

BRIEF ANALYSIS ON COMPANIES (AUDITOR'S REPORT) ORDER, 2020

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Abstract

This paper aims to analyse the rationale behind the disclosures mandate brought forth pursuant to Companies (Auditor's Report) Order 2020 (hereinafter referred to as "CARO 2020"). As against the 16 clauses reported by the Statutory Auditors under the earlier Companies (Auditor's Report) Order 2016 (CARO 2016), 21 clauses are now required to be reported under CARO 2020. An attempt is made to conduct a detail and exhaustive Clause-wise analysis in order to reflect the requirement and authenticity of the statutory audit carried out by the statutory auditors with reference to reporting under CARO 2020 clauses.

Key Words: Companies (Auditor's Report) Order 2020, Companies (Auditor's Report) Order 2016, Regulatory Measure, Auditors, Audit

I. INTRODUCTION

Over the past few years, in order to establish transparency within the Corporate ecosystem and in order to avoid repetitions of the cons and scams, the reporting requirement for every corporate is becoming stringent. Every year, the statutory auditors are required to evaluate the financial performance of every corporate and report the same to the shareholders of the Company. The evaluation is briefed and backed-up by auditors' report wherein all the observations and qualifications are summarized and reported for the shareholders to understand the working of the Company and to establish validity in the financial statements. In spite of the efforts undertaken to reduce and eliminate the scams and cons within the Country, the number of scams and cheats is continuously increasing and since the scams and cons take birth within the financials of the Company, the audit and report thereon become one of the most crucial documents for study and scrutiny. Therefore, in order to overcome the lapses in existing reporting standards and establish transparency, the Ministry of Corporate Affairs has issued Companies (Auditor's Report) Order, 2020, after consultation with the National Financial Reporting Authority (NFRA) and by virtue of the powers conferred pursuant to Section 143 of Companies Act, 2013.

The Ministry of Corporate Affairs (MCA) has issued the Companies (Auditor's Report) Order, 2020 (hereinafter referred to as 'CARO 2020'), on 25th February 2020. With the advent of this CARO 2020, the earlier Companies (Auditor's Report) Order, 2016 (hereinafter referred to as 'CARO 2016') is suppressed. This CARO 2020 is brought forth to bring transparency & faith in true spirit in the Financials Statements of Companies. With the arrival of this new CARO, the role of auditors has become more crucial as a reporting authority. Now, the Auditors have to report to the stakeholders of the Companies, all the essentialities with more transparency than before on all the central aspects of any company and its financials are required to be reported. The applicability for the eligible companies commences on or after the 01st April, 2019 (F.Y. 2019-20). The earlier CARO 2016 had 16 matters which the auditors were required to report while carrying out statutory audit of Company, however now the CARO 2020 is notified with 21 matters. These 21 clauses of reporting are a combination of certain new clauses that are added, certain existing that are modified and few are removed altogether.

I.1 Objectives of the Study

The following are the research objectives set for the research study:

1. To review & narrate the applicability of Companies (Auditor's Report) Order, 2020
2. To discuss & analyse the reporting requirement of all 21 clauses of Companies (Auditor's Report) Order 2020

I.2 Scope of the Study

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All the 21 clauses of Companies (Auditor's Report) Order 2020 as required to be disclosed and reported by the Statutory Auditors are analysed.

I.3 Limitations of the Study and Sample Size

Under the earlier CARO 2016, there were 16 clauses required to be reported under CARO 2016, no comparative study is undertaken and only the 21 clauses of CARO, 2020 are discussed and analysed in this study.

I.4 Tools and Techniques

For the purpose of detailed and critical review of all the 21 clauses of CARO, 2020, descriptive analysis is undertaken.

