



# THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

(SETUP BY AN ACT OF PARLIAMENT)

## KOZHIKODE BRANCH OF SIRC E-NEWSLETTER

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# CARO 2020 AND CHANGES IN MAIN AUDIT REPORT (CONTINUED)

- HEMAL SHAH

## ► Material uncertainty in repayment of liabilities when they fall due

### ● Disclosures required under Schedule III

- 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;

### ● Key considerations

- Emphasis is on the company's ability to meet its liabilities – different from assessment of going concern
- Test of existence of material uncertainty is to be as on the date of audit report for the position of liabilities existing at the date of BS
- One-to-one relationship between the unpaid liabilities and the realisable financial assets not required - Evaluation to be done on an overall basis
- Whether a paragraph relating to material uncertainty on going concern would also have reporting implications under this clause?
- The emphasis in this clause, is on the company's ability to meet its liabilities. If the main audit report contains a paragraph on "material uncertainty related to going concern", it should be duly considered while making comment under this clause.
- There can be a situation wherein going concern assumption may be appropriate due to support letters provided by the holding company, but the company may not be able to meet its liabilities falling due within a period of one year from the balance sheet date
- Going concern is an assumption that the entity will continue for the foreseeable future. Reporting under this clause and going concern are related but separate assessments. Outcome of these assessments can be different - Company can be capable of meeting its liabilities when due but may have going concern challenges



- Auditor of Company A concluded that a material uncertainty related to going concern exist

### Going concern triggers:

- Net-worth eroded to the extent of 60%
- Expected to continue to incur losses in next 2 years
- Loss of a major customer (20% of revenue) during the year
- No default in payment of liabilities
- Credit downgrade due to negative business environment

### Mitigating factors

- Unused financing facilities
- New financing facilities can be obtained by pledging unencumbered assets
- Cost reduction measures implemented
- Process of identifying new investors

### ● Points for consideration

- Auditor concluded that the holding company has the ability to discharge the financial liabilities of the company as and when they fall due
- Auditor to state this fact in CARO while also state the facts on the financial position of the company

- Auditor of Company A concluded that a material uncertainty related to going concern **DONOT** exist

### Going concern triggers:

- Reduction in gross margin
- Liquidity position stretched – financing facilities exhausted:
  - Delay in payment of certain liabilities
  - Doubt that liabilities due within 1 year would be settled within due date

### Mitigating factors

- Unconditional Support letter from Parent (parent has strong financial position)
- New products with high margin introduced after YE
- In-principal approval (not binding) from lenders for new financing facilities
- Close monitoring of recovery of trade receivables

### ● Points for consideration

- Auditor concluded that the holding company has the ability to discharge the financial liabilities of the company as and when they fall due
- Auditor to state this fact in CARO while also state the facts on the financial position of the company



## ● Other issues

- Consider subsequent period transactions between the date of balance sheet and the date of audit report; refer SA 560 - Subsequent Events
- Liabilities to be examined for payment should exist at the date of balance sheet which falls due within a period of one year from the balance sheet date
- “Liabilities falling due within one year” and “current liabilities” are different as
  - classification of current/non-current is based on operating cycle which could be shorter/longer than 1 year
  - Current liability as per Schedule III is where the company does not have unconditional right to defer the obligation
- Classification of liabilities into current and non-current in the financial statements as per the requirements of Schedule III of the Act
- Financial assets and financial liabilities may be identified as per Ind AS 32
- Final comment of the auditor is “.....the company is capable of meeting its liabilities” and hence it includes non current and non financial liabilities also which are falling due in next 12 months

## **XVII. Clause (XVII) : Cash Losses**

### ● Reporting on cash losses

- CARO 2003 contained reporting for the amount of cash losses incurred by the Company in the current year and in the immediately preceding year.
- No such provision was there in CARO 2016. The same has been reintroduced.
- Term “cash loss” is not defined.
- Following non-cash items to be adjusted for arriving at cash losses. The starting point would be profit/loss as per P&L (without OCI)
  - Depreciation, Amortization
  - Impairment losses/ reversals
  - fair value changes
  - Revaluations
  - Unrealised exchange fluctuation
  - deferred tax



