

Companies (Auditors' Report) Order, 2016 [CARO]

- Note:** 1. Section References are from Companies Act 2013, under otherwise specifically indicated.]
2. CARO 2016 is applicable from Financial Year 2015 – 2016 onwards.

A. CARO – Applicability & Reporting Matters

1. What types of Companies are specifically exempted from application of CARO?

1. **Applicability:** CARO 2016 applies to all Companies, including a Foreign Company as defined u/s 2(42).
2. **Exceptions / Exemptions:** CARO **does not apply** to the following classes of Companies –
 - (a) Banking Company as defined u/s 5(c) of the Banking Regulation Act, 1949,
 - (b) Insurance Company as defined Insurance Act, 1938,
 - (c) Company licensed to operate u/s 8,
 - (d) One Person Company as per Sec.2(62) and a Small Company as per Sec.2(85),
 - (e) Private Limited Companies which satisfy **all** the following conditions –
 - Should **not** be a Subsidiary or Holding Company of a Public Company,
 - Aggregate of Paid Up Capital and Reserves & Surplus $\leq ₹ 1 \text{ Crore}$, as on the Balance Sheet date,
 - Total Borrowings from any Bank or Financial Institution at any point of time during the Fin. Year $\leq ₹ 1 \text{ Crore}$,
 - Total Revenue (including Revenue from Discontinuing Operations) as disclosed in the Financial Statements as per Schedule III of the Companies Act, $\leq ₹ 10 \text{ Crores}$. [**Note:** Total Revenue includes "Other Income" also.]
3. **CFS:** CARO 2016 reporting shall **not** apply to the Auditor's Report on Consolidated Financial Statements.

2. Bring out the differences between compliance with the requirements of Sec. 143 of COA 2013 and CARO.

CARO Requirements are **supplemental** to the provisions of Sec.143 regarding the Auditor's Report. However, certain points of distinction between CARO and Sec.143 requirements are –

Requirements of Sec 143	Requirements of CARO
1. Sec.143 (1), (2), (3) and (4) are applicable to all Companies .	1. Certain classes of Companies are exempt from CARO. (Refer previous question).
2. Sec.143 (1) requires the Auditor to make certain specific enquiries during the course of his audit. The Auditor is, however, not required to report on any of the matters specified in the sub-clauses, unless he has any special comments to make on the said matters, i.e. if he is satisfied with the results of his enquiries, he has no further duty to report that he is so satisfied.	2. CARO requires a statement on each of the matters specified therein, even if the Auditor has no comments to make on any of the matter(s) contained therein.

3. Bring out the professional necessity for complying CARO. Is it mandatory?

1. **Additional Matters for reporting [Sec.143(11)]:** The Central Government may order for the inclusion of a Statement on specified matters in the Auditor's Report for specified class or description of Companies. Accordingly, CARO 2016 is issued by the Central Government, and should be complied by the Statutory Auditor of the Company.
2. **Nature of CARO:** CARO is **not intended to limit the duties and responsibilities** of Auditors, but only requires a Statement to be included in the Audit Report in respect of the matters specified therein.
3. **Govt. Cos:** For Govt. Companies, CARO is **supplemental** to the Directions given by the C&AG of India. So, in respect of Govt. Companies, the matters specified in CARO will also form part of the Auditor's Report.

4. List the matters to be reported under CARO, 2016.

1. **FIXED ASSETS [3(i)]:**
 - (a) Whether the Company is maintaining proper records showing full particulars, including quantitative details and situations of Fixed Assets.

- (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.
 - (c) Whether the Title Deeds of Immovable Properties are held in the name of the Company. If not, provide the details thereof.
2. **INVENTORIES [3(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 accounts.
3. **LOANS TO DIRECTORS AND INTERESTED PARTIES [3(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 u/s 189. 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.
4. **Compliance of Sec.185 & 186 [3(iv)]:** In respect of Loans, Investments, Guarantees, and Security, whether provisions of Sec.185 and 186 have been complied with. If not, provide the details thereof.
5. **DEPOSITS FROM PUBLIC [3(v)]:** In case, the Company has accepted Deposits, whether the directives issued by the Reserve Bank of India and the provisions of Sec.73 to 76 or any other relevant provisions of COA 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 RBI or any Court or any other Tribunal, whether the same has been complied with or not?
6. **COST ACCOUNTING RECORDS [3(vi)]:** Whether maintenance of Cost Records has been specified by the Central Government under Sec.148(1), and whether such accounts and records have been so made and maintained.
7. **STATUTORY DUES [3(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).
8. **REPAYMENT OF DUES [3(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).
9. **APPLICATION OF MONEYS RAISED [3(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.
10. **FRAUD [3(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.
11. **MANAGERIAL REMUNERATION [3(xi)]:** Whether Managerial Remuneration has been paid or provided in accordance with the requisite approvals mandated by the provisions of Sec.197 read with Schedule V? If not, state the amount involved and steps taken by the Company for securing refund of the same.
12. **NIDHI COMPANY [3(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?

13. **RELATED PARTY TRANSACTIONS [3(xiii)]:** Whether all transactions with the Related Parties are in compliance with Sec.177 and 188 where applicable, and the details have been disclosed in the Financial Statements, etc. as required by the applicable Accounting Standards?
14. **PREFERENTIAL ALLOTMENT, etc. [3(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 Sec.42 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.
15. **NON CASH TRANSACTIONS WITH SPECIFIED PERSONS [3(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 Sec.192 have been complied with.
16. **REGISTRATION UNDER RBI ACT [3(xvi)]:** Whether the Company is required to be registered under Sec.45-IA of the Reserve Bank of India Act, 1934 and if so, whether the registration has been obtained.
17. **Reasons to be stated for unfavourable or qualified answers [Para 4]**
 - (a) Where the answer to any of the above questions is unfavourable or qualified, the Auditor's Report shall state the reasons for such unfavourable or qualified answer, as the case may be.
 - (b) If the Auditor is unable to express any opinion in answer to any particular question, his Report shall indicate such fact, together with reasons why it is not possible for him to give an answer to such a question.

B. Meaning of Terms

5. Explain the term "Paid-up Capital" in determining CARO applicability for Private Limited Companies.

1. **Exemption:** To be exempt from application of CARO, a Private Limited Company should have Paid Up Capital and Reserve & Surplus $\leq$ ₹ 1 Crore as on the Balance Sheet date.
2. **Sec.2(64):** "Paid-Up Capital" means aggregate amount of money credited as paid-up as is equivalent to the amount received as paid up in respect of Shares issued.
It also includes any amount credited as paid up in respect of Shares of the Company.
It does not include any other amount received in respect of such shares, by whatever name called.
3. **ICAI Guidance Note:** As per ICAI Guidance Note on Terms used in Financial Statements, the term "Paid-Up Share Capital" is defined as that part of the Subscribed Share Capital for which consideration in Cash or otherwise has been received. This includes Bonus Shares allotted by the Corporate Enterprise.
4. **PSC included:** Paid-Up Share Capital would include **both** Equity Share Capital as well as Preference Share Capital.
5. **Exclusions:** Share Application Money received should **not** be considered as part of the Paid-Up Capital.
6. **Other Items:** While calculating Paid-Up Capital, amount of Calls Unpaid should be deducted therefrom, and the Amount Originally Paid-Up on Forfeited Shares should be added to the figure of Paid-Up Capital.

6. Explain the term "Reserves" in determining CARO applicability for Private Limited Companies.

1. **Reserves:** As per ICAI Guidance Note on Terms used in Financial Statements, "**Reserve**" is 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.
2. **Capital Reserve** is a Reserve of a Corporate Enterprise which is **not** available for distribution as Dividend. **Revenue Reserve** means any Reserve other than Capital Reserve.
3. **Schedule III:** Reserves & Surplus shall be classified as –
 - (a) Capital Reserves,
 - (b) Capital Redemption Reserve,
 - (c) Securities Premium Reserve,
 - (d) Debenture Redemption Reserve,
 - (e) Revaluation Reserve,

- (f) Share Options Outstanding Account,
- (g) Other Reserves,
- (h) Surplus, i.e. balance in Statement of P&L disclosing allocations & appropriations such as Dividend, Bonus Shares and Transfer to/from Reserves etc. (Additions & Deductions since last B/s to be shown under each of specified heads).