I.5 Significance of the Study

The significance of this research study is narrated as follows:

1. To review and analyse both sides of the coin with reference to CARO, 2020 reporting viz-a-viz: reviewing and assessing the extent to which existing reporting new brought forth standards and practices are matching the current need of the hour as well as attempting to develop and invent new and advanced reporting standards and practices to address the loopholes, if any, in the existing reporting standards in order to keep pace with or adapt with the ever-changing business conditions and the ever growing needs of the future with reference to economic, financial and societal requirements.
2. To improve and provide understanding of all the stakeholders of the Corporates who are actually utilizing this reported information, available in public domain, for making investment and such other financial decisions.
3. Making contribution to academic literature of accountancy related research works by conducting assessment and analysis of all the clauses to understand the meaning and intent behind the advent of such new reporting criteria and provisions. To help the students gain knowledge and understanding on the subject matter along with understanding the need and requirement of critical evaluation in the accountancy disclosures.

II. APPLICABILITY:

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 to the following class of Companies:

1. A banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);
2. An insurance company as defined under the Insurance Act, 1938 (4 of 1938);
3. A company licensed to operate under section 8 of the Companies Act;
4. 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

5. 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.

III. CARO 2020 CLAUSE WISE ANALYSIS

A brief analysis is done for all the CARO, 2020, clauses, with more focus on the fresh / new clauses:

Clause (i) (a) Reporting the maintenance of proper records showing full particulars, including quantitative details and situation of **Property, Plant and Equipment** AND Reporting the maintenance of proper records showing full particulars of **Intangible Assets**.

➤ Analysis:

The earlier CARO 2016 covered only disclosure and details with respect to the fixed assets, whereas in CARO 2020 the scope of the reporting is enhanced and the terminology used is "Property, Plant &

Equipment” and the disclosure in prescribed format with regards to all the quantitative details and situation of all the assets along with the details of ownership is required to be reported. Additionally, the information with reference to maintenance of intangible assets is also required to be reported in CARO 2020.

Clause (i) (b) Reporting on Physical verification of Property, Plant, Equipment and Intangible Assets.

- Analysis:
The earlier CARO 2016 also required the verification to be conducted by the Management at regular intervals and reporting the discrepancies, if any. CARO 2020 requires Property, Plant and Equipment **AND** Intangible Assets verified by the management at reasonable intervals; and to report any material discrepancies, if any, and to properly deal with such discrepancy in the books of account. This reporting is to discontinue the mere reporting of the verification and discrepancy year after year, the information with respect to measure undertaken to deal with and fix the discrepancies is also to be reported.

Clause (i) (c) Reporting on Title Deeds of all 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, the details are required to be given in tabular format.

- Analysis:
The mandate is to determine the ownership of the assets – tangible or intangible. The reporting will clarify whether the assets are used on rental basis or owned by Management. This reporting will primarily be beneficial to the lending institutions to understand the rationale and risk of the financial exposure they provide built upon the ratio analysis carried out from the fixed assets displayed in the Financial Statements. At many events, it is witnessed the lending institutions provide the lending with clear ownership clarity towards the assets given as collateral. This reporting will also clarify whether the assets purchased is utilized for primary commercial activities or given on rent for earning rental income as investment asset.

Clause (i) (d) Reporting on whether the Revaluation of Property, Plant, Equipment and Intangible Assets is carried out, and to specify the change if more than 10%, if carried out.

- Analysis:
It has been common practice, that Corporate revalue the assets in order to adjust the ratios to make the balance sheet appear favourable for investment and/or to obtain funds from external sources and / or to meet the requisite stipulation. However, such revaluation become the start for the scams and cheats of the future and thus now the revaluation shall be carried out based on the valuation by a Registered Valuer and the auditors are required to report the 10% or more change in the aggregate of the net carrying value of each class of Property, Plant and Equipment or intangible assets, if any. The relevant entries revaluation and profit and loss account entries shall also to be reported in the financial statements disclosing the financial and liquidity position of the Company with maximum transparency.

Clause(i) (e) Reporting on about the Proceedings, if any, initiated or pending for holding any Benami Property under Benami Transactions (Prohibition) Act, 1988, if so, to appropriately disclose the details in its financial statements.

