

ANNEXURE TO CARO 2016 dated 29.03.2016 read with Guidance Note on the Companies (Auditor's Report) Order, 2016 dated 23.04.2016.

S.O. 1228(E). —In exercise of the powers conferred by sub-section (11) of section 143 of the Companies Act, 2013 the Central Government, after consultation with the, committee constituted under proviso to sub-section (11) of section 143 of the Companies Act, 2013 hereby makes the following Order, namely: —

Paragraph-1. Short title, application and commencement. - (1) This Order may be called the Companies (Auditor's Report) Order, 2016.

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

(except means companies not covered by the order-and this status is done at balance sheet date)

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

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

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

(iv) a One Person Company as defined under clause (62) of section 2 of the Companies Act and a small company as defined under clause (85) of section 2 of the Companies Act; 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 rupees 1 crore as on the balance sheet date and which does not have total borrowings exceeding rupees 1 crore 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, 2013 (including revenue from discontinuing operations) exceeding rupees 10 crore during the financial year as per the financial statements. *(That means in order to be exempt from the applicability of the Order, must satisfy all the conditions mentioned above collectively. In other words, even if one of the conditions is not satisfied, a private limited company's auditor has to report on the matters specified in the Order.)*

Points extracted from guidance note:

1. It may be noted that in case a company is covered under the definition of small company, it will remain exempted from the applicability of the CARO even if it falls under any of the criteria specified for private company.

2. Paid-up share capital would include both equity share capital as well as the preference share capital. While calculating the paid-up capital, amount of calls unpaid should be **deducted** from and the amount originally paid-up on forfeited shares should be added to the figure of paid-up capital. Share application money received should **not** be considered as part of the paid-up capital.

3. the term **“reserve”** as, “The portion of earnings, receipts or other surplus of an enterprise (whether capital or revenue) appropriated by management for a general or specific purpose other than provision for depreciation or diminution in the value of assets or for a known liability.

4. As per schedule III of Companies Act 2013 **“Reserves & Surplus”** consists of:- Capital Reserves; • Capital Redemption Reserve; • Securities Premium Reserve; • Debenture Redemption Reserve; • **Revaluation Reserve**; • Share Options Outstanding Account; • Other Reserves—(specify the nature

and purpose of each reserve and the amount in respect thereof); • Surplus i.e., balance in Statement of Profit and Loss (Debit balance of Statement of Profit and Loss shall be shown as a negative figure under the head "Surplus".)

5. For determining the applicability of the Order to a private limited company, both capital as well as revenue reserves should be taken into consideration while computing the limit of rupees 1 crore;

6. There is no stipulation in the Order that the borrowing should be a long-term borrowing or a short-term borrowing or that it should be a secured borrowing or an unsecured borrowing. Current maturity of long term borrowings will also form part of borrowings. Moreover, outstanding dues in respect of credit cards would also be considered while calculating the limit of Rs. 1 crore; Therefore, loans taken from a private bank or a foreign bank would also be taken into consideration while examining the applicability of the Order.

7. total revenue would include **other income** as per Schedule III.

Paragraph-2. 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 $\geq$ 1st April, 2015, shall in addition, contain the matters specified in paragraphs 3 and 4, as may be applicable:

Provided the Order shall not apply to the auditor's report on consolidated financial statements(CFS).

Points extracted from guidance note:

1. Reporting under this Order shall be applicable for the financial year 2015-16 and onwards. In case the auditor has to report on the financial statements for the financial year prior to 2015-16, then the relevant earlier Order shall be applicable (i.e. CARO 2015).

Paragraph-3. Matters to be included in the 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:

-
Clause (i) (a) whether the company is maintaining proper records showing full particulars, including quantitative details and situation of fixed assets;

Points extracted from guidance note:

1. what constitutes proper records is a matter of professional judgment made by the auditor after considering the facts and circumstances of each case.

(b) whether these fixed assets 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;

Points extracted from guidance note

1. If a material discrepancy has been properly dealt with in the books of account (which may or may not imply a separate disclosure in the accounts depending on the circumstances of the case), it is not necessary for the auditor to give details of the discrepancy or of its treatment in the accounts but he is required to make a statement that a material discrepancy was noticed on the verification of fixed assets and that the same has been properly dealt with in the books of account.