- Cash profit/loss realised and recognised in OCI should be considered. Subsequent reclassification to P&L should not be considered
- In case of restatement, net profit/loss after such restatement should be considered
- In case of any qualifications, figures of cash losses for current year and previous year should also be adjusted for impact of qualification to the extent these are quantified

#### ▶ Auditors resignation

- 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

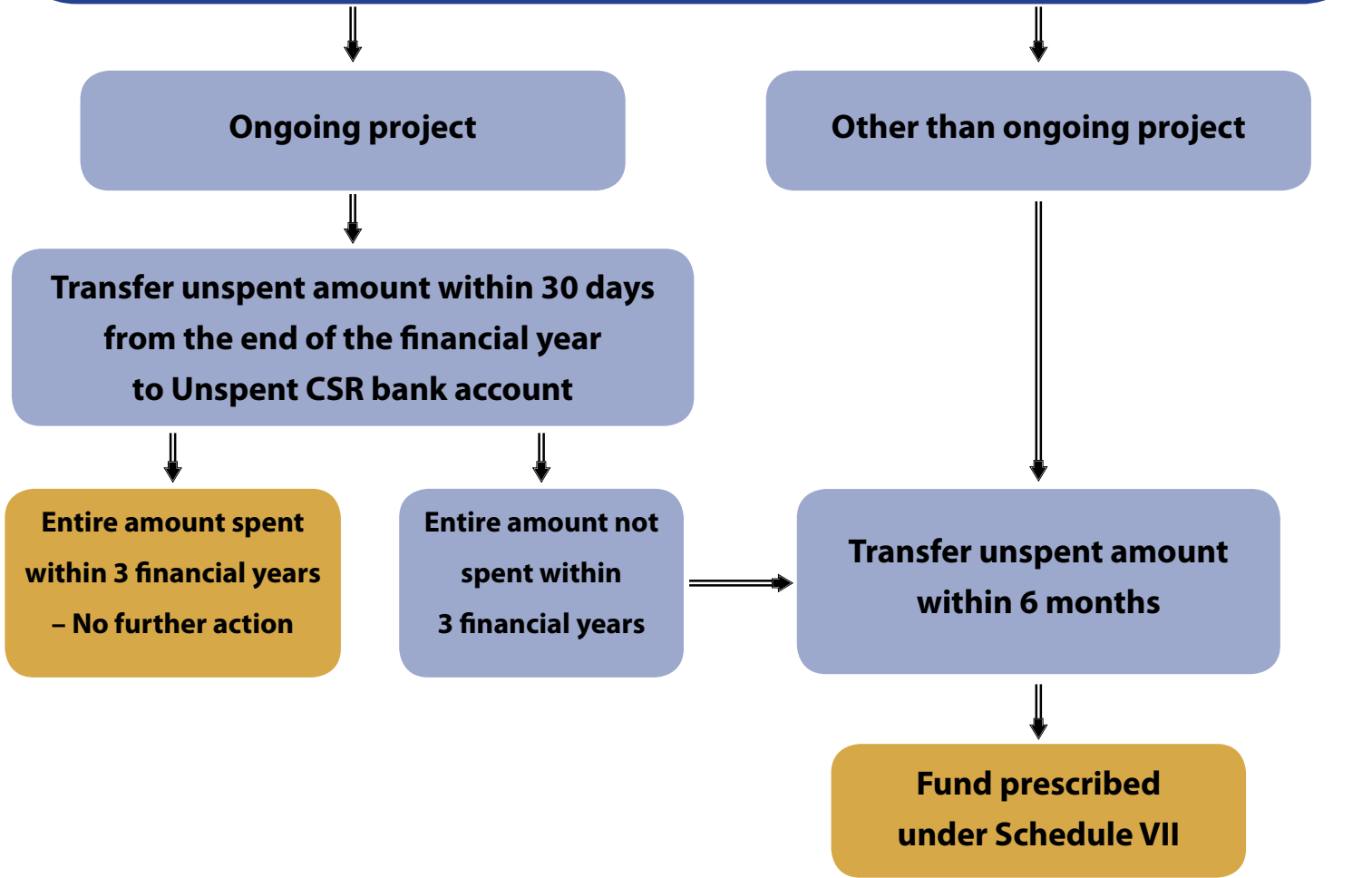
#### ● Key considerations

- Applicable where incoming auditor is appointed during the year to fill a casual vacancy caused by resignation of the auditor created in the office of the previous auditor under section 140(2) of the 2013 Act
- Incoming auditor (prior to accepting the position as auditor) to communicate with the previous auditor to know the reasons for the change in order to be able to safeguard his own interest, the legitimate interest of the public and the independence of the existing accountant (as required by ICAI Code of Ethics)
- Incoming auditor to obtain copy of letter of resignation (as submitted to management) and copy of Form ADT 3 (as submitted to ROC)
- Incoming auditor to consider the reasons for resignation and also refer to last audit/ review report of the outgoing auditor to understand the modifications to audit/review opinion
  - As part of obtaining 'no objection' from outgoing auditor, the incoming auditor should enquire in respect of modifications/ adverse comments of the outgoing auditor in the last issued audit/review report, since CARO casts an obligation on the incoming auditor
- Compliance to be ensured with ICAI pronouncements including:
  - Listed entities: SEBI Circular - Resignation of statutory auditors from listed entities and their material subsidiaries
  - Others: ICAI Implementation Guide on Resignation/ Withdrawal from an Engagement to Perform Audit of Financial Statements