- Analysis:
There were no such previous reporting provisions under any compliance requirement or head. Now with this mandate, all the auditors are required to report whether the Company holds any Benami Property under Benami Transactions (Prohibition) Act, 1988 and to report:
1. Details of any/all proceedings initiated against Company under Benami Transactions (Prohibition) Act and Rules
2. Details of any/all proceedings pending under Benami Transactions (Prohibition) Act and Rules

The transactions initiated or pending with government authorities pursuant to Benami Transactions (Prohibition) Act and Rules will be reported. When such reporting will be made along with the details of the property/ies involved, there will be clarity towards the ownership of the properties listed / disclosed under assets head. A segregated reporting of such properties and transactions will be seen in the financial statements.

Clause(ii)

(a) Reporting 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) Disclosure 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.

➤ Analysis:

This reporting is made more stringent and here now the auditors are required to report the method adopted for physical inventory verification and the intervals of such physical verification by the management. Also, if there are any discrepancies noticed of 10% or more in the aggregate for each class of inventory noticed are also required to be reported and the measure undertaken by the management to deal with such discrepancies in books of account is also to be reported by the auditors. Now, the casually reporting that the verification is carried out, will see an end.

This insertion is the one of the boldest and biggest steps towards transparent reporting which will have a very significant impact. Pursuant to this clause, any Corporate which has borrowed / availed working capital limits from Banks or Financial Institutions by giving the Assets in security and where such total sanction borrowed / availed limit/s exceed Rs. 5 Crores (Rupees Five Crores Only) whether taken together or in tranches from single institution or multiple; the statutory auditors of such Corporate/s are required to report whether the data filed and submitted, by the company, in the quarterly results or statements with the such banks and lending institutions, is in line with the books of accounts entries. Here, the disclosure and reporting will create an extremely transparent spectrum for all the stakeholders such as: (i) The lending institutions will get a clear idea about their existing debt exposure within the organization (ii) The government and regulatory authorities will be in the position to determine the harmony between the data filed with the banks and lending institutions and Ministry of Corporate Affairs (MCA); any mismatch in the data and the government / external and bank auditors will be in position to fishiness within the Corporate (iii) Since all the reporting is duly verified and authenticated by the statutory auditors, there shall be no practice and efforts by the auditors to hide or not disclose essential information to favour the Corporates. (iv) The shareholders will be in the position to understand their spot as the owners of the Company.

Clause(iii) (a) & (b) Reporting whether during the year, the Company **has made investments, provided guarantee or security or granted any loans or advances, 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**, if so, indicate whether: -

(A) the aggregate amount during the year, and balance outstanding at the balance sheet date is with respect to **subsidiaries, joint ventures and associates**

(B) the aggregate amount during the year, and balance outstanding at the balance sheet date is with respect 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) **Schedule of repayment** of principle and interest stipulated and whether the **receipts are regular**

(d) the **amount is overdue**, if so, state the overdue total **amount for more than ninety days, and steps undertaken for recovery**

(e) any loan or advance in the nature of loan granted has fallen due during the year, which is renewed, 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];

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(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;

➤ Analysis:

The scope of reporting the financial transactions pursuant to CARO 2020 is enhanced and widened so much that now the reporting covers transactions with respect to investments made, guarantee or security provided or any loans or advances granted, secured or unsecured, with any / all parties; whether outsiders or insiders, whether related parties or not related parties. Furthermore, it is also required to be reported by the statutory auditors that all such financial transactions are not prejudicial to the Company's interest. With the increased stringent reporting requirements, the non-compliance or lethargy towards the non-compliant transactions is expected to end, along with expecting an active involvement by the promoters and professionals involved towards all such transactions. The other essential details such as repayment of the amount borrowed, settlement of the loans etc., purpose and realization of amount of funds utilized for / from loans, relevant in depth details of investment, guarantees or security/ies to any/all by persons and/or entities will also be required to be reviewed by the auditors and covered under the scope of reporting making the entire balance sheet more transparent for the stakeholders to review and analyse. Further, the subsequent sub-clauses of Clause (iii) of CARO 2020 requires the auditors to report and disclose the details with respect to repayment of principal and interest, whether the receipts are regulars and in consensus with repayment schedule, details about the overdue amount, if any, and the total overdue amount for more than 90 days is also required to be reported along with steps taken for recovery of such overdue amount. The details about the enhancement / renewal of the existing loans or advances granted, investments made, guarantee or security provided, and details whether the renewal/enhancement is done for clearing the existing loans or any amount fallen due during the period; and whether any loan or advance is granted to promoters or related parties without specifying repayment terms is also required to be reviewed, audited and reported in the auditors report. This reporting will help reduce the attempts of evasion of repayment of loans and advances and reduce the number of defaults with respect to repayment of loans and advances. Merely reporting that the amount is not recoverable or not realizable will not hold any authenticity or validity, instead adequate justification will be required for all such transactions and subsequent reporting.