4. **Reserves for the purpose of CARO** = Any Reserve (Capital Reserves + Revenue Reserves + Other Reserves) as disclosed in Schedule III of the Companies Act, 2013

Note: Profit and Loss Account (Dr.): Debit balance of Statement of P&L shall be shown as a Negative Figure under the head 'Surplus'. Similarly, the balance of 'Reserves & Surplus', after adjusting Negative balance of Surplus, if any, shall be shown under the head 'Reserves & Surplus' even if the resulting figure is in the negative. Similar to Schedule III requirement, for the purpose of applicability of CARO, debit balance of Profit and Loss Account, **same shall be netted** for computing Reserves & Surplus.

7. Explain the term "Borrowings" in determining CARO applicability for Private Limited Companies.

1. **Exemption:** To be exempt from application of CARO, **Total Borrowings** from any Bank or Financial Institution of a Private Limited Company, at any point of time during the Financial Year, should not exceed ₹ 1 Crore.
2. **Aggregate Amount:** For this purpose, "Any Bank or Financial Institution (FI)", would refer to the **aggregate** to all Loans and not with reference to each Bank or Financial Institution.
3. **Types:** Borrowings from Banks or Financial Institutions can be Long Term or Short Term, and includes Term Loans, Demand Loans, Export Credits, Working Capital Limits, Cash Credits, Overdraft Facilities, Bills Purchased or Discounted.
4. **Amount Outstanding:** Outstanding Balances of such Borrowings should be considered as Borrowing Outstanding for the purpose of computing the limit of ₹ 1 Crore.
5. **Fluctuating Balances:** In case a Company enjoys a facility, (e.g. Cash Credit facility), whose balance is fluctuating in nature, CARO would apply in case **on any day** during the Financial Year, the amount outstanding in Cash Credit Facility exceeds ₹ 1 Crore.
6. **Other Points:**
 - (a) Where the Company is granted an Overdraft Facility against Fixed Deposits of the concerned Bank, the amount Outstanding in Overdraft Facility (and **not net of FD**) is considered for the purpose of CARO.
 - (b) Outstanding Dues in respect of **Credit Cards** would also be considered while calculating the limit of ₹ 1 Crore in respect of "Borrowings" from a Bank or Financial Institution.

8. Explain the term "Banks" and "Financial Institution" for the purpose of applicability of CARO.

1. The term **"Banks"** refers to a Bank as defined under Banking Regulation Act, 1949. Therefore, even Loans taken from a Private Bank or a Foreign Bank would also be taken into consideration while examining the applicability of CARO.
2. The term **"Financial Institution"** used in CARO includes a Scheduled Bank and any other Financial Institution, defined or notified by RBI. It also includes NBFC's.

C. Applicability of CARO – Practical Issues

9. Explain the applicability of CARO to Foreign Companies.

1. CARO applies to **all Companies**, except certain categories of Companies specifically exempted therein.
2. CARO also **applies to Foreign Companies** as defined u/s 2(42). "Foreign Company" means any Company or Body Corporate incorporated outside India which –
 - (a) has a place of business in India whether by itself or through an Agent, physically or through electronic mode, **and**
 - (b) conducts any business activity in India in any other manner.
3. In respect of Foreign Companies, an established place of business in India would **include a Liaison Office**.

10. CA Vishwam is appointed as the Branch Auditor of VVK Ltd. Is he required to comply with the CARO when issuing his Branch Audit Report, or is CARO applicable only with respect to the Audit Report issued by the Principal Auditor?

1. Sec.143(8) specifies that a Branch Auditor has the same duties in respect of audit, as the Company's Auditor.
2. Also, the Branch Auditor shall prepare a report on the accounts of the Branch examined by him and send it to the Auditor of the Company who shall deal with it in his report in such manner as he considers necessary.
3. The Report submitted by the Branch Auditor should contain a statement on all the matters specified in CARO, to enable the Company's Auditor to consider the same. Hence, CARO is **applicable** for Branch Audits also.

11. BK Ltd, a Benefit Fund, registered under NBFC Regulations, is in existence for the past two decades. On 31st December 2015, this Company is converted into a Bank. You have been appointed as an Auditor for the Financial Year 2015–2016. Comment whether CARO is applicable for this Company.

1. Banking Companies are exempted from CARO Reporting Requirements.
2. As on the date of B/Sheet, the Company is a Banking Company. Hence, CARO is **not applicable**, irrespective of the fact that the Company was converted from NBFC during the year.

12. Samraksha Pvt Ltd is the Holding Company of Suraksha Ltd. The Paid Up Capital and Reserves ₹ 30 Lakhs. The Borrowings from SBI is ₹ 60 Lakhs. Total Revenue from Operations (including from Discontinuing Operations) are ₹ 8 Crores.

The Auditors of Samraksha Pvt Ltd is of the view that CARO is not applicable since it is a Private Limited Company satisfying the condition relating to Paid up Capital, Borrowings and Total Revenue. Is their contention valid?

Whether CARO reporting is applicable for reporting on Consolidated Financial Statements?

1. **Principle:** Refer **Q. No. 1** on the **4 conditions, all of which** have to be satisfied by a Private Limited Company, to be exempt from CARO Reporting.
2. **Analysis:** In this case, Samraksha Pvt Ltd is the **Holding Company** of Suraksha Ltd, a Public Company. Hence, CARO is applicable for Samraksha Pvt Ltd. [Monetary Limits in other 3 conditions are **not relevant** in this case.].
3. CARO 2016 Reporting shall **not apply** to the Auditor's Report on Consolidated Financial Statements.

13. Mittal Pvt Ltd provides the following information for the Financial Year 2015–2016. Comment whether CARO is applicable for this Company: (a) Paid-up Share Capital and Reserves – ₹ 100 Lakhs, (b) Borrowings from Banks – ₹ 98 Lakhs, (c) Total Revenue – ₹ 12 Crores.

1. **Principle:** Refer **Q. No. 1** on the **4 conditions, all of which** have to be satisfied by a Private Limited Company, to be exempt from CARO Reporting.

2. **Analysis:**

Condition	Analysis
(a) Not a Holding or Subsidiary of a Public Company	Assumed satisfied
(b) Paid up Capital and Reserves & Surplus on B/s date ≤ ₹ 1 Crore	Satisfied, since it is equal to ₹ 1 Crore.
(c) Bank / Fin.Institution Borrowings at any time, ≤ ₹ 1 Crore	Satisfied, since it is less than ₹ 1 Crore.
(d) Total Revenue ≤ ₹ 10 Crores	Not satisfied, i.e. > ₹ 10 Crores

3. **Conclusion:** CARO is **applicable** in the above case, since Total Revenue condition is attracted.

14. CA Bhava is appointed as the Auditor of BB Pvt Unlimited, a Company registered under Companies Act, with Unlimited Liability. For Financial Year 2015–2016, the Company had a Total Revenue of ₹ 8 Crores, Borrowings from Banks and FI of ₹ 86 Lakhs and Paid-Up Capital with Reserves of ₹ 97 Lakhs. Explain whether his Audit Report must include CARO.

1. The term "Private **Limited** Company", as used in the exemption from CARO, should be construed to mean a Company registered as a "Private Company" [as defined in Sec.2(68)], **and** which has a **Limited Liability**.

2. So, CARO would be **applicable to Private Unlimited Companies**, irrespective of the size of their Paid-Up Capital and Reserves, Total Revenue, Borrowings from Banks/Financial Institutions.
3. Hence, in the present case, Total Revenue / Capital Base / Borrowings Criterion need not be considered for the Company and CARO is **applicable** fully to BB Pvt. Unlimited.

15. Guru Pvt Ltd has 2 Branches – in Chennai and in Mumbai. Each Branch has a separate Statutory Auditor and the Company, as a whole, has a Central Statutory Auditor. Comment which of these Auditors must comply with CARO.

