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(SETUP BY AN ACT OF PARLIAMENT)

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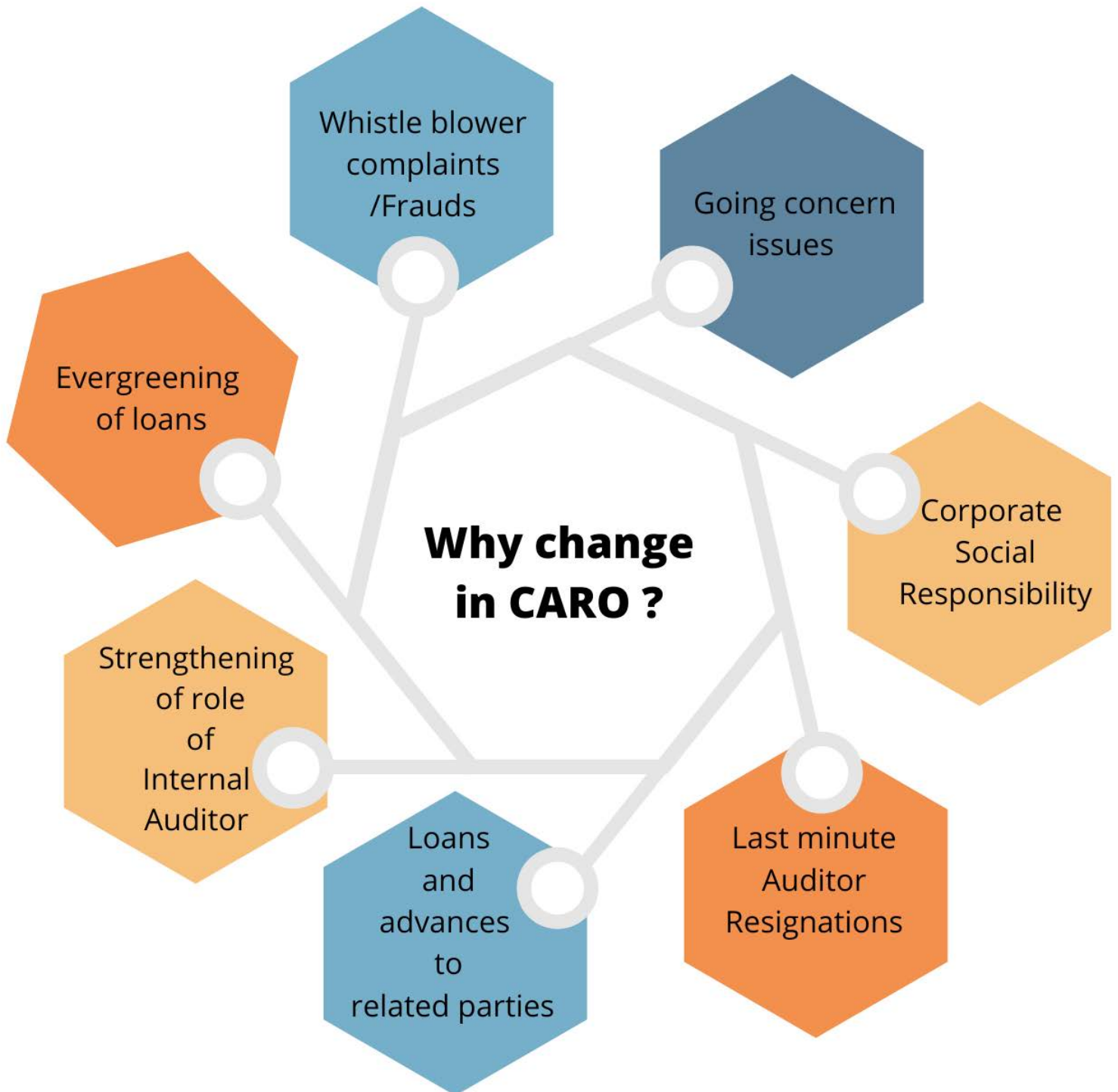
Editor : CA. SANTHOSH PAI G
Sub Editor : CA. SURYA NARAYANAN