(This clause is not applicable, to the extent as specified in the CARO 2020 circular, to companies whose principal Business is to Give Loans).

Clause (iv) Reporting whether there is Compliance of **Section 185 & 186** of the Companies Act, 2013, with respect of loans, investments, guarantees and security. If not, provide the details thereof.

➤ Analysis:

There is no change with respect to reporting requirement between the previous CARO 2016 and the new CARO 2020. The most non-compliant and serious transactions are generally rising from transactions pursuant to Section 185 & 186 of the Companies. This reporting requirement has always been mandatory and required and hence even in the earlier CARO 2016 reporting this was included.

Clause (v) Reporting 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;

➤ Analysis:

The previous CARO 2016 also mandatorily required the auditors to report about the compliance with respect to deposits provisions and applicable sections, however pursuant to this detailed insertion in CARO 2020, even those events and transactions which earlier were not considered under the deposits section compliance; are now covered and required to be reported and disclosed by the auditors. There were certain transactions attracting and hinting the applicability of deposits provisions, however such transactions were under the earlier CARO reporting requirement were disclosed as additional facts and reported as regular business transaction in the grouping, additional information and/or notes to accounts; but now accurate reporting and disclosure by the auditors will be mandatorily required.

Clause (vi) Reporting 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;

➤ Analysis:

There is no change in the reporting requirement with respect to this Clause, between the previous CARO 2016 and the new CARO 2020. Pursuant to applicable cost records provisions certain class of companies are required to maintain cost records details and give regular disclosures for the accounts and records maintained by the Company.

Clause(vii) (a) & (b) Reporting whether the **undisputed statutory dues** to various authorities are regularly deposited by the Company, if not, the outstanding statutory dues details are required to be reported. In case where the **amount is not deposited due to dispute then the amount and forum where dispute is pending**, is required to be reported.

➤ Analysis:

There is as such not change in the reporting required between CARO 2016 and 2020, only the Goods and Services Tax has been additionally included for reporting by auditors. The purpose is to learn about the existing unpaid dues to authorities along with knowing about the existing disputes, if any.

Clause (viii) Reporting 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, if so, whether the previously unrecorded income has been properly recorded in the books of account during the year.

➤ Analysis:

This newly added clause of CARO 2020 aims to give chance to the corporates to report and disclose properly in the books of account - the unreported and unaccounted income for all the years. The aim of such reporting is to determine the details of the income/s properly reported in the books of account by auditors and the due taxes required to be paid on such reported / unreported income are accurately paid or not. When the auditors will report the relevant information with respect to all the current as well as previous unrecorded incomes along with giving confirmation or non-confirmation about the income tax and relevant provisioning with respect to the same, it will help reduce the tax avoidance or evasion by the Companies. Since the auditors are required to report and confirm the same, it can be presumed that the Auditors will not provide any leverage to the Companies considering their certification is at stake.

Clause (ix)

(ix) (a) Reporting whether company has **default in repayment of loans or borrowings**. If yes, then amount and period of default to be reported in Specified Format provided.

(ix) (b) Whether the company is **declared wilful defaulter** by any bank or financial institution or other lender is to be reported.