Details	Chennai Branch	Mumbai Branch	Total
Paid up Capital and Reserves (in ₹ Lakhs)	40	70	110
Borrowings from Banks (in ₹ Lakhs)	10	26	36
Total Revenue (in ₹ Crores)	3	6	9

1. **Principles:**
 - (a) Conditions to be satisfied for being exempt from CARO are laid down for the Company **taken as a whole**.
 - (b) So, if CARO is applicable to the Company as a whole, then **each and every Branch** of the Company will also be automatically covered under CARO (irrespective of the fact that the Branch's transactions are within the limits).
 - (c) The Branch Auditor has the same reporting responsibilities in respect of the Branch, as those of the Company Auditor in respect of the Company. The comments of the Branch Auditor in respect of the Branch are dealt with by the Central Statutory Auditor of the Company while finalizing his report under CARO.
2. **Analysis:** In the given case, the Company has a Paid up Capital and Reserves of ₹ 110 Lakhs, which exceeds the exemption limit ₹ 100 Lakhs / 1 Crore. CARO is applicable for the Company.
3. **Conclusion:** So, in this case, all the 3 Auditors. (2 Branch Auditors + Central Statutory, Auditor) must comply with CARO.

16. Vayu Pvt Ltd has a Turnover of ₹ 8 Crores for the Financial Year 2015–2016. The Outstanding Balance of Loans from Banks and Financial Institutions is ₹ 24 Lakhs throughout the year. The Company had a Capital of ₹ 120 Lakhs at the beginning of the year and on 15.09.2015 the Company made a Buy Back of Shares worth ₹ 30 Lakhs resulting in a Share Capital of ₹ 90 Lakhs as on 31st March 2016. Comment whether CARO is applicable for the Company.

1. **Analysis:**

Condition	Analysis
(a) Not a Holding or Subsidiary of a Public Company	Assumed satisfied
(b) Paid up Capital and R&S on B/s date ≤ ₹ 1 Crore	Satisfied, since the condition is with respect to B/s date. Net Amount ₹ 90 Lakhs is ≤ ₹ 1 Crore.
(c) Bank / Fin.Institution Borrowings at any time, ≤ ₹ 1 Crore	Satisfied, since ₹ 24 Lakhs ≤ ₹ 1 Crore.
(d) Total Revenue ≤ ₹ 10 Crores	Satisfied, since ₹ 8 Crores ≤ ₹ 10 Crores.

2. **Conclusion:** Since all 4 conditions are satisfied, CARO is **not** applicable in this case.

17. Keshav Pvt Ltd has a balance of ₹ 30 Lakhs as Capital Reserve, ₹ 30 Lakhs as Revenue Reserves, ₹ 40 Lakhs as Revaluation Reserve and ₹ 20 Lakhs as Paid-Up Share Capital as on 31st March. Comment on the applicability of CARO to this Company.

1. Reserves includes **all types of Reserves** (Capital Reserves, Revenue Reserves, Revaluation Reserve, etc)
2. Here, Paid-Up Capital + Reserves = ₹ 20 Lakhs (Paid-Up Capital) + ₹ 100 Lakhs (Capital Reserve + Revenue Reserve + Revaluation Reserve) = ₹ 120 Lakhs. Hence, CARO is applicable for this Company, since this exceeds the limit of ₹ 1 Crore.

18. Mahath Pvt Ltd provides the following information for the financial year ending 31st March. Comment whether CARO is applicable for this Company.

	(amounts in ₹ Lakhs)
Paid Up Share Capital	₹ 70.00
Capital Reserve	₹ 14.00

Revaluation Reserve	₹ 20.00
General Reserve	₹ 20.00
Profit and Loss (Dr.)	₹ 24.00

- As per Schedule III Requirements, Debit balance of P&L A/c, should be **reduced from the figure of Reserves**.
- In the present case,

(a) Paid-Up Capital	= ₹ 70 Lakhs
(b) Reserves	= 14 + 20 + 20 = ₹ 54 Lakhs
Less: P&L (Dr.)	= ₹ 24 Lakhs = ₹ 30 Lakhs
Paid Up Capital + Reserves	= ₹ 100 Lakhs
- Since Aggregate of Paid Up Capital and Reserves **does not exceed** ₹ 1 Crore, CARO is **not applicable** for this Company. (assuming other 3 conditions of exemption are satisfied.)

19. H Private Ltd had taken Overdrafts from SBI & HSBC with a limit of ₹ 40 Lakhs each against the security of Fixed Deposit it had with those Banks and an Unsecured Overdraft from a Financial Institution of ₹ 29 Lakhs. The said loans were outstanding as at 31st March. The Paid Up Capital and Reserves of the Company as at that date was ₹ 80 Lakhs and its Total Revenue during the financial year ended on 31st March was ₹ 6 Crores. The Management of the Company is of the opinion that CARO is not applicable to it because Total Revenue and Paid-Up Capital were within the limits prescribed and Borrowings against the Fixed Deposit cannot be considered. The Company further contended that Borrowings Limit is to be reckoned per Bank or Financial Institution and not cumulatively. Comment.

- Principles w.r.t. Borrowings:**
 - Borrowings against FD:** Amount Outstanding must be included in determining the limit. It should not be netted off against the amount of Fixed Deposit
 - "Borrowings from any Bank":** Total Borrowings from all Banks & Financial Institutions should be considered cumulatively, and **not** on "per Bank / FI basis". Thus, all Loans / Borrowings (secured or unsecured) should be included.
- Analysis:** Total Borrowings in this case = ₹ 40 + ₹ 40 + ₹ 29 = ₹ 109 Lakhs = ₹ 1.09 Crores.
- Conclusion:** Since Borrowings > ₹ 1 Crore, CARO Reporting is applicable to the Company.

20. In the current financial year, AP Pvt Ltd has borrowed ₹ 1.20 Crores on 15th June and repaid the entire loan before 31st March. Comment on the applicability of CARO to this Company.

- For the purpose of applicability of CARO, Balance Outstanding from a Bank or Financial Institution, shall be construed **at any point of time**, during the year and not as at the end of the year (i.e. 31st of March).
- Where the Company had Borrowings from a Bank in excess of ₹ 1 Crore during the year, but the year-end balance of the same is NIL, the Company would be still covered by CARO, notwithstanding that it fulfills all other conditions for exemption from the Order. In the present case, AP Pvt Ltd will be covered under CARO.

21. Anand Pvt Ltd is incorporated on 1st July 2015. During the year ended 31st March 2016, it had issued Shares (fully paid up) of ₹ 80 Lakhs, had borrowed ₹ 25 Lakhs each from 2 Financial Institutions and its Total Revenue (Net of Excise of ₹ 50 Lakhs which is credited to a separate account) is ₹ 975 Lakhs. Will CARO be applicable to Anand Pvt Ltd?

- Analysis:**

Condition	Analysis
(a) Not a Holding or Subsidiary of a Public Company	Assumed satisfied.
(b) Paid up Capital and R&S on B/s date ≤ ₹ 1 Crore	Satisfied, since ₹ 80 Lakhs ≤ ₹ 1 Crore.
(c) Bank / Fin.Instn Borrowings at any time, ≤ ₹ 1 Crore	Satisfied, since 25×2 = ₹ 50 Lakhs ≤ ₹ 1 Crore.
(d) Total Revenue ≤ ₹ 10 Crores	If Excise Duty is taken / credited to a separate account, it shall not form part of the Total Revenue. So, Total Revenue for this Co. = ₹ 9.75 Crores, i.e. ≤ ₹ 10 Crores.

- Conclusion:** CARO does not apply to Anand Pvt Ltd, since **all** the conditions relating to exemption are satisfied.

22. Tarun Pvt Ltd's Paid Up Capital and Reserves are less than ₹ 100 Lakhs and it has no Borrowings from any Bank or Financial Institution. Its Sales are ₹ 12 Crores before deducting Trade Discount ₹ 20 Lakhs and Sales Returns ₹ 190 Lakhs. The services rendered by the Company amounted to ₹ 20 Lakhs. Comment on applicability of CARO to this Company.