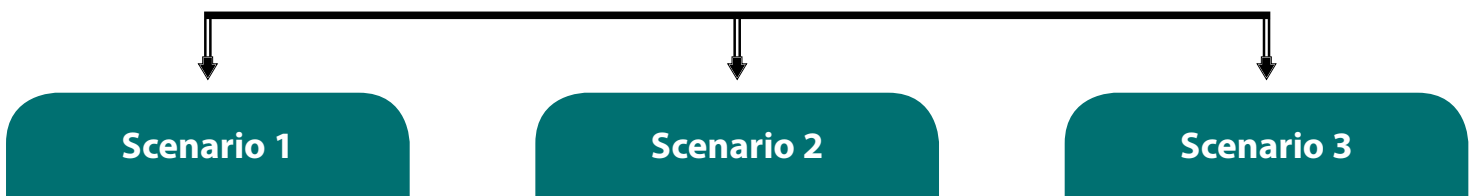
**XVIII. Clause (XX) : Corporate Social Responsibility**

**Auditor’s Report shall include a statement on whether the Company has transferred any unspent amount to an Unspent Fund/Unspent CSR account, as the case may be**



**CSR routed through trust/society/Section 8 company – the auditor still needs to satisfy the above rules are complied with**

**► Reporting on consolidated financial statements**







### Scenario 1

▶ **Statutory audit reports AVAILABLE for all components**

- ❑ Basis the statutory audit report of the component, principal auditor to identify clauses having qualification/ adverse remarks
- ❑ Cross reference to be made to the Other Matters paragraph which state the fact of reliance placed on audit report of the component auditor

### Scenario 2

▶ **Statutory audit reports NOT AVAILABLE for any component**

▶ **Component auditor would PROVIDE INFORMATION on CARO in its audit report on group pack prepared for consolidation purpose**

- ❑ Basis the audit report on group pack, principal auditor to identify clauses having qualification/ adverse remarks
- ❑ Principal auditor to state the name of such entities and the fact that statutory report of these component has not been issued till the date of principal auditor's report
- ❑ Cross reference to be made to the Other Matters paragraph which state the fact of reliance placed on audit report of the component auditor

### Scenario 3

▶ **Statutory audit reports NOT AVAILABLE for any component**

▶ **Component auditor would PROVIDE INFORMATION on CARO in its audit report on group pack prepared for consolidation purpose**

- ❑ Principal auditor to state the name of such entities and the fact that CARO report of these component has not been issued till the date of principal auditor's report
- ❑ Cross reference to be made to the Other Matters paragraph which state the such components are unaudited.