➤ Analysis:

This Clause (ix) reporting is made exhaustive and transparent to the maximum extent possible. The earlier CARO 2016 required reporting the default in repayment of loans or borrowing **to a financial institution, bank, Government or dues to debenture holders** against which the CARO 2020

requires reporting default in repayment of borrowings **to any lender** in the specified format for disclosing Lender-wise details about the nature of the borrowings, amount of default to be reported, amount unpaid on due date, No. of days of delay. The purpose here is to get clear idea - whether the Company / the Management is making regular payments towards the borrowings or not; as well as whether there is enough liquidity in the Company to repay the debts from time to time. Additionally, under this clause, it is required to report if the company is **declared wilful defaulter** by any bank or financial institution or other lender. Simplifying the terminology - A *wilful defaulter* is a Company / Individual that has ability to repay the borrowings but has not repaid the debts, wilfully creating default. With Auditors reporting such tags and titles to the Company as well as the Board, all the stakeholders will know about the actual situation of the Company. All the lending institutions will also be clear about not financing the Company anymore and identify and implement ways to recover the existing amounts lent. With the continuous increase in the number of defaults cases such disclosure and reporting by the auditors is quite essential.

(ix) (c) Whether the **term loans** were applied for the purpose intended, if not, the amount of loan so diverted and purpose for which it is used is required to be reported.

(ix) (d) Whether the **funds raised on short term** basis have been **utilized for long term purpose**, if yes, then amount and nature of the same is required to be reported.

➤ Analysis:

Next sub-clause requires reporting whether the terms loans were applied for the purposes intended or not - with this CARO 2020 reporting, it will be identified clearly if there is any siphoning of funds. If there are instances where the funds borrowed in name of business assets acquisition or expansion are actually paid to directors of the Company and / or indirectly diverted to the directors for their personal benefit. The funds being borrowed public money; it is required to keep a constant watch and hence the disclosure requirement is essential. The next sub-clause require confirmation whether the funds raised on short term basis are utilized for long term purpose, if yes, to report the amount and nature of such transactions. Such reporting will also clarify the route of the transactions and determine whether the Company in actuality utilizes the funds for the purpose which they are raised for. There is no change in the reporting requirement from the earlier CARO 2016 reporting requirement, the same provision is continued.

(ix) (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;

(ix) (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;

➤ Analysis:

The Clause (ix) (e) requires auditors to report and confirm if any amount is borrowed for meeting the obligations of its subsidiaries, associates or joint ventures, if yes, then nature of transaction and / or the default if any on such transaction is required to be reported. Such reporting will highlight and disclose all the financial transactions with all the sister concerns and clear picture of where the borrowed funds are routed can be known along with ensuring that all the compliance with respect to such transactions are taken care of. The next sub-clause (ix) (f) requires auditors to confirm and report if company has raised any loans by pledging the securities held in its subsidiaries, associates or joint ventures, and if yes, then details with respect to such loans and such pledged securities is required to be given along with disclosing the details of defaults, if any, occurred or created, on such loans. With the mandatory dematerialization of shares / securities it has become quite easy to determine the class of securities, details of pledged securities, the date, duration, the details of pledgee and pledgor. With subsequent reporting by the auditors of all these transactions with relevant disclosures will give clear understanding of the entire money routing as well as the extent of involvement in the transaction will be clearly recognized.

Clause (x) (a) Reporting 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;

Clause (x) (b) Reporting 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,

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whether the compliance with relevant section is done 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 non-compliance;

➤ Analysis:

The public money is to be infused in the Company by way of initial / further public offering, while making offer to the public for infusing their monies into the Company, as a part of compliance it is required to intimate the purpose for which the funds are raised. However, this after money receipt compliance disclosure that the monies are actually utilized for the purpose/s they are raised for will help understand clearly whether the funds raised from public are not diverted to promoters and directors of the Company through uncertain transactions.

Similarly, when funds are raised through preferential allotment or private placement of shares, pre-transactions action require confirmation by the Companies to disclose the purpose and reasons for which the funds are raised. Now, in case if the funds are used for any other purpose/sother than specified is required to be disclosed by the auditors along with details of amount involved and nature of non-compliance. This attempt will help resolve the issues of funds diversion since even the auditors reporting and disclosure can be reconciled with the relevant accounting entries.

Clause (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;

Clause (xi) (b) Whether any report under sub-section (12) of Section 143 of the Companies Act, 2013, has been filed by the auditors in Form ADT-4.

Clause (xi) (c) Whether auditor has considered whistle-blower complaints, if any.

➤ Analysis:

According to previous CARO 2016, reporting with respect to any fraud by company is noticed or reported during the year was required to be confirmed and reported by the auditors, however CARO 2020 made the scope of this clause more exhaustive covering the frauds being reporting by the auditors as well as by any insider or outsider under the whistle blower mechanism. There could be clear possibility that the auditors while carrying out audit and investigating the transactions of the Company might have found some suspicious entries or transactions and might as well have reported to the Central Government within such time and in such manner as may be prescribed under the Act. And with this reporting disclosure the clarity will be obtained for not only current transactions but also for preceding such transactions which might be hid or not reported by the previous auditors. With the rotation of auditors also one of the mandatory criteria more and more transparency will be brought in reporting standards. Furthermore, this clause also covers the reporting/s pursuant to whistle-blower mechanisms, there are clear possibility that there are certain suspicious transactions or unethical behaviour reported through whistle-blower complaints. The auditors are required to review and consider the same along with taking in consideration the opinions and reports of the internal auditors on such internal transactions reporting/s. This disclosure intends to showcase whether the auditors are reporting the reality and considering the whistle-blowing complaints and subsequent actions against the wrongdoings and unethical behaviour within the organization.

Clause (xii) (a) to (c)

Clause (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;

Clause (xii) (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;

Clause (xii) (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;

➤ Analysis:

The earlier CARO 2016 required only a plain text confirmation about the applicability and compliance with respect to Nidhi Company provisions. In CARO 2020 reporting, the scope of disclosure is enhanced and additional and specific reporting is required to be made by the auditor with respect to maintaining ten per cent. unencumbered term deposits, default in payment of interest on deposits and repayment thereof etc. Such disclosures will bring more transparency with respect to compliance of Companies Nidhi (Rules), 2014.

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

➤ Analysis:

The earlier CARO 2016 provision is continued without any change. In any business transaction, the biggest and the major loophole in the transparency is the related party transactions (RPTs). There are Corporates which enter in to the RPTs with malafide intention to siphon the public funds. Though the transactions undergo approval from the audit committee and subsequently from the board, but there are clear chances of the transactions being unethical. When the reporting and disclosures of the narrations of the transactions along with factual representation from the statutory auditors after considering the reports of internal auditors will validate and vouch the authenticity of the transactions and confirm compliance with applicable provisions of the Companies Act, 2013.

Clause (xiv) (a) Whether **Internal Audit System** is commensurate with the size and nature of the Company.

Clause (xiv) (b) Whether **reports of Internal Auditors** were considered by the Statutory Auditor.

➤ Analysis:

The earlier CARO 2016 provision is continued here and the only purpose behind this disclosure requirement was to ensure that there exists a check and control within the organization not leaving any loophole for any insider or outside fraudster to take benefit of it. There are genuine organization which adopt the internal control systems even when it is not applicable to them pursuant to mandatory provision requirement of Companies Act, 2013. Now, the next sub-clause is included to ensure that where there are internal auditors appoints their reports are considered and reviewed before giving final verdict on the financial position of the Company. Almost all those companies which have public funds infused are required to appoint internal auditors and it is a part of internal auditors' duty to diligently review the performance and working of every unit, sub-unit, division, sub-division, plant, entity site etc., based upon their scope of work and reporting time frame, every internal auditors after due verification of all the working and performance of the company must have updated the shortfalls, if any, in the internal audit reports, which are duly placed before the board and the board thereafter it is also determined whether the board has taken relevant measure to remove and eliminate the deficit in the functioning within due time. Such compliance will ensure transparent working and limit chances of fraud occurrence. At the year end, when statutory auditors review all the reporting by the internal auditor along with the minutes of the meetings, they can easily cross examine everything and come to concrete conclusion.

Clause (xv) Reporting whether any **non-cash transactions** with directors or persons connected with him were entered into, if yes, then whether provisions of Section 192 of the Companies Act, 2013 have been complied with.

➤ Analysis:

Non-cash transactions are those transactions that do not directly involve actual transfer of money. Non-cash transactions such as depreciation gain/loss on sale of assets, increase in taxes payable which have impact on the financials of the Company do not really have any impact and are covered under the textual notes of the independent statutory auditors' report. However, reporting such transactions will shut down the window of scheming and befooling the investors. Reporting in the independent auditors report as well as reporting confirmation in CARO clause with respect to all the non-cash transactions of the Company as well as Directors will help identify the uncertain routes, if any, adopted to misuse the funds or if unnecessary leverage taken from any law or provision or Section or statute.

Clause (xvi) (a) Reporting whether the company is **required to be registered u/s 45-IA of the Reserve Bank of India Act, 1934**, if yes, whether the registration is obtained or not.

Clause (xvi) (b) Whether any **non-banking financial or housing finance activities** are carried out without a valid certificate of registration from RBI.

➤ Analysis:

Such disclosure is to ensure that the companies are carrying out activities as specified in their main object clause only and that no other business activities are carried out to earn other incomes. There

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are events where the Companies are incorporated with certain main object activities but instead start earning revenues by way of dividend income or interest income and such other incomes / revenues which are generated through NBFC activities. And such financial revenues generated have higher share than the main business activities revenues in the total revenue making them NBFC Companies. According to the compliance criteria, necessary approvals (Certificate of Registration - CoR) from RBI is required to be obtained before carrying out such activities. This is one of the major non-compliance which is generally overlooked not just by the auditors but also at times by the authorities such as Ministry of Corporate Affairs etc. Pursuant to this clause confirmation compliance, the auditors are required to closely review the revenue earned and disclose that the NBFC activities are not carried out by the Company without a valid certificate of registration from RBI, since the otherwise consequences will be very harmful for the Company as well as the Management.

Clause (xvi) (c) Whether the Company is a **Core Investment Company (CIC)**, if yes, whether it fulfils the criteria of CIC and where company is exempted or unregistered CIC, whether it continues to full such criteria.

Clause (xvi) (d) Whether the **group has more than 1 CIC as part of the group**, if yes, indicate the numbers of CIC's.

➤ Analysis:

Under this CARO 2020 clause, the auditors are required to check whether any Company is exempted or Unregistered CIC and whether the Company continues to fulfil the required criteria as prescribed by RBI from time to time. Further, the auditors are also required to check if there is any group of CICs, then the auditor is required to make report all the details of all CICs under that group. Core Investment Companies (CICs) are NBFCs holding not less than 90% of their net assets in the form of investment in equity shares, preference shares, bonds, debentures, debt or loans in group companies. Group Companies mean any of the relation such as: subsidiary, parent, joint venture, associate, and/or any other related parties in terms of all the sections, provisions, clauses, rules etc. of Act, Regulations etc. as applicable to the Company. With this disclosure of CARO 2020, the big scams and the default can be avoided.

Clause (xvii) Reporting 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.

➤ Analysis:

The earlier CARO 2016 provision clause is continued. The Cash losses such as: Depreciation and amortization are to be added in giving negative representation in profit before tax. All the cash losses incurred by company in current and previous financial year/s are reported separately or cumulatively along with giving related details in the books notes of accounts. Separate amount and accounting details with reference to operational, financial and investing activities are be clearly known and understood.

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

➤ Analysis:

There are instances where when the statutory auditors have identified something fishy within the organization or with respect to any transactions, and the statutory auditors might have intimated the board about his intention to report all such transactions in financial statements prepared and signed by the auditors. Under such circumstances there is a possibility that either the auditor/s is forced to resign or on insistence of the board / management to not report certain details / certain transactions the auditors must have voluntary resigned. Either way the required reporting was not reached to the stakeholders of the Company. In order to overcome such reporting lapses the financial issues, CARO 2020 requires reporting the resignation of previous auditors along with identifying and reporting the issues, objections or concerns of the outgoing auditors. Furthermore, where the outgoing auditors do not submit valid reasons for his/her resignation then he/she is likely to undergo scrutiny by their alma mater - ICAI on professional and ethical courtesy basis.

Clause (xix) Reporting whether 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,

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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**

- Analysis:
CARO 2020 requires a specific certification that no material uncertainty exists, as on audit report date, in a company to pay off its liabilities existing on the balance sheet date, within a period of one year from balance sheet date. This new clause has increased the auditor's responsibility to determine very closely the entire working and the financial health of any Corporate audited. Reviewing and obtaining details about the financial ratios, ageing of financial assets along with expected date of realisation and obtaining the details with respect to payment dates of financial liabilities and such other information such as board's plan, the auditors will be able to reach to a conclusive opinion whether the organization is financially stable and capable to pay-off the liabilities at any future date of one year from now. This in its basic understanding is reviewing the working of the Company and confirming the accounting assumption of going concern. There is a Standard of Auditing (570 – *Going Concern*) which requires auditors to validate the fundamental of going concern as well.

Clause (xx) (a) & (xx) (b)

(a) Reporting 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 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) Reporting whether **any amount remaining unspent** under sub-section (5) of section 135 of the Companies Act, 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;

- Analysis:
Earlier reporting only with respect to CSR spending was required to be done, along with disclosing the details of non-spending or short-spending, if any. Pursuant to amendment, any amount remaining unspent towards CSR, if not related to any ongoing project to transfer the amount to the fund specified in Schedule VII with *six months* from the end of financial year and where the amount unspent is pursuant to any ongoing project (fulfilling such conditions as may be prescribed), undertaken by a company in pursuance of its CSR Policy, shall be transferred by the company within a period of *thirty days* from the end of the financial year to a special account being opened by the company in that behalf for that financial year in any scheduled bank to be called the “**Unspent Corporate Social Responsibility Account**”, and such amount shall be spent by the company in pursuance of its obligation towards the CSR Policy within a period of *three financial years* from the date of such transfer, failing which, the company shall transfer the same to a Fund specified in Schedule VII, within a period of *thirty days* from the date of completion of the third financial year. And the amendment also attracts the penalties for contravention of the provisions of the Act. This mandate and disclosure will reduce the incidence of mismanagement of CSR funds which is left unspent by the Company and merely reported as the non-spending in the Board's Report.

Clause (xxi) Reporting whether there have been **any qualifications or adverse remarks by the respective auditors** in the 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.

- Analysis:
As per the requirement of Act and applicable provisions, accounts of group entities are required to be consolidated, in such case of multiple entities such as: subsidiaries, joint ventures and associates etc., it is possible that either one audit firm may undertake and carry out all the audits of group entities or different audit firms may be involved for the auditing process of the entire group. CARO 2020 requires that any qualifications or adverse remarks by the respective auditors in the CARO reports of the companies included in the consolidated financial statements are to be disclosed. Such reporting was

not there in CARO 2016, however with this inclusion in new reporting format the auditors will review all the transactions with the group entities are consider the judgements and comments of other professionals involved in the verification and scrutiny process making the entire reporting more transparent and crystal clear for the stakeholders of all the group companies.

IV. ADDITIONAL REPORTING POINTS OF CARO 2020

Further, CARO 2020, also required the auditors to state the basis for such unfavourable or qualified answers or reporting, as the case may be. And where the auditor/s is unable to express any opinion on any specified matter, the report shall indicate such fact as well together with all the reasons as to why it is not possible for the auditor/s to give any opinion – whether qualified or not qualified, on the same.

With the pandemic spreading all around the globe, the Ministry of Corporate Affairs vide its circular dated 24th March, 2020, extended the applicability of the CARO 2020 from the Financial Year 2019-2020 to Financial Year 2020-2021.

V. CONCLUSION

The entire set of financial statements is under the scanning and scrutiny by the audit professionals with the introduction of the CARO, 2020. This reporting not only sets multiple filters for the compliance and verification of the applicable acts, regulations and the rules framed for applicable entities. The whole and sole motive behind the introduction of such new audit disclosure and compliance requirement was to ensure that the audit professionals minutely verify, scrutinize and report any/all discrepancies found internally with the organization to all the stakeholders extremely transparently. The expectations from the reporting format and reporting professionals increase emphasis and trust on the reported financial stability, profitability and liquidity position of the organization. An attempt towards reducing the chances of frauds presuming that the professionals and governing authorities involved will carry out the check and controls extremely precisely, morally, consciously and transparently.

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