2. The auditor has, therefore, to use his judgement to determine whether a discrepancy is material or not. In making this judgement, the auditor should consider not merely the cost of the asset and its relationship to the total cost of all assets but also the nature of the asset, its situation and other relevant factors.

(c) whether the title deeds of immovable properties are held in the name of the company. If not, provide the details thereof;

Points extracted from guidance note

1. This clause shall cover the immovable properties which are included under the head Fixed Assets, as the reporting under Clause 3(i)(a) & 3(i)(b) pertains to Fixed Assets only.

2. The Act does not define the term **“Immovable Property”**. However, as per General Clauses Act, 1897, “Immovable Property” shall include land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth.

3. TDRs (Transfer Development Rights), Plant and Machinery embedded in land etc., are **not** considered as an immovable property.

4. Following documents mainly constitute title deeds of the immovable property: -

(i) Registered sale deed / transfer deed / conveyance deed, etc. of land, land & building together, etc. purchased, allotted, transferred by any person including any government, government authority / body/ agency / corporation, etc. to the company.

(ii) In case of leasehold land and land & buildings together, covered under the head fixed assets, the lease agreement duly registered with the appropriate authority.

Clause (ii) whether physical verification of inventory has been conducted at reasonable intervals by the management and whether any material discrepancies were noticed and if so, whether they have been properly dealt with in the books of account;

Points extracted from guidance note

1. What constitutes “reasonable intervals” depends on circumstances of each case. Normally, wherever practicable, all the items of inventories should be verified by the management of the company at least once in a year. It may be useful for the company to determine the frequency of verification by ‘A-B-C’ classification of inventories, ‘A’ category items being verified more frequently than ‘B’ category and the latter more frequently than ‘C’ category items.

2. If the item for which the discrepancy cannot be established is not material, the discrepancy, if any, will also not be material. For example, an item categorised as ‘C’ in ABC analysis might not be material and therefore, the discrepancy, if any, in regard to such an item would not be material.

3. In other cases, however, the auditor will have to report that he is unable to determine the discrepancy, if any, on physical verification for the item or class of items to be specified.

Clause (iii) whether the company has granted any loans, secured or unsecured to companies, firms, Limited Liability Partnerships or other parties covered in the register maintained under section 189 of the Companies Act, 2013. If so,

(a) whether the **terms and conditions** of the **grant** of such loans are not prejudicial to the company’s interest;

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

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

Points extracted from guidance note

1. Clause 3(iii)(a) uses the term “**grant**” which would ordinarily be understood to mean loans granted/given during the year, however, it may be appropriate to include such loans also that were renewed during the year.

2. Clauses 3(iii)(b) and 3(iii)(c) cover the loans granted during the year and also all loans having opening balances.

3. The auditor is required to disclose the requisite information in his report in respect of all parties covered in the register maintained under section 189 of the Act irrespective of the period to which such loan relates.

4. Further, there is no stipulation regarding the loan being given in cash or in kind.

5. the auditor should also take into consideration the loan transactions that have been squared-up during the year and report such transactions under this clause. For example, the company has, during the financial year, granted a loan of Rs. 1,00,000/- to a firm in which one of the directors of the company is interested and the firm repays the loan during the financial year concerned. The auditor is also required to consider such transaction while commenting upon this clause of the Order.

6. The “**terms and conditions**” would primarily include rate of interest, security, terms and period of repayment and restrictive covenants, if any.

7. the auditor may also come across a situation where the company has a policy of providing loans at concessional rates of interest to its employees and such a loan has been given to a relative of the director who is also an employee of the company. In such a case also, the auditor would be required to examine and comment whether loan is prejudicial to the interests of the company. It may, however, be noted that normally such terms as per the policy followed by the company cannot be said to be prejudicial to the interest of the company if other employees of the company also receive the loan on the same terms.

8. The word ‘**regular**’ should be taken to mean that the principal and interest should normally be received whenever they fall due, respectively.

9. The auditor should ask the management to give in writing, the steps which have been taken. The auditor should arrive at his opinion only after consideration of the management’s representations and other relevant evidence.

10. The particulars of all contracts or arrangements in which directors are interested is required to be maintained by every company in Form MBP-4 as specified in Rule 16(1) of the Companies (Meetings of Board and its Powers) Rules, 2014. It is, however, suggested that the auditor should acquaint himself with all the requirements of sections 184, 188 and 189 of the Act and rules there under.