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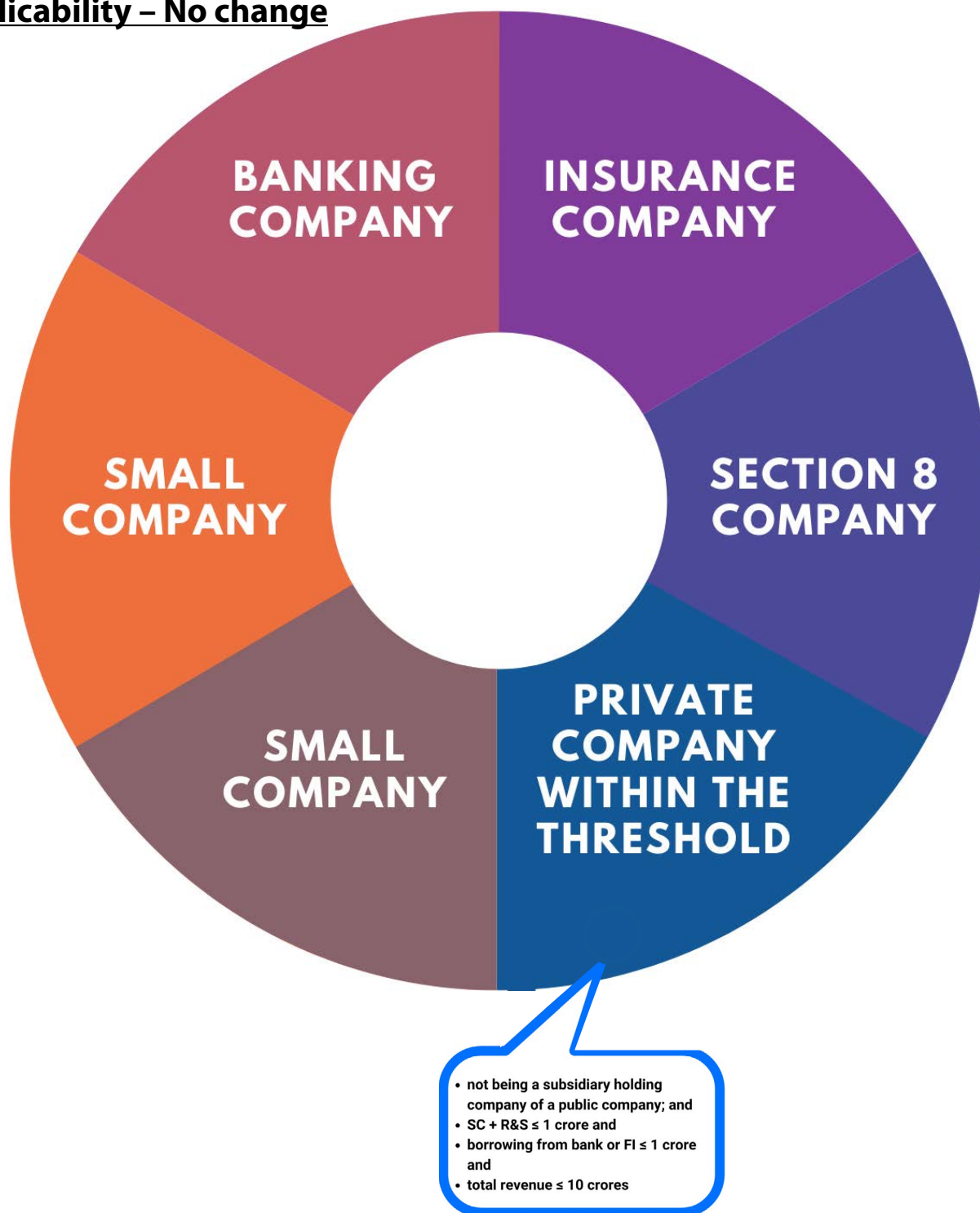
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CARO 2020 AND CHANGES IN MAIN AUDIT REPORT (CONTINUED)

- HEMAL SHAH



I. Applicability – No change



- Order not applicable to Investment Trusts and Real Estate Investment Trusts governed by SEBI Infrastructure Investment Trust Regulations
- CARO 2020 shall not apply to the auditor's report on the consolidated financial statements except one specific clause whereby
 - ▶ Qualification/Adverse remarks in CARO in the audit report of components which are consolidated in the CFS will be required to be reported.