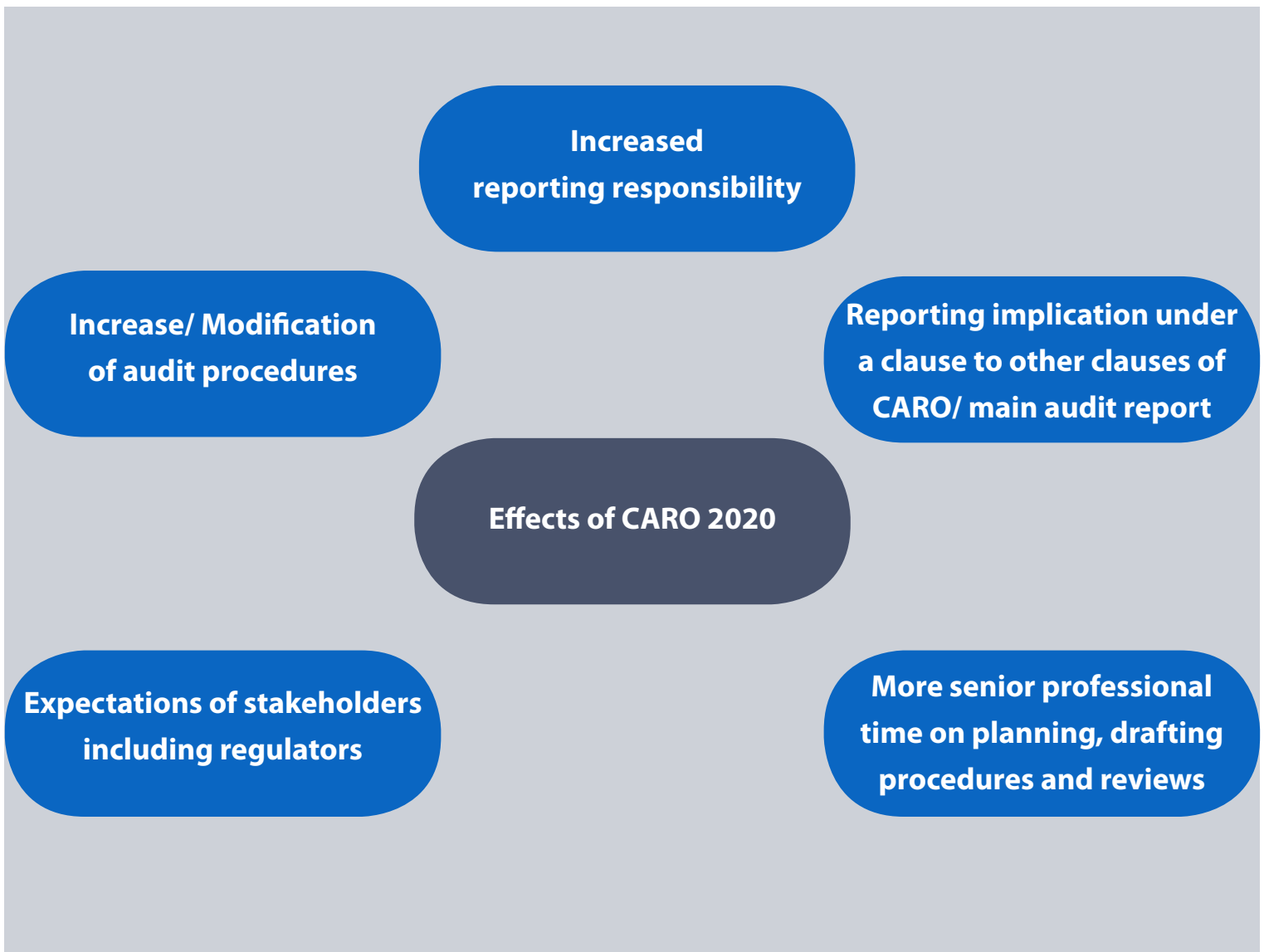
► **Interplay between Schedule III and reporting under CARO 2020**