Clause (iv) in respect of loans, investments, guarantees, and security whether provisions of section 185 and 186 of the Companies Act, 2013 have been complied with. If not, provide the details thereof.

Points extracted from guidance note

1. Obtain from the management the details of the directors or any other person in whom the director is interested. He may also check the details of the persons covered under this clause from Form MBP-1 and from the Register maintained u/s 189 of the Act.
2. In case of transactions that are covered under the exceptions as provided under section 185, the auditor should obtain the necessary evidence in support of such exception.
3. Section 185 prohibits advance of any loan to directors, etc., directly or indirectly. What is an indirect loan is not defined in section 185 or elsewhere in the Act. For example, if company A borrows from company B and lends the same to company C and loan from B to C is covered by section 185. In this case section 185 shall also be applicable in case of lending from company A to C because it would be construed as an indirect loan from B to C.
4. Check whether the company has maintained a register (as per Form MBP-2) in the manner as prescribed and also check the compliances of other provisions and relevant rules.

Clause (v) in case, the company has accepted 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, 2013 and the rules framed 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?

Points extracted from guidance note

1. Section 2(31) has defined ‘**deposit**’ to include any receipt of money by way of deposit or loan or in any other form by a company, but does not include such categories of amount as may be prescribed in consultation with the Reserve Bank of India.
2. The auditor should plan to test for compliance with the provisions of sections 73 to 76 of the Act and the Rules made thereunder i.e. the Companies (Acceptance of Deposits) Rules, 2014. For such purpose, the auditor should also obtain an understanding of the requirements of sections 73 to 76 and rules thereunder.
3. The auditor may also make a “check list” to ensure that all the requirements of the Rules regarding the records to be maintained, returns to be filed, etc., are complied with.
4. The auditor, under this clause, is required to verify whether the company has complied with the order passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any Court or any other Tribunal. If the company has not complied with the order, the same is to be reported stating therein the nature of contravention and the fact that the company has not complied.

Clause (vi) whether maintenance of cost records has been specified by the Central Government under sub-section (1) of section 148 of the Companies Act, 2013 and whether such accounts and records have been so made and maintained.

Points extracted from guidance note

1. The word “made” applies in respect of cost accounts (or cost statements) and the word “maintained” applies in respect of cost records relating to materials, labour, overheads, etc.
2. The auditor has to report under the clause irrespective of whether a cost audit has been ordered by the central government.
3. The Order does not require a detailed examination of such records. The auditor should, therefore, conduct a general review of the cost records to ensure that the records as prescribed are made and maintained. He should, of course, make such reference to the records as is necessary for the purposes of his audit.
4. Where the auditor finds that the records have not been written or are not prima facie complete, it will be necessary for the auditor to make a suitable comment in his report.

Clause (vii)

(a) whether the company is regular in depositing undisputed statutory dues including 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 6 months from the date they became payable, shall be indicated;

(b) where dues of income tax or sales tax or service tax or duty of customs or duty of excise or value added tax 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).

Points extracted from guidance note

1. It may be noted that the auditor has to report on the regularity of deposit of statutory dues irrespective of the fact whether or not there are any arrears on the balance sheet date.
2. For the purpose of this clause, the auditor should consider a matter as “**disputed**” where there is a positive evidence or action on the part of the company to show that it has not accepted the demand for payment of tax or duty, e.g., where it has gone into appeal. For this purpose, where an application for rectification of mistake (e.g., under section 154 of the Income Tax Act, 1961) has been made by the company, the amount should be regarded as disputed. Where the demand notice/intimation for the payment of a statutory due is for a certain amount and the dispute relates only to a part and not the whole of such amount, only such amount should be treated as disputed and the balance amount should be regarded as undisputed.
3. It is quite possible that an amount is disputed and has not been deposited but on consideration of the likely outcome of the dispute, a provision has been made in the accounts. Such an amount will need to be reported, notwithstanding that it has been provided for. Similarly, even if it had not been provided for, it would have to be reported as long as it is not deposited.

Clause (viii) whether the company has defaulted in repayment of loans or borrowing to a financial institution, bank, Government or dues to debenture holders? If yes, the period and the amount of default to be reported (in case of defaults to banks, financial institutions, and Government, lender wise details to be provided).