The new/revised clauses (including sub-clauses) have been bifurcated into the following :-

Particulars	Count
New reporting requirements under CARO 2020	28
Reporting requirements modified	16
Reporting requirements carried forward with no modifications	7
Reporting requirement of CARO 2016 deleted	(1)
Total	50

II. Maintenance of Fixed Asset Register, Revaluation of PPE and Intangibles

• Maintenance of Fixed Asset Register:

- ▶ Fixed asset register to also cover investment property, ROU assets and intangible assets including intangible assets generated on business combination

• Title Deeds:

- ▶ Title deeds – all the immovable property are covered for reporting except assets taken on lease and lease agreements are duly executed
- ▶ Properties considered as stock in trade eg in real estate industry, then reporting is not triggered
- ▶ Reporting is triggered for assets taken on lease if lease agreements are not duly executed
- ▶ What about companies not following Ind AS and hence not implemented Ind AS 116?
- ▶ Additional disclosures (e.g.: name of the title owner, relationship, period, reasons) whose title deeds are not in the name of the Company

• Revaluation:

- ▶ Verify that disclosure is made for companies following revaluation model – since under cost model revaluation is not permitted
- ▶ Reporting on whether the company has revaluated its PPE or intangible assets and whether revaluation has been carried out by a Registered valuer
- ▶ Additional reporting of change $\geq 10\%$ in aggregate in the net carrying value of each class of PP&E or intangibles assets; Change can be up/downward
- ▶ Whether ROU measurements due to lease modification or fair valuation of PPE for first time adoption of Ind AS covered for reporting ?

• Additional reporting on disclosure of new/pending proceedings in respect of benami properties in financial statements.

III. Proceedings initiated/pending against company for holding Benami Property



Benami Property reporting Requirement

New reporting in CARO on any proceedings that have been initiated or pending against the company for holding any Benami property as defined under the "Benami Transactions (Prohibitions) Act, 1988 and Rules thereunder (Act).

Appropriate disclosure

Management should make appropriate disclosure in relation to any proceedings which have been initiated or pending against the company for holding any benami property.

Benami Transactions (Prohibition) Act, 1988 defines a 'benami' transaction as any transaction in which property is transferred to one person for consideration paid by another person. A "benami property" means a property which is the subject matter of a benami transaction and also includes the proceeds from such property.

Punishment for contravention in the Act

Where a company contravenes, then the Company itself AND every Person (including Director, manager, secretary, CEO etc.) who was responsible for such Transaction shall be deemed to be guilty of the contravention; and shall be liable to be proceeded against and punished accordingly. But if such person proves that such transaction was made without his/her knowledge then such a person would not be considered as guilty



IV. Physical verification of inventories

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;

Key considerations

- Additional reporting on coverage and procedure followed. Management to conduct physical verification of inventories. Auditor expected to examine methods, procedures and the coverage:
 - ▶ Periodicity of verification depends upon the nature of inventories, location and the feasibility of conducting a verification
 - ▶ Coverage and procedure will normally not be appropriate if it is not reasonable and adequate in relation to the size of the company and nature of its business
- Only in cases where discrepancy of 10% or more arises in value, for any class of inventory, the auditor has to report the fact and also report whether they have been properly dealt with in the books of account. For the purpose of reporting under this clause, materiality threshold as may be applicable for the auditee is not relevant
- Whether auditor is required to report following for a class of inventory:
 - ▶ Scenario 1: Discrepancies more than 10% in value but less than 10% in quantity – Reporting triggered
 - ▶ Scenario 2: Discrepancies less than 10% in value but more than 10% in quantity – No reporting triggered

Discrepancy of 10% or more to be assessed for each class of inventory separately

V. Working capital limits

- The auditor is not required to audit such quarterly returns/ statements, but only required to compare the same with the books of account and report disagreement, if any..
- Auditor not required to audit the books of the account on the basis of which such statements/ quarterly returns have been prepared and submitted to the banks/ FIs. However, while opining



on this clause, the auditor should consider:

- ▶ The impact of modifications, if any, to the audit opinion e.g. audit opinion is modified as proper records were not maintained
 - ▶ Appropriateness of underlying internal controls established for generating reliable information including impact of continuing Internal control weaknesses
- Auditors to ensure managements process for the disclosure is thorough and compare Returns/ statements with books of account
 - Auditor to assess that disclosure is provided considering the sanctioned borrowings even if the same is unutilized during the period/ as at the end of the reporting period

VI. Investments, guarantees, loans and advances

- Sub - clause (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) 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;
 - a) 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)

Key Consideration

- Reporting loans/advances in the nature of loans granted, guarantee or security provided to all parties (as against those parties covered under Section 189 of the Act in the erstwhile clause)
- Sub-clause (a) & (e) not applicable to companies who are in the principal business of giving loans (e.g. FIs, NBFCs)
- Requires determination of gross amounts (i.e. without considering subsequent settlements) of all loans, advances in the nature of loans, guarantees, security provided during the year to sub-



sidiaries, joint ventures, associates and to any other parties

- Loans given in cash or in kind – reporting required; loans squared up during the year to be reported
 - Guarantees to cover financial guarantees only and not performance guarantees
 - Auditor to ensure compliance with sections 179, 180, 185, 186, 187 of the Companies Act, 2013
- Whether supplier advances are covered within the ambit of this clause?
- It is clarified that the auditor's comments on all the six clauses are to be made with reference to all the loans/advances in nature of loans granted, guarantee or security provided to companies, firms, limited liability partnerships or any other parties.
 - Whether an advance is in the nature of a loan would depend upon the circumstances of each case
 - The clause includes loans/ advances in nature of loans but do not cover advances unless such advances are in the nature of loans. Key principles for identifying advances in the nature of loans are:
 - ▶ Amount/ period of advance - whether far in excess of the value of an order/ far in excess of the period as per normal trade practice
 - ▶ Another way to consider is the operating cycle i.e. the time between the purchase of the raw material and the delivery of the finished product by the supplier. An advance which exceeds this period would normally be an advance in nature of loan
 - ▶ A stipulation regarding interest may normally be an indication that the advance is in the nature of loan

VII. Investments, guarantees, loans and advances – whether prejudicial

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)
- 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;



Key considerations

- Applicable to all companies including companies like NBFCs whose principal business is to grant loan
- For loans/advances in nature of loans, the “terms and conditions” would primarily include rate of interest, security, terms and period of repayment and restrictive covenants, nature of entity
- For investments made, the auditor would have to give due consideration to the factors connected with such an investment, including company’s ability to make such investment, financial standing of the investee company, sources of fund, valuation of the proposed investment, covenant’s attached, etc
- Whether the clause covers reporting of loans/ advances in nature of loans, investments, guarantees and security which were given in previous years and existing on the date of applicability of CARO 2020?
 - ▶ Clause 3 refers to “Whether during the year the company.....” and hence reporting obligation applies prospectively
 - ▶ Reference should be made to reporting u/s 143(1)(a) under Companies Act, 2013 which requires auditor to report 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 member

VII. Evergreening of loans and advances

- 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];

Key considerations

- Covers instances of ‘evergreening’ of loans/ advances in nature of loans
- Auditor to consider loans falling due as on the balance sheet date and which were renewed/ extended/settled post balance sheet date and before the date of audit report
- Consider amendment in the Companies (Audit and Auditors) Amendment Rules, 2021



- In case of complex group structures, it would be difficult to establish a clear audit trail for the transactions and thus making it difficult to identify any such transaction
- Determining the Total Loans and Advances in the nature of loans could pose challenges
- The term 'evergreening' is not defined in the Act. However, in general parlance it implies an attempt to mask loan default by giving new loans to help delinquent borrowers to repay/adjust principal or pay interest on old loans.
- Intent seems to mask loan default. Conversion of interest into loan is an attempt to provide extended time period to the borrower

January 2021

- Loan obtained Rs 100
- Repayable on September 2021
- Interest rate 10% pa



September 2021

- Total amount due Rs. 105
- Interest is converted in to loan
- Rs 105 provided as fresh loan

IX. Loans and advances

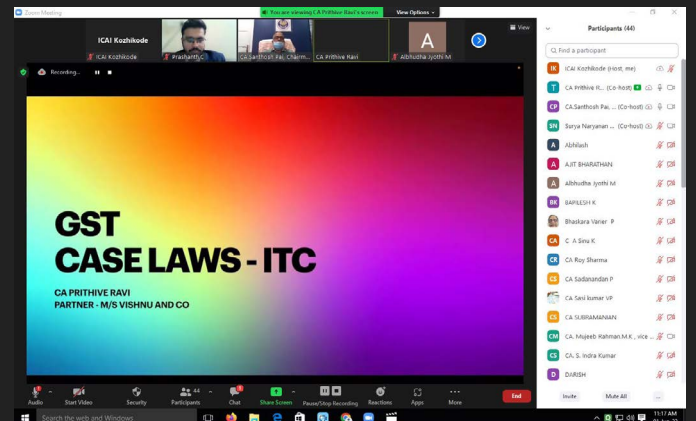
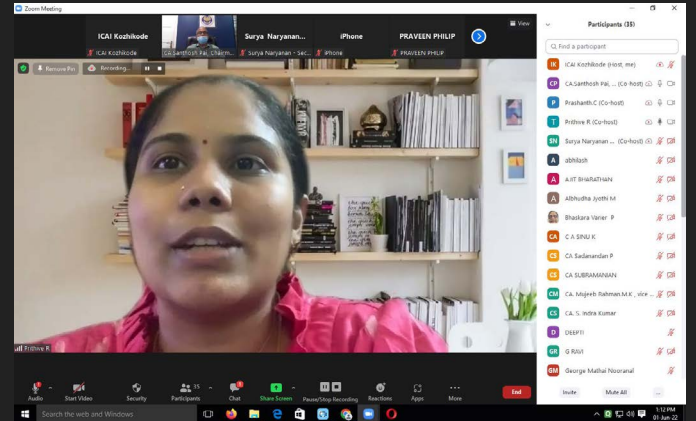
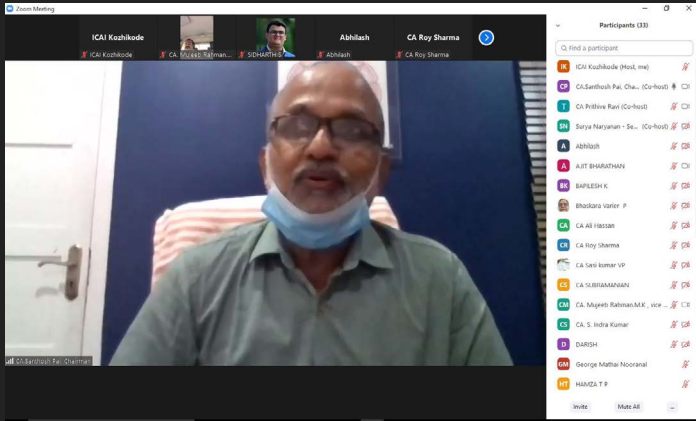
● Other clauses for loans and advances

- Clause (iii) (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;
- Clause (iii) (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;
- The above two clauses are also applicable to companies whose principal business is to give loans
- This may put significant challenges for NBFCs

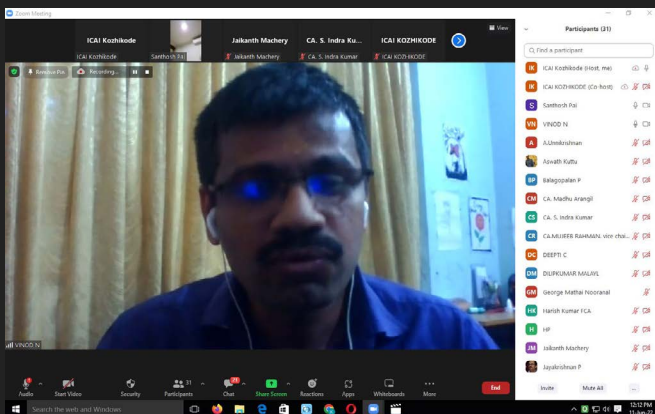
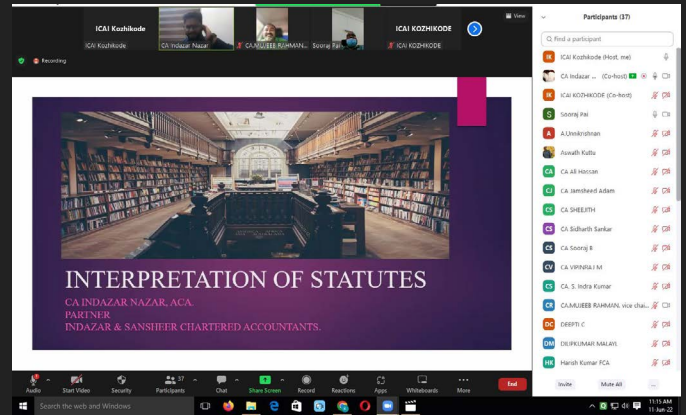
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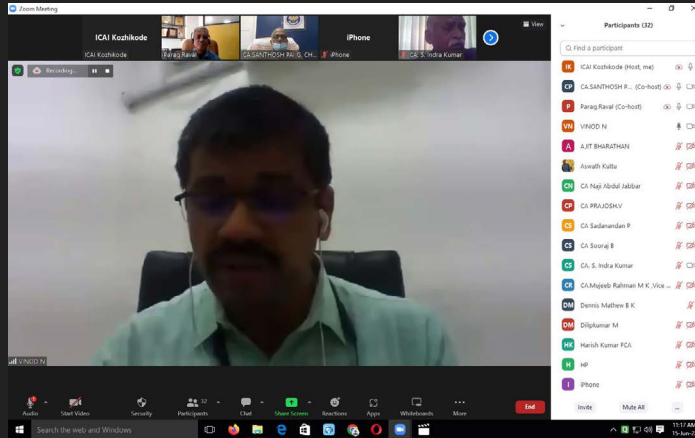
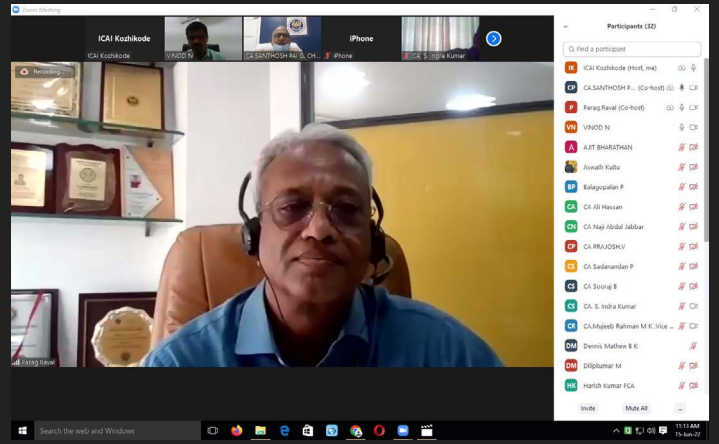
ACTIVITIES - JUNE, 2022



Virtual CPE Meeting on "Important Case Laws relating to ITC in GST"
Speakers - CA. Prithive R., Chennai and - CA. Prashanth C., Chennai. - 01.06.2022



Virtual CPE Meeting on "Interpretation of Statutes"
Speaker - CA. Indazar Nazar, Calicut. - 11.06.2022



Virtual CPE Meeting on "Ethical Behaviour and Professional Enhancement"
Speaker - CA. Parag Raval, Ahmedabad. - 15.06.2022



Virtual CPE Seminar on "Startups & Fund Raising"
Speaker - CA. Abhijith Preman. - 18.06.2022



Kozhikode Branch of SIRC celebrated its 40th Branch formation day, CA. Jose Pottokaran, Past Chairman, SIRC of ICAI was honoured at the function. CA. Satheesan P. Chairman, SICASA, SIRC attended the function. Students secured highest marks in CA Intermediate and Final examinations under Kozhikode Branch were given CA T.K. Menon Memorial Award and CA Subbarama Iyar Memorial award respectively at the function. Virtual CPE Seminar on "Small and Medium Practitioners" Speaker - CA Satheesan P. - 26.06.2022



Kozhikode Branch of ICAI and SICASA organized blood donation camp in association with Blood bank, Govt. hospital for Women and Children, Calicut. - 28.06.2022

UPCOMING PROGRAMMES - JULY, 2022

JULY

1

74th CA Day celebrations
at Hotel Woodies, Kallai Road, Kozhikode.
Chief Guest - Dr. Beena Philip, Mayor, Kozhikode Corporation

2

Certification course on Forensic Accounting and Fraud Detection.

14

Seminar
Topic - Indian Capital Market - Trends, Strategies and Wayforward
Speaker - CA. Lalit Kumar, Chennai.

Contributions to e-newsletter

Contributions in the form of articles, poems, jokes, travelogues etc. are invited from members for consideration in the monthly e-Newsletter. Interested members may email their contribution to icaikoznewsletter@gmail.com along with name, membership number and mobile number.