1. **Principles:** Total Revenue = [Sales ₹ 12 Crores (–) Trade Discount ₹ 20 Lakhs (–) Returns ₹ 190 Lakhs] + Services Income ₹ 20 Lakhs = Net ₹ 10.10 Crores

2. **Analysis:**

Condition	Analysis
(a) Not a Holding or Subsidiary of a Public Company	Assumed satisfied.
(b) Paid up Capital and R&S on B/s date ≤ ₹ 1 Crore	Satisfied, since it is given as ≤ ₹ 1 Crore.
(c) Bank / Fin.Institution Borrowings at any time, ≤ ₹ 1 Crore	Satisfied, since there are no Borrowings.
(d) Total Revenue ≤ ₹ 10 Crores	Not satisfied, Since Total Revenue > ₹ 10 Crores.

3. **Conclusion:** CARO applies to Tarun Pvt Ltd, since the Total Revenue **exceeds** ₹ 10 Crores.

D. CARO Reporting – Practical Issues

23. Bring out the requirements under CARO with regard to proper maintenance of Fixed Assets Register. [3(i)]

1. **Contents of FA Register:** The records relating to Fixed Assets should contain, the following details – (a) Description of Asset, (b) Classification (e.g. Plant and Machinery, Office Equipment, etc.), (c) Situation, (d) Quantity, (e) Original Cost, (f) Year of Purchase, (g) Adjustment for Revaluation or for any increase / decrease in cost, (h) Date of Revaluation, (i) Rate(s) / Basis of Depreciation or Amortization, (j) Depreciation / Amortisation Amount for the current year, (k) Accumulated Depreciation / Amortization, (l) Particulars regarding Impairment, (m) Particulars regarding Sale, Discarding, Demolition, Destruction, (n) Distinctive Number of Assets, etc.

2. **Coverage:** The FA Register must contain details in respect of the following assets –

- (a) Both Tangible or Intangible Assets.
- (b) Self-Financed or Acquired through Finance Lease.
- (c) Assets which are fully held for disposal, retired from active use, fully depreciated assets, period of useful life as per Schedule II of the Act.
- (d) Fully Impaired Assets.

3. **Form of Record:** FA Register can be maintained in manual form or in electronic form. The e-Form FA Register–

- (a) should be capable of being can be retrieved in a **legible form**.
- (b) should ensure that the information contained in the electronic records remains **accessible and unaltered** and its origin, destination, date, etc. can be identified.

Even if one of the above conditions is **not** satisfied, the Auditor should obtain a duly authenticated print-out of the Fixed Assets Register.

4. **Special Points:**

- (a) In case of Fixed Assets with **changing locations** (e.g. a Construction Equipment which has to be moved to various sites), it is sufficient if records of movement / custody of the Equipment is maintained.
- (b) In case of Assets like Furniture, etc. located in the **residential premises of the Staff**, the FA Register should indicate the Name / Designation of the Staff.
- (c) Electrical Installations need not be shown as a separate asset. For purposes of identification, it is suggested that the initial sub-division may be made according to the User, e.g. Factory Buildings, Plant, Service Departments, Township Buildings, etc. A further sub-division can be made according to the sub-division already made for Buildings, Plant, etc.
- (d) For Furniture & Fittings, individual identification can be made for high-value items, and by groups for other items.

24. Bring out the responsibilities of Management in relation to Verification of Fixed Assets. Also explain the Auditor's duties in this regard, with reference to CARO. [3(i)]

A Ltd, having Fixed Assets at 10 different locations, in total valuing ₹ 5,000 Crores, have been physically verifying the assets every third year. Auditor insists for yearly verification of the same. Comment.

1. **Outsourcing:** It is not necessary that only the Company's Staff should make the verification of Fixed Assets. It may also be verified by outside Expert Agencies engaged by the Management.
2. **Method of Verification:**
 - (a) The Auditor should examine whether the method of verification is **reasonable**, in the circumstances relating to each Asset. For example, in the case of certain process industries, verification by direct physical check may not be possible in the case of Assets which are in continuous use or which are concealed within larger units.
 - (b) Also, it is not always possible to suspend manufacturing operations merely to conduct a physical verification of the Fixed Assets, unless there are compelling reasons which would justify such an extreme procedure. In such cases, indirect evidence of the existence of the Assets may suffice. For example, the very fact that an Oil Refinery is producing at normal levels of efficiency may be sufficient to indicate the existence of the various process units even where each such unit cannot be verified by physical or visual inspection.
3. **Reasonable Intervals:**
 - (a) What constitutes "reasonable intervals" depends upon the **circumstances of each case**.
 - (b) While an **annual** verification may be **reasonable**, it may be impracticable to carry out the same in some cases (due to nature of assets, difficulty in verification, spread, etc). Even in such cases, the verification programme should be such that all assets are verified at least once in **every 3 years**.
 - (c) Where verification of all assets is not made during the year, it will be necessary for the Auditor to report that fact, but if he is satisfied regarding the frequency of verification he should also make a suitable comment to that effect.
4. **Material Discrepancies:** If a material discrepancy has been properly dealt with in the Books of Accounts (which may or may not imply a separate disclosure in the accounts), it is not necessary for the Auditor to give details of the discrepancy / its treatment in the Accounts. However, 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.

25. CA Tejas was appointed as the Auditor of AKS Ltd, which is covered under CARO. The Company has not maintained its Fixed Asset Register for the period April 2015 to December 2015. But from 1st Jan 2016, the Company started to maintain its Asset Registers properly and as on 31st March 2016, the FA Register is properly kept. Should CA Tejas report on the maintenance of FA Register in his report?[3(i)]

1. **Reporting Responsibilities:** The Auditor's reporting duties can be analysed from two perspectives, i.e. in the Main Audit Report (where he expresses his opinion on the Financial Statements) and in the CARO Report.
2. **CARO Reporting:** Compliance with CARO requirements should be judged based on the **whole Accounting Year** and not merely with reference to the position existing at the Balance Sheet date, or the date on which the Auditor makes his Report. Hence, in the above case, the Auditor will make a negative remark in his CARO Report.
3. **Main Audit Report:**
 - (a) In the Main Audit Report, the Auditor reports on the State of Affairs as they existed during the Accounting Year.
 - (b) In deciding whether or not to make an Adverse Report, the Auditor should consider what detrimental effect, if any, has been caused by the failure to comply with the requirements of CARO, for any part of the year.
 - (c) For example, if records for Fixed Assets were not properly maintained for some part of the year but were properly maintained at the B/S date and physical verification was made after the records were properly maintained, there is no detrimental effect on the Company. However, for example, if Internal Control with respect to the items specified in CARO Clauses was inadequate during a part of the year, there may be a detrimental effect on the Company.
 - (d) Also, the Auditor cannot ignore the position existing at the B/S date or at the time at which he makes his Report. The Auditor might consider, in the light of the circumstances and provided he is able to satisfy himself regarding the facts, as to whether a reference to the State of Affairs existing at the B/S date or at the date when he makes his report would be necessary to give a more complete picture to the Members to whom he is reporting.
4. **Conclusion:** In the present situation, the Auditor would comment on the non-maintenance of FA Register (for the part of the year) in his CARO Report & may consider issuing a Qualified Opinion in his Audit Report (considering facts of the case).
5. **Non-Reporting:** Also, where a requirement of CARO is not complied with, but still the Auditor decides to issue a Clean Report, he should record in his **working papers**, the reasons for not doing so.

26. Bring out the requirements of CARO in relation to Physical Verification of Inventory. [3(ii)]

1. **Periodicity:** Physical Verification of Inventory is the responsibility of the Management. Hence, Management should **verify all material items at least once in a year** and more often in appropriate cases. The Auditor should satisfy himself that the Physical Verification of Inventories has been conducted at "reasonable intervals" by the Management and that there is adequate evidence on the basis of which the Auditor can arrive at such a conclusion.
2. **Reasonable Intervals:**
 - (a) What constitutes "Reasonable Intervals" depends on **circumstances of each case**. The Management normally determines the periodicity of the Physical Verification of Inventories. Wherever practicable, all the items of inventories should be verified by the Management **at least once in a year**.
 - (b) 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.

**27. Comment on the following extracts from the Statutory Auditor's reports on the accounts of Limited Companies indicating with reasons, whether or not the form of reporting complies with the statutory and professional requirements –
"On the basis of examination, the valuation of Inventories is fair and proper and in accordance with normally accepted accounting principles, and is on the same basis as in the previous year except for some changes in the method of valuation of the inventories of Finished Goods". [3(ii)]**

1. **Principle:** As per Accounting Standards, any change in the accounting policy relating to Inventories which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. When there is a change in accounting policy (which has a material effect in the current period) the amount by which any item in the Financial Statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated.
2. **Conclusion:**
 - (a) Change in basis of Inventory Valuation amounts to a change in the basis of accounting. If the effect on profit is material, adequate disclosure should be made in the accounts or notes.
 - (b) The Auditor should ensure such change in method of valuation (including quantification of effect on the Financial Statements) should be disclosed in the Financial Statements or in the Notes. Else, he would not have satisfied the statutory reporting requirements.

28. Raji Ltd has fully computerized its accounting operations. The Stock Records are maintained up to date with timely entries passed for all receipts and issues. The Company has hired a professional security agency, which monitors and implements a close vigilance over the operations of the Company. As such, the Company had dispensed with the practice of taking stock of their Inventories as at the year-end, as in their opinion the exercise is redundant, time consuming and intrusion to normal functioning of the operations. [3(ii)].

The Auditor should **report** that the Company does not have any system of physical verification of Stock. Further, Stock being a material item in the Statement of P&L and Balance Sheet, the Auditor should qualify his report on the truth and fairness of Financial Statements.

29. What are the aspects that the Auditor has to verify in relation to Stock Registers? State with reference to CARO. [3(ii)]

1. **Proper Records:**
 - (a) Records relating to Inventories should contain data like – (a) Particulars of the Item like Nomenclature, Nature, etc.
 - (b) Identification Code of the Item, (c) Details regarding Quantity of Receipts, Issues, Balances and Dates of Transactions in a chronological manner, (d) Relevant Document Number and Department Identification, Location.
 - (b) If Priced Stores Ledger is maintained, the records of the inventory should also disclose the Prices at which the recording of the Issues and Receipts is made.
 - (c) The records should contain the particulars in respect of all items of inventories.
 - (d) The record of movement/custody of the inventory should be maintained.
2. **Auditor's Duties:** The Auditor should ensure that the Stock Registers are updated as and when the transactions occur. He should also verify that the transactions entered in Stock Registers are duly supported by relevant documents.

3. **Work in Progress:**

- (a) If the Company maintains Stock Records for WIP, the Auditor would normally be able to verify the same.
- (b) If it is impracticable to maintain Stock Records for WIP, the Auditor should consider the fact whether the Company, at any point of time, can arrive or calculate the quantity and amount involved in the WIP. For example, the value of WIP can be calculated based on production cycle, input/ output ratio analysis, production and stock records for the immediately following period, etc.
- (c) If the Company is able to do so, then no adverse comment of the Auditor under this Clause would be required.

30. **ABC Private Ltd has granted Loan of ₹ 20 Crores to XYZ Ltd, a Sister Concern, and it remains outstanding at the year-end. How would you report the fact? [3(iii), 3(iv), 3(xiii)]**

1. **Legal Compliance:** The Auditor should verify compliance with Sec.186 with respect to the above loan.
2. **Disclosure:** The Loan given should be shown in the Assets Side of the Balance Sheet, suitably classified as "Current" or "Non-Current" Loans and Advances.
3. **AS Compliance:** Since ABC Private Ltd granted Loan to XYZ Ltd (Sister Concern), requirements of Accounting Standards on "Related Parties" should be followed by ABC Private Ltd.
4. **Inquiry:** If the terms and conditions of the loan are prejudicial to the interest of the Company, the Auditor shall also report the same u/s 143(1).
5. **CARO:** The Auditor should also consider disclosure of these aspects in his Report under Clause 3(iii), 3(iv) and 3(xiii).

31. **A Public Company defaulted in the repayment of deposits together with interest on the due date for more than a year and the CFO contends that the Auditor need not report on the default committed by the Company. Comment. [3(v)]**

1. **Principle:** Refer –
 - (a) Reporting Requirements to Clause 3(v) of CARO, and
 - (b) Sec.143(3)(g), i.e. Reporting on Directors' Disqualification u/s 164(2).
2. **Conclusion:** The Auditor should report on default committed by the Company, under CARO clause 3(v).

32. **Discuss the responsibilities of an Auditor under CARO, on verification of Deposits received by the Company. [3(v)]**

1. **Scope:** This Clause requires the Auditors to report on compliance with the requirement of Sec.73 to 76, Rules there under and the directives of RBI relating thereto.
2. **Audit Procedures:**
 - (a) **Understanding:** The Auditor should obtain an **understanding** of the requirements of Sec.73 to 76, Rules thereunder, RBI Directions, etc. and should verify their compliance.
 - (b) **Audit Plan:** The Auditor should **plan** to test for compliance with the provisions of Sec.73 to 76 of the Act.
 - (c) **Examining Controls:** The Auditor should examine the **efficacy of Internal Controls** instituted by the Company so that the Deposits accepted by the Company remain within the limits. It may be difficult for the Auditor to ascertain that Deposits accepted by the Company are within the limits **on each day** of the Accounting Year. He would, therefore, be justified in making a reasonable **test check** to ensure that the Company has not accepted Deposits during the year in excess of the limits.
 - (d) **Check List:** 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.
 - (e) **Verifying Documentation:** The Auditor should examine the system by which deposits are accepted and records are maintained and make a reasonable **test check** to ensure the correctness of the system.
 - (f) **Special Consideration:** For Financial Companies, the Auditor should make a similar examination having regard to the RBI directives (e.g. Sec.45MA of RBI Act) in force from time to time.
 - (g) **Verifying Default:** The Auditor has to determine whether there is a default in any repayment of Deposits. Non-compliance of provisions.
 - (h) **Management Representation:** The Auditor should obtain a Management Representation to the effect whether the Company has complied Sec. 73 to 76, Rules there under, Directives issued by RBI & any other relevant orders.

- (i) **Reporting:** If the Auditor is of the view that any kind of contravention of Sec.73 to 76 or any other relevant provisions of the Act or Rules, has taken place, he should state in his report that the provisions have not been complied with, along with the nature of contraventions.

33. Bring out the reporting responsibilities of an Auditor under CARO, on maintenance of Cost Records. [3(vi)]

1. Maintenance of Cost Records [Sec.148(1)]:

- (a) **Requirement:** Companies notified by Central Government are required to maintain proper Books of Account showing particulars relating to utilization of material or labour or to other items of Cost as may be prescribed.
- (b) The Cost Accounting Records Rules issued for various industries contain requirements relating to two matters:
- maintenance of proper **Books of Account** relating to Materials, Labour, and Other items of Cost, and
 - preparation of **Cost Statements** at the end of the Financial Year in accordance with the Industry Rules.
- (c) **Periodicity:** While the records relating to Materials, Labour, etc. are required to be maintained on a day-to-day basis, the Cost Statements have to be prepared periodically.

2. Cost Audit [Sec.148(2)]:

- (a) Where in the opinion of the Central Government, it is necessary to do so in relation to any Company required u/s 148(1) to maintain the particulars prescribed under that Section, it may order a Cost Audit to be conducted of its Cost Accounts.
- (b) While a Cost Audit can be done only in respect of Companies governed by the Rules made u/s 148(1), Cost Audit is not necessary in respect of every Company which is required to maintain Cost Records.

3. Audit Considerations:

Scope of Review	• CARO does not require a detailed examination of Cost Records. The Auditor should, therefore, conduct a general review of Cost Records to ensure that the records as prescribed are made and maintained. • CARO requires the Auditor to report whether Cost Accounts and Records have been made and maintained. 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. • The Auditor has to Report under the clause irrespective of whether a Cost Audit has been ordered by the Central Government. • Where the Auditor finds that the records have not been written up or are not prima facie complete, it will be necessary for the Auditor to make a suitable comment in his report.
Management Representation	The Auditor should obtain a Written Representation from Management stating – • Whether Cost Records are to be maintained for any product of the Company u/s 148(1), • Whether Cost Accounts and Records are being made and maintained regularly, and • List of Books/records made and maintained in this regard.
Reporting Format	The following reporting format is suggested – "We have broadly reviewed the Books of Account maintained by the Company pursuant to the Rules made by the Central Government for the maintenance of Cost Records u/s 148(1) of the Act and are of the opinion that prima facie, the prescribed Accounts & Records have been made & maintained."

34. Bring out the Auditor's responsibilities in relation to Statutory Dues of the Company under CARO. [3(vii)]

1. Scope:

- (a) **Regular Levies:** The intention of this Clause is to ascertain how **regular** the Company is in depositing Statutory Dues with the Appropriate Authorities. Since the emphasis of the Clause is on the **regularity**, the scope of Auditor's inquiry is restricted to only those Statutory Dues, which the Company is required to deposit regularly to an Authority.
- (b) **Other Levies:** The Auditor is not required to ascertain whether the Company is regular in depositing amounts, which may be levied by an Appropriate Authority from time to time upon occurrence or non-occurrence of certain events and therefore are not required to be paid regularly.

2. Meaning of Statutory Due:

- (a) Any sum, which is to be regularly **paid to an Appropriate Authority under a Statute** (whether Central, State or Local or Foreign) applicable to the Company, should be considered as a "Statutory Due". So, the **obligation** to

pay a Statutory Due is created or **arises out of a Statute**, rather than being based on an Independent Contractual or Legal relationship.

- (b) Where any dues are **recoverable as Arrears of Land Revenue** by the concerned Authority, the same shall be treated as a Statutory Due. **Examples:** Municipal Taxes, TDS, License Fees (for Cinema Halls, etc).
- (c) Any sum payable to an Electricity Company as **Electricity Bill** would **not** constitute a Statutory Due, despite the fact that such a Company has been established under a Statute. This is so because the due has arisen on account of Contract of Supply of Goods or Services between the Parties.

3. **Regularity:**

- (a) The Auditor should understand clearly, the nature of each Statutory Due payable by the Company while examining the aspect of regularity before commenting on the same.
- (b) Regularity is a normal feature in case of certain Statutory Dues such as, PF, ESI, VAT, etc. because the Companies are required to deposit the money with Appropriate Authorities on a monthly or quarterly basis.
- (c) However in case of, say, Custom Duty on import of goods or Demands arising on account of Assessment Orders, etc. which a Company is required to pay as and when an event giving rise to the liability of the Company occurs. Such Dues should be construed to have been paid regularly, if the Company deposits them as and when they become due.
- (d) However, the Auditor would be required to comment upon the regularity of the Company in depositing the **instalments**, if any, granted by an Authority in respect of a Demand against the Company.

4. **Reporting Format Examples:**

- (a) While the Auditor has to report upon the regularity of the deposit, he is not required to specify in detail each instance where there has been a delay or the extent of the delay. It should be sufficient if he indicates whether **generally** the deposits have been regular or otherwise.

(b) **Reporting Examples –**

- “Undisputed Statutory Dues including PF or ESI, IT, VAT, Wealth Tax, ST, Custom Duty, ED, Cess have been regularly deposited by the Company with the Appropriate Authorities in all cases during the year” (or)
 - “Undisputed Statutory Dues ... Cess have generally been regularly deposited with the Appropriate Authorities though there has been a slight delay in a few cases” (or)
 - “Undisputed Statutory Dues..... Cess have not generally been regularly deposited with the Appropriate Authorities, though the delays in deposit have not been serious” (or)
 - “Undisputed Statutory Dues Cess have not been regularly deposited with the Appropriate Authorities and there have been serious delays in a large number of cases”.
- (c) In indicating the Arrears, the period to which the Arrears relate should also preferably be given and further, wherever possible, the fact of subsequent clearance or otherwise may also be indicated. The following is the format in which the Auditor may report the extent of the Arrears of Outstanding Statutory Dues:

Statement of Arrears of Statutory Dues Outstanding for More than Six Months

Name of the Statute	Nature of the Dues	Amount (₹)	Period to which the amount relates	Due Date	Date of Payment

5. **Amounts not fallen due:** The Report should be restricted to the Actual Arrears, and should not include the amounts which have not fallen due for payment to Appropriate Authority and have been recognized as Outstanding Dues at the Balance Sheet date.

35. Under CARO, an Auditor is required to report on the regularity of payment of Provident Fund and Employees' State Insurance dues. Give alternative drafts of the report on this Clause, mentioning the circumstances of reporting. [3(vii)]

1. **Auditor's Duties:**

- (a) The Auditor has to report on the regularity of deposit of PF / ESI dues irrespective of the fact whether or not there are any arrears on the Balance Sheet date. There may be situations where a Company has deposited the relevant dues before the end of the year, while it has been in default in the matter for a significant part of the year.
- (b) While the Auditor has to report upon the **regularity** of the deposit, he is not required to specify in detail each instance where there has been a delay or the extent of the delay. However, the extent of the arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than 6 months from the date they became payable, should be indicated.

2. **Alternative Drafts for Reporting:** Some examples of wordings, which may be used, are given below –
- "Provident Fund / Employees' State Insurance dues have generally been regularly deposited with the appropriate authorities in all cases during the year".
 - "Provident Fund / Employees' State Insurance dues have generally been regularly deposited with the appropriate authorities, though there has been a slight delay (less than 6 months) in a few cases".
 - "Provident Fund / Employees' State Insurance dues have not generally been regularly deposited with the appropriate authorities though the delays in deposit have not been serious".
 - "Provident Fund / Employees' State Insurance dues have not been regularly deposited with the appropriate authorities and there have been serious delays in a large number of cases. However, there are no arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than 6 months from the date they became payable".
 - "Provident Fund / Employees' State Insurance dues relating to the period and aggregating to ₹ which had fallen due for deposit with the appropriate authorities had not been so deposited as at..... Out of these, ₹ have been deposited subsequently".
 - "Provident Fund / Employees' State Insurance dues relating to the period and aggregating to ₹ which had fallen due for deposit with the appropriate authorities had not been so deposited as at..... The details of amounts outstanding for a period exceeding **6 months** from the date they became payable are given below:"

36. A Company having several departments with separate payrolls and where payments of wages are spread over several days, makes lump-sum deposits of estimated amounts of Provident Fund and Employees State Insurance dues and adjusts the excess or deficit against the following month's deposit. Comment on the above. [3(vii)]

- In a large Company with a number of departments with separate payrolls, and where payments are spread over a number of days, the collection of data regarding the PF / ESI collection and the Company's contribution thereto may take some time.
- To avoid delayed payments, the Company may make lumpsum deposits of estimated amounts and adjust the excess or deficit against the following month's deposit.
- If this method is consistently followed and the difference between the total dues and the lumpsum deposit is not material, it can be deemed as regularly deposited and hence, no adverse comment is necessary.

37. ABC Ltd has not deposited Provident Fund Contributions of ₹ 20 Lakhs to the authorities, but accounted in the books. Comment on the above. [3(vii)]

- Accrual:** Provident Fund contributions should be accounted in the books on accrual basis, whether paid or not. As per Sec.128(1), a Company has to maintain proper books of account, on accrual basis of accounting.
- Companies Act:** Under Sec.143(3)(e), the Auditor shall state whether the Balance Sheet and the Profit & Loss Account comply with the Accounting Standards u/s 133.
- CARO Requirements: Note: Refer to Clause 3(vii) of CARO.**
- Conclusion:** In the instant case, even though accrual principles have been followed, disclosure of non-payment is necessary in view of CARO. The Auditor should disclose the fact of non-payment of ₹ 20 Lakhs in his Report.

38. During the course of audit of ABC Ltd, it is noticed that out of ₹ 12 Lakhs of PF Contributions accounted in the books, only ₹ 2 Lakhs has been remitted to the Authorities during the year. On enquiry, the Chief Accountant informed that due to financial problems they have not remitted but will remit the same as and when the position improves. As a Statutory Auditor, how would you deal with the above situation? [3(vii)]

Hint Answer: In the given case, the Company has not complied with the requirements as to deposit of PF Contributions, to the tune of ₹ 10 Lakhs. Financial problems do not constitute sufficient reason for non-compliance. Hence, the Auditor shall report the non-compliance under Clause 3(vii) of CARO in his report.

39. B Ltd, manufacturing cycles, has 150 employees. Auditors observe that it has not registered itself for Provident Fund and ESI purposes, not remitting the dues in time and Auditor insists for qualifying the Report. Management contends that in the absence of registration, it cannot be construed that the Company is in default of statutory dues on regular basis. Comment. [3(vii)]

Hint Answer: Management's contention that it has not registered and so not paid the statutory due is not a valid reason for non-payment. Auditor is required to verify legal compliance as per **SA-250**. Hence, the Auditor shall report the non-compliance under Clause 3(vii) of CARO in his report, and also consider the effect of non-compliance with applicable Laws and Regulations.

40. Adhvaryu Ltd has not paid ESI and EPF on a monthly basis. However, the entire arrears are paid on the month of March (along with respective interest) and as on the Balance Sheet date, no amount is due to be paid in respect of EPF and ESI. Bring out the Auditor's responsibilities under CARO. [3(vii)]

1. 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. There may be situations where a Company has deposited the relevant dues before the end of the year while it has been in default in the matter for a significant part of the year.
3. In cases where there are no arrears on the Balance Sheet date, but the Company has been irregular during the year in depositing the Statutory Dues, the Auditor should **state this fact** in his Audit Report.

41. Karanja Imports Ltd imported goods 5 years back and were placed in Bonded Warehouse. The Import Duty remains due, and payable by the Company. The goods have not been removed from the Warehouse till the end of the Financial Year under audit. Bring out the reporting duties of the Auditor under CARO. [3(vii)]

1. **Import Duty:** When the Imported Goods are lodged in a Bonded Warehouse, Import Duty should be paid, only when the goods are removed from the Bonded Warehouse.
2. **Rent & Interest:** Till the time the Importer opts to remove the goods from the Bonded Warehouse, he is required to incur the Rent and Interest expenditure on the amount of Customs Duty Payable.
3. **Customs Duty:** Since the payment of the Custom Duty is not due in the current case, the question of regularity does not arise in respect of Custom Duty.
4. **Interest and Rent Dues:** Interest & Rent that are required to be incurred under Customs Act would come under "Other Statutory Dues". The Auditor should examine & comment under CARO, on the regularity of the Company in depositing such Interest and Rent.

42. Bhargava Ltd has not paid Advance Tax for the current Financial Year. Is it an irregularity in payment of Statutory Dues? Should the Auditor comment under CARO? [3(vii)]

1. **General Rule:** Non-payment of Advance Income Tax **would constitute default** in payment of Statutory Dues, since there are specified due-dates in respect of payment of Advance Income Tax.
2. **Windfall Gains:** It may, however, happen that the Company might not have any Taxable Income on the due dates on which Advance Tax is required to be paid. If a Company has such an Income after the last date on which the Advance Tax was required to be paid and consequently the Company incurs interest under the relevant provisions of the Income Tax Act, 1961, it should not be construed as irregularity in Advance Tax payment.

43. Bring out the meaning of the term "Disputed Due" for the purpose of Clause 3(vii) of CARO.

1. **Meaning:** 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.
2. **Rectification:** For this purpose, where an application for rectification of mistake (e.g. u/s 154 of Income Tax Act, 1961) has been made by the Company, the amount should be regarded as disputed.
3. **Representation:** Mere representation to the concerned Department does **not** by itself constitute a dispute.
4. **Dispute in part:** 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.

5. **Scope:** The Auditor need not examine the sustainability or otherwise of the claim of the Company regarding disputed amounts. It is sufficient for his purpose if the evidence available shows that the amount is disputed by the Company.

44. Rithvik Services Ltd provides “specified services” which was erstwhile exempt from Service Tax. In the current year, the Company, for the first 5 months, has neither collected nor remitted the Service Tax. However, the Central Government brought in the “specified services” in the ambit of Service Tax Levy, with retrospective effect from 1st April of current financial year. The Department of Excise and Customs raised a demand notice on the Company for the full year's Service Tax (along with interest for delayed payment for the first 5 months). The Demand Notice specified a due date of March 15th and the Company paid the entire due on that date. Is it an irregularity in Statutory Payment? [3(vii)]

1. **First View:** The Statutory Dues referred in Clause 3(vii) become payable on the last date by which payment can be made without attracting penalty and/or interest under the relevant law. Hence, in the above case, there is an irregularity in relation to the first 5 months Service Tax due.
2. **Second View:** It can also be argued that the amounts referred to in Clause 3(vii) become so payable as at the date of the expiry of the stay granted by the Authorities or, where instalments have been granted for the payment of Statutory Dues referred to in the Clause, the date on which the default occurs and the amount becomes payable to the Authorities. If this view is taken, in the above case, there is no irregularity in remittance of Service Tax.
3. **Conclusion:** As the purpose of this Clause is to indicate the amounts which have become actually payable & are outstanding as at the Balance Sheet date for a period of more than 6 months from the date they became payable, the latter view conforms more closely to the requirements of CARO. Hence, it can be concluded that the Company is not irregular in depositing Statutory Dues.

45. Bring out the reporting duties of an Auditor in CARO in relation to Disputed Statutory Due. [3(vii)]

1. **Scope of Reporting:** In case of Disputed Statutory dues, the Auditor is required to report the amounts involved, along with the Forum where the dispute is pending.

2. **Disputed Due:**

(a) Show Cause Notice (SCN)	• A SCN generally contains the requirements / queries of the Assessing Officer. However, normally, mere issuance of a SCN by the concerned Department, should not be construed to be a demand payable by the Company. • In some cases, a SCN and Demand may be combined in one document. Normally, in such cases, the Demand would not be construed to have arisen till the time the Assessee has disposed-off the requirements of the SCN. Hence, it is necessary to evaluate each situation individually.
(b) Demands Set Aside	Tax Demands that have been set aside are clearly not 'dues'.
(c) Re-Assessment	If a demand has been referred for re-assessment and the effect of such referral is the cancellation of the earlier demand, this would not constitute an amount due. The wording of the Re-assessment Order would be of significance, if the demand is not cancelled, it will remain Disputed Dues.
(d) Demands in Stay	Demands that have been stayed should be regarded as Disputed Dues. These should be disclosed along with a disclosure of the fact of stay. The Stay normally is a concession that the amount may not be deposited immediately or that it may be deposited in installments.
(e) Appeal by the Department	There may be a situation that the Appellate Authority has decided a case in favour of the Company but the Department may prefer to make an appeal to a Higher Authority. In such case, there is no dispute until the time the Department makes an appeal to the relevant Appellate Authority.
(f) Cases Pending Appeal	Where the amount under the dispute is pending for an Appeal to be filed and the time limit for filing the Appeal has lapsed , the disputed amount would become a Statutory Due . The reporting responsibilities of the Auditor as are applicable to any other Undisputed Statutory Due under Clause 3(vii) of CARO.

3. **Accounting Considerations:** The amounts to be reported under this Clause are those which have not been deposited on account of any Dispute, irrespective of the treatment of such disputed amounts in accounts.
 - (a) **If Provision created:** 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.
 - (b) **Provision not created:** Even if it had not been provided for, it has to be reported as long as it is **not deposited**.

- (c) **Treated as Recoverable:** It is also possible that an amount is disputed, has been deposited and on consideration of the likely outcome of the dispute, has been shown as a **Recoverable** (Asset in Balance Sheet). Though such an amount is not contemplated for reporting under the Clause, since it has been deposited, the fact of such deposit having been made under protest should be brought out by the Auditor in his Report under the Clause.

4. **Reporting Format:** The information required under this Clause may be reported in the following format:

Statement of Disputed Dues	Statute	Financial Year	Nature of Dues	Amount (₹)	Period to which the amount relates	Forum where dispute is pending

46. XYZ Pvt Ltd has submitted the Financial Statements for the year ended 31.03.2016 for audit. The Audit Assistant observes & brings to your notice that the Company's records show the following dues. As an Auditor, how would you bring this fact to the Members?

- (a) Income Tax relating to AY 2011–2012 ₹ 125 Lakhs. Appeal is pending before Hon'ble ITAT since 30.09.2013.
 (b) Customs Duty ₹ 85 Lakhs. Demand Notice received on 15.09.2015, but no action has been taken to pay or appeal.

1. **Income Tax Appeal:** **Refer Clause 3(vii) of CARO**

- (a) **Audit Procedures:** Obtain Management Representation and perform other audit procedures to verify the same.
 (b) **AS–29:** Check whether there is a need for the Company to make a Provision for the liability.
 (c) **Reporting:** Since the matter is under appeal, non-payment of dues is on account of a dispute. So, the amount involved and the forum where the dispute is pending should also be mentioned while reporting under CARO.

2. **Customs Duty Notice:** **Refer Clause 3(vii) of CARO**

- (a) Demand Notice has been received but no action has been taken for 6 months.
 (b) The Auditor shall report, the extent of the arrears of outstanding statutory dues as at the last day of the Financial Year concerned for a period of more than 6 months from the date they became payable.

47. Big and Small Ltd received a Show Cause Notice from Central Excise Department intending to levy a demand of ₹ 25 Lakhs in December 2015. The Company replied to the above notice in January 2016, contending that it is not liable for the levy. No further action was initiated by the Central Excise Department upto the finalization of the audit for the year ended on 31st March 2016. As the Auditor of the Company, what is your role in this? [3(vii)]

Hint: There is a **mere** Show Cause Notice and reply for the same. There is **no demand** made by the Department. Hence there is no dispute. The Auditor need **not** report on the same.

48. There is a Sales–Tax Demand of ₹ 3 Crores against X Ltd, relating to prior years against which the Company has gone into an appeal. Comment. [3(vii)]

1. **CARO:** It is a **disputed** statutory due. Hence, the Auditor has to report under **Clause 3(vii) of CARO**.
 2. **AS–29:** The Auditor has to verify whether there is a need for the Company to make a Provision for the liability.

49. Mani Ltd had obtained a Term Loan of ₹ 300 Lakhs from a Bank for the construction of a Factory. Since there was a delay in the construction activities, the said funds were temporarily invested in Short Term Deposits. Comment. [3(ix)]

1. **Clause 3(ix) of CARO** requires the Auditor to report on whether or not Term Loans are applied for the purpose for which such Loans were obtained.
 2. During the construction phase, Companies, generally, temporarily invest the surplus funds to reduce the cost of capital or for other business reasons. However, subsequently the same are utilized for the stated objectives.
 3. In such cases, the Auditor should mention the fact that pending utilization of the Term Loan for the stated purpose, the funds were temporarily used for the purpose other than for which the loan was sanctioned but were ultimately utilized for the stated end–use.

50. During the course of production, a Company accumulates huge quantity of Scraps and certain By-Products. The Scraps are sold by auction and for the sale of By-Products, reasonable records are maintained, but no records are maintained for recording the generation of Scraps and By-Products and accordingly not being satisfied with the state of affairs, you want to qualify your report. But Management views that under CARO, the Auditor is not required to report about maintenance of records in connection with generation of Scraps and By-Products. Comment on the view of the Management.

1. **CARO Requirements:** The following reporting requirements of CARO are relevant in this regard –
 - (a) **Cost Accounting Records [3(vi)]:** Refer to **Clause 3(vi) of CARO**.
 - (b) **Fraud [3(x)]:** Refer to **Clause 3(x) of CARO**.
2. **Observations:**
 - (a) Since the quantum of Scrap and By-Products is considerable, it appears that maintenance of records for generation as well as records for sale of Scrap/ By-Products is necessary, but the Company has not maintained such records.
 - (b) The Auditor has to evaluate and consider the effect of non-maintenance of records for Scrap & By-Products in the light of – (a) effectiveness of internal control system, (b) compliance with Cost Accounting (Records) Rules, where applicable, & (c) possibility of frauds in relation to such Scrap & By-Products.
 - (c) The Auditor will have to issue an adverse comment on non-maintenance of reasonable records for sale of Scrap/ By-Products and decide on the aspect of records on generation, on the basis of facts and circumstances of the case.

51. Lakshmi, a CA, argues that Clause 3(x) of CARO requires an Auditor to report on the Frauds evidenced in the Company. Hence, indirectly it casts responsibility on the part of the Auditor to find out all the Frauds happened in the Company. However Harini, another CA, rejects the above statement saying that the Auditor is not responsible for finding the frauds in the Company. Comment on the correctness of above statements.

1. **Scope of Audit:** The Clause does **not** require the Auditor to discover the Frauds on the Company and by the Company. The scope of Auditor's inquiry under this Clause is restricted to Frauds '**noticed or reported**' during the year. The use of the words "**noticed or reported**" indicates that the Management should have the knowledge about the Frauds on the Company or by the Company that have occurred during the period covered by the Auditor's Report.
2. **Duties under SA:** However, this Clause does not relieve the Auditor from his responsibility to consider Fraud and Error in an audit of Financial Statements. In other words, irrespective of the Auditor's comments under this Clause, the Auditor is also required to comply with the requirements of SA-240 on "The Auditor's Responsibility to Consider Fraud and Error in an Audit of Financial Statements".
3. **Duties under Companies Act:** Refer to Auditors' Duties on reporting regarding frauds u/s 143(12).

52. As the Statutory Auditor, how would you report on the following under CARO? [3(x)]

ABC Pvt Ltd is a manufacturer of Jewellery. A Senior Employee of the Company informed you that the Company does not disclose the purity of gold used on the Jewellery.

1. If purity of gold is not properly disclosed on the jewellery, it amounts to defrauding of customers by the Company's Management, in order to obtain an illegal advantage. However, this does not create any material mis-statement in the Financial Statements, and hence the Auditor is not concerned with the same.
2. Purity of Gold may have an impact on valuation of inventory, but the Auditor is not required to comment and report on the valuation of inventory under CARO.
3. As long as the books of account are not falsified arising out of the difference in the purity of gold, i.e. actual cost of gold and sale price thereof, there is no implication for mis-statement in the Financial Statements. In such cases, the Auditor need not report on non-disclosure of purity of gold on the jewellery.

53. The Auditor's reporting considerations under CARO may involve adverse comments also. Would these Adverse Comments necessarily call for a Qualified Audit Report?

There is a need for consistency between CARO Remarks and Main Audit Report. Comment.

1. **Consistency:** It is normally expected that CARO Report and the Main Audit Report should go hand in hand. If any of the comments in CARO are adverse, the Auditor should consider whether his comments have a bearing on the True and Fair view presented by the Financial Statements and, therefore, might warrant a modification in the report u/s 143(2), (3), (4).

2. **Adverse CARO Comment vs Qualified Audit Report:** Every adverse comment under CARO need **not** necessarily result in a Qualified Audit Report. This is due to the following reasons –
- Irrelevant to True and Fair:** The adverse comment may arise regarding a matter which has no relevance to the true and fair view of the accounts, e.g. delayed payment of PF / ESI dues to the statutory authorities.
 - Immaterial:** The non-compliance may be material enough to warrant an adverse comment under CARO, but not material enough to vitiate a true and fair view of the accounts.
 - Remediable:** The non-compliance under CARO may be in an area which calls for remedial action from the Management, e.g. lack of internal control in a certain minor operational area, which does not affect the truth and fairness of Financial Statements.

The Auditor must use his discretion based on facts and circumstances of each case, in deciding whether the adverse comment under CARO should result in an adverse audit opinion.

3. **Mandatory Phrases:**

- Many of the requirements in CARO will involve Expression of Opinion and not necessarily Statement of Facts. Hence it is necessary to prefix such Statements by the words "In our opinion" or "In terms of the information and explanations given to us and the books and records examined by us in the normal course of audit and to the best of our knowledge and belief, we state that....."
- Even when there are no Adverse Comments under CARO, it may be advisable for the Auditor to preface his report u/s 143 (2), (3) & (4) with the words: "Further to our comments in the Annexure, we state that....."

4. **Sequence of