or

(iv) A separate opinion on individual matters

11. **Basis for Opinion:** 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 Standards on Auditing;

(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.

(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.

12. An auditor shall express an adverse opinion, when the auditor having obtained sufficient and appropriate audit evidence, concludes that misstatements, individually or in aggregate are both material and pervasive.

Whereas, when the auditor, having obtained sufficient and appropriate audit evidence, concludes that misstatements are material but not pervasive, shall express a qualified opinion.

SA705 – "Modifications To The Opinion In The Independent Auditor's Report" deals with the form and content of both types of report. The following are the draft of the opinion paragraphs of the reports.

(a) Adverse Opinion

We have audited the accompanying consolidated financial statements of ABC Company Limited (hereinafter referred to as the "Holding Company") and its subsidiaries (the Holding Company and its subsidiaries together referred to as "the Group"), its associates and jointly controlled entities, which comprise the consolidated balance sheet as at March 31, 2021, the consolidated statement of profit and Loss, (consolidated statement of changes in equity) and the consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies (hereinafter referred to as the "consolidated financial statements"). In our opinion and to the best of our information and according to the explanations given to us, because of the significance of the matter discussed in the Basis for Adverse Opinion section of our report, the accompanying consolidated financial statements do not give a true and fair view in conformity with the accounting principles generally accepted in India, of their consolidated state of affairs of the Group, its associates and jointly controlled entities, as at March 31, 2021, of its consolidated profit/loss, (consolidated position of changes in equity) and the consolidated cash flows for the year then ended.

(b) Qualified Opinion

We have audited the standalone financial statements of ABC Company Limited ("the Company"), which comprise the balance sheet as at March 31, 2021, and the statement of Profit and Loss, (statement of changes in equity) and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information (in which are included the Returns for the year ended on that date audited by the branch auditors of the Company's branches located at (location of branches)) . In our opinion and to the best of our information and according to the explanations given to us, except for the effects of the matter described in the Basis for Qualified Opinion section of our report, the aforesaid financial statements give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as at March 31st, 2021 and profit/loss, (changes in equity) and its cash flows for the year ended on that date.

13. Sub-section (8) of section 143 of the Companies Act, 2013, prescribes the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor. Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company (herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section 139, or where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country and the duties and powers of the company' s auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as may be prescribed:

It may be noted that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

Further as per rule 12 of the Companies (Audit and Auditors) Rules, 2014, the branch auditor shall submit his report to the company's auditor and reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.

14. **Before the commencement of the audit, the joint auditors should discuss and develop a joint audit plan.** In developing the joint audit plan, the joint auditors should:

    (a) identify division of audit areas and common audit areas;

    (b) ascertain the reporting objectives of the engagement;

    (c) consider and communicate among all joint auditors the factors that are significant in directing the engagement team's efforts;

    (d) consider the results of preliminary engagement activities, or similar engagements performed earlier.

    (e) ascertain the nature, timing and extent of resources necessary to accomplish the engagement.

15. **Joint Audit:** The practice of appointing Chartered Accountants as joint auditors is quite widespread in big companies and corporations. Joint audit basically implies pooling together the resources and expertise of more than one firm of auditors to render an expert job in a given time period which may be difficult to accomplish acting individually. It essentially involves sharing of the total work. This is by itself a great advantage.

    In specific terms the **advantages** that flow may be the following:

    (i) Sharing of expertise.

    (ii) Advantage of mutual consultation.

    (iii) Lower workload.

    (iv) Better quality of performance.

    (v) Improved service to the client.

(vi) In respect of multi-national companies, the work can be spread using the expertise of the local firms which are in a better position to deal with detailed work and the local laws and regulations.

(vii) Lower staff development costs.

(viii) Lower costs to carry out the work.

(ix) A sense of healthy competition towards a better performance

16. The following are the disclosure requirements as per CARO 2020, with respect to the moneys raised by the company by way of initial public offer or further public offer and where the company has made any preferential allotment or private placement of shares.

(a) whether moneys raised by way of initial public offer or further public offer (including debt instruments) during the year were applied for the purposes for which those are raised, if not, the details together with delays or default and subsequent rectification, if any, as may be applicable, be reported;

(b) whether the company has made any preferential allotment or private placement of shares or convertible debentures (fully, partially or optionally convertible) during the year and if so, whether the requirements of section 42 and section 62 of the Companies Act, 2013 have been complied with and the funds raised have been used for the purposes for which the funds were raised, if not, provide details in respect of amount involved and nature of noncompliance;

17. CARO 2020 shall apply to every company including a foreign company as defined in clause (42) of section 2 of the Companies Act, 2013, except–

(i) a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);

(ii) an insurance company as defined under the Insurance Act,1938 (4 of 1938);

(iii) a company licensed to operate under section 8 of the Companies Act;

(iv) a One Person Company as defined in clause (62) of section 2 of the Companies Act and a small company as defined in clause (85) of section 2 of the Companies Act; and

(v) a private limited company, not being a subsidiary or holding company of a public company, having a paid up capital and reserves and surplus not more than one crore rupees as on the balance sheet date and which does not have total borrowings exceeding one crore rupees from any bank or financial institution at any point of time during the financial year and which does not have a total revenue as disclosed in Scheduled III to the Companies Act (including revenue from discontinuing operations) exceeding ten crore rupees during the financial year as per the financial statements.

Answers to Test your Understanding

1. The 18-digit alpha numeric number noticed by her at end of audit report is Unique Document Identification number (UDIN). It is a system generated unique number. Its basic objective is to curb the malpractices of non-CAs impersonating themselves as CAs. It helps in securing reports and documents issued by practising CAs.

   It is required to be stated in case of audit reports and certificates.

2. "Basis for Opinion" is one of basic elements of an audit report in accordance with SA-700. Even in cases where unmodified opinion is expressed by auditor, "Basis for opinion" has to be provided by auditor. Basis for opinion section provides context about auditor's opinion.

   Therefore, Sana's thinking is not proper.

3. In the given case, auditor has not been able to obtain sufficient appropriate audit evidence relating to inventories, debtors, creditors, revenues and expenses. The matter has brought to knowledge of management but no result has been achieved. Besides, auditor opines that there could be misstatements and their possible effects could be both material and pervasive.

   In such circumstances, he should make disclaimer of opinion in accordance with SA 705.

4. As per SA 600 - "Using the Work of Another Auditor", the principal auditor might discuss with the other auditor the audit procedures applied or review a written summary of the other auditor's procedures and findings which may be in the form of a completed questionnaire or check-list. Such review of audit procedures and findings can be undertaken if principal auditor feels

that it is necessary to apply such procedures to obtain sufficient appropriate audit evidence. It is not an encroachment of another auditor's domain.

5. Clause (ix) (d) of CARO, 2020 whether funds raised on short term basis have been utilised for long term purposes, if yes, the nature and amount to be indicated.

   In the given situation, funds have been raised for meeting working capital requirements for ₹ 4 crores. Cash credit facilities for meeting working capital requirements are, by their very nature, short term borrowings. Out of above, ₹1 crore have been used by the company for investment in effluent treatment plant which is ostensibly for a long-term purpose.

   Hence, the matter needs to be reported in accordance with requirements of Clause (ix) (d) of CARO, 2020.