Points extracted from guidance note

1. It is clarified that the auditor should report the period and amount of all defaults existing at the balance sheet date irrespective of when those defaults have occurred.
2. The auditor should obtain the confirmation of the concerned bank or financial institution as to the status of the loan account including the overdue position as at the balance sheet date.
3. It may be noted that for the purposes of reporting of default under this clause the term "borrowings" may be construed as the principal amount since it has been used in the context of the word "repayment" and the term "dues" would mean the principal and the interest.

Clause (ix) whether moneys raised by way of initial public offer or further public offer (including debt instruments) and term loans 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;

Points extracted from guidance note

1. Currently, there is no legal requirement under the Act to disclose the end use of money raised by Initial Public Offer or Further Public Offer (including debt instruments) in the financial statements. The companies, however, make such a disclosure in the Board's Report. Schedule III to the Act requires that only unutilized amount of any Initial Public Offer or Further Public Offer (including debt instruments) made by the company should be disclosed in the financial statements of a company. In the absence of any legal requirement of such disclosure, it appears that the clause envisages that the companies should disclose the end use of money raised by the Initial Public Offer or Further Public Offer (including debt instruments) in the financial statements by way of notes and the auditor should verify the same.
2. If, for any reason, the auditor is not able to verify the end-use of money raised from Initial Public Offer or Further Public Offer (including debt instruments), he should state that he is not able to comment upon the disclosure of end-use of money by the company since he could not verify the same. He should also mention the reasons which resulted in the auditor's inability to verify the disclosure.
3. In case, the company has appointed a monitoring agency for the purpose of the issue, reports of the monitoring agency would also be helpful to the auditor while reporting under the clause.
4. offer for sale of specified securities (i.e. equity shares and convertible securities) to the public by any existing holder does not result in any moneys raised in a company, the same is outside the purview of the reporting requirement under this clause.
5. moneys raised from foreign capital markets and by way of issuance of Global Depository Receipts and American Depository Receipts may not fall within the scope of reporting under this clause.
6. Cash credit, overdraft and call money accounts/deposits are, therefore, not covered by the expression "term loans".
7. It is not necessary to establish a one-to-one relationship with the amount of term loan and its utilisation. It is quite often found that the amount of term loan disbursed by the bank is deposited in the common account of the company from which subsequently the utilisation is made. In such cases, it should not be construed that the amount has not been utilised for the purpose it was raised.

Clause (x) whether any fraud by the company or any fraud on the Company by its officers or employees has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated;

Points extracted from guidance note

1. Fraud involving one or more members of management or those charged with governance is referred to as "management fraud"; fraud involving only employees including officers of the entity is referred to as "employee fraud". In either case, there may be collusion with third parties outside the entity. In fact, generally speaking, the "management fraud" can be construed as "fraud by the company".
2. In this context, the auditor should also have regard to the Guidance Note on Reporting on Fraud under Section 143(12) of the Companies Act, 2013, issued by ICAI.
3. Two types of intentional misstatements are relevant to the auditor's consideration of fraud - misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.
4. Misappropriation of assets involves the theft of an entity's assets. Fraudulent financial reporting may be committed by the company because management is under pressure, from sources outside or inside the entity, to achieve an expected (and perhaps unrealistic) earnings target particularly when the consequences to management of failing to meet financial goals can be significant.
5. However, this Clause will include only the reported frauds and not suspected fraud.

Clause (xi) whether managerial remuneration has been paid or provided in accordance with the requisite approvals mandated by the provisions of section 197 read with Schedule V to the Companies Act? If not, state the amount involved and steps taken by the company for securing refund of the same;

Points extracted from guidance note

1. It may be noted that section 197 applies only to a public company. The term "public company" has been defined under section 2(71) of the Act. Thereby, section 197 of the Act is not applicable to a Private Company, and, accordingly, reporting under this clause would not be required.
2. term "Remuneration" under section 2(78) is defined.