No	CARO Reporting and Sch III
1.	Title deeds of all the immovable properties are held in the name of the company. If not, provide prescribed details [Clause 3(i)(c)]
2.	For revalued PPE (including Right of Use assets) or IA whether the revaluation is based on the valuation by a Registered Valuer and specify the amount of change, if change is 10% or more in the aggregate of the net carrying value of each class of PPE or / IA [Clause 3(i)(d)]
3.	Proceedings initiated/ pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, and rules
4.	For sanctioned working capital limits in excess of five crore rupees secured by current assets, whether the quarterly returns are in agreement with books of account, if not, give details; [Clause 3(ii)(b)] - <b>Sch III covers all borrowings and no monetary threshold</b>
5.	Whether the company has granted any loans or advances in the nature of loans <b>either repayable on demand or without specifying any terms or period of repayment</b> , if so, specify the aggregate amount, percentage to the total loans granted, aggregate amount of loans granted to Promoters, related parties as defined in section 2 (76) Clause 3(iii)(f)] – <b>Sch III – transactions with promoters, etc to be disclosed</b>
6.	Transactions not recorded in the books have been surrendered or disclosed as income during the year in tax assessments under Income Tax Act, if so, whether the previously unrecorded income has been properly recorded in the books of account during the year [Clause 3(viii)]
7.	Whether the company is a declared wilful defaulter by any bank or financial institution or other lender [Clause 3(ix)(b)]
8.	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 [Clause 3(ix)(c)] – <b>Sch III covers all borrowings and where used</b>
9.	Whether any material uncertainty exists that company is capable of meeting its liabilities within a period of one year from the balance sheet date on the basis of the <b>financial ratios</b> , 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 [Clause 3(xix)] – <b>Sch III – 8 ratios to be disclosed with management comments for changes &gt; 25% from PY</b>





No	CARO Reporting and Sch III
10.	<p>CSR compliance – Whether unspent amount transferred to a specified fund within a period of 6 months of the expiry of the FY. For any ongoing project, unspent amount transferred to special account [Clause 3(xx)]</p> <p><b>Sch III - Details of CSR - amount to be spent, shortfall, total of previous years, reason for shortfall and nature of CSR activities</b></p>



# ACTIVITIES - AUGUST, 2022



**CA Cricket Tournament 2022**

Inter branch cricket tournament for members held at Sports Arena, Karaparamba, Calicut. - 05.08.2022



**Kozhikode Branch of ICAI Donated old books related to CA Course and ₹. 5,000 to Kovoor Library. - 14.08.2022**





**Independence Day 2022 - CA. Santhosh Pai G, Chairman, Kozhikode Branch of ICAI hoisted the flag. - 15.08.2022**



**Seminar on Tax Audit and Standards on Auditing  
Speakers - CA. Mohan R. Lavi & CA. Chinnsamy Ganesan. - 19.08.2022**





**CA Sports Day 2022**  
Held at Cosmopolitan Club, Calicut. Members and their family members participated in various sports events including badminton, Caroms, Chess and Swimming. 20.08.2022



**Seminar on Recent Updates in TDS**  
**Speaker - CA. Radhesh L Bhat. - 27.08.2022**

# Upcoming Programmes September, 2022

**3** Onam Celebration & Seminar on Stress Management  
 Venue - City House hall, Kannur Road, Kozhikode.  
 Speaker - Adv. Dinesh A

## 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](mailto:icaikoznewsletter@gmail.com) along with name, membership number and mobile number.