Clause (xii) whether the Nidhi Company has complied with the Net Owned Funds to Deposits in the ratio of **1:20** to meet out the liability and whether the Nidhi Company is maintaining 10% unencumbered term deposits as specified in the Nidhi Rules, 2014 to meet out the liability;

Points extracted from guidance note

1. The auditor should note that as such a Nidhi Company can accept deposits not exceeding 20 times of its net owned funds as per last audited balance sheet.
2. As per Rule 3(d) Net Owned Funds are defined as the aggregate of paid up equity share capital and free reserves as reduced by accumulated losses and intangible assets appearing in the last audited balance sheet: **Provided** that, the amount representing the proceeds of issue of preference shares, shall not be included for calculating Net Owned Funds.

3. A Nidhi company can accept fixed deposits, recurring deposits accounts and savings deposits from its members in accordance with the directions notified by the Central Government. The aggregate of such deposits is referred to as “deposit liability”.

4. The auditor should ask the management to provide the computation of the deposit liability and net owned funds. The comments of the auditor should be based upon such a statement provided by the management and verification of the same by the auditor.

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

Points extracted from guidance note

1. The Related Party, with reference to a company is defined in section 2(76) of the Act.

2. duty of the auditor, under this clause is to report:

(a) Whether all transactions with the related parties are in compliance with section 177 and 188 of the Companies Act, 2013.

(b) Whether related party disclosures as required by relevant Accounting Standards (AS 18, as may be applicable) are disclosed in the financial statements.

3. Auditor can refer SA 550, “Related Parties” which has prescribed auditor’s responsibilities regarding related party relationships and transactions when performing an audit of financial statements, including guidance on the procedures to be performed by auditors.

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

Points extracted from guidance note

1. It may be noted that the term “preferential allotment” is not defined under the Act.

2. The term ‘Private Placement’ has been defined under the Explanation (ii) to section 42(2) to mean any offer of securities or invitation to subscribe securities to a select group of persons by a company (other than by way of public offer) through issue of a private placement offer letter and which satisfies the conditions specified in section 42 of the Act.

3. All monies payable towards subscription of securities under section 42 of the Act shall be paid through cheque or demand draft or other banking channels but not by cash.

4. the auditor should compare such information provided by the Company in Form PAS-4 with the actual utilization of the monies as per the books of account of the Company.

Clause (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 Companies Act, 2013 have been complied with;

Points extracted from guidance note

1. The reporting requirements under this clause are in two parts. The first part requires the auditor to report on whether the company has entered into any non-cash transactions with the directors or any persons connected with such director/s. The second part of the clause requires the auditor to report whether the provisions of section 192 of the Act have been complied with. Therefore, the second part of the clause becomes reportable only if the answer to the first part is in affirmative.

2. In other words, such transactions involving change in the assets or liabilities of a company but not involving “cash” or cash equivalents” as defined under Accounting Standard (AS) 3, “Cash Flow Statement” may be construed as **non-cash transactions**.

3. The term **“person connected with the director”** has not been defined in the Act, or the Rules thereunder. Instead, the term “to any other person in whom the director is interested” is defined in the Explanation to sub section (1) of section 185 of the Act.

4. Form No. MBP 1, Form No. MBP 2, Form No. MBP 4, would provide evidence of any such non-cash transactions that have actually taken place.

5. The auditor should check compliance with Section 192(2) and verify the notice of the General Meeting that it includes particulars of arrangement along with the value of the assets involved such arrangements. The said value should be calculated by the register valuer.

6. the auditor would need to obtain a management representation letter from the holding company through the management of the auditee company.

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

Points extracted from guidance note

1. Registration is required where the financing activity is a principal business of the company. “Financial activity as principal business is when a company’s financial assets constitute more than 50 per cent of the total assets and income from financial assets constitute more than 50 per cent of the gross income. A company which fulfils both these criteria will be registered as NBFC by RBI. The term 'principal business' is not defined by the Reserve Bank of India Act. The Reserve Bank has defined it so as to ensure that only companies predominantly engaged in financial activity get registered with it and are regulated and supervised by it. Hence if there are companies engaged in agricultural operations, industrial activity, purchase and sale of goods, providing services or purchase, sale or construction of immovable property as their principal business and are doing some financial business in a small way, they will not be regulated by the Reserve Bank. Interestingly, this test is popularly known as 50-50 test and is applied to determine whether or not a company is into financial business.

2. Whether the company has net owned funds as required for the registration as NBFC.

3. Whether the company has obtained the registration as NBFC, if not, the reasons should be sought from the management and documented.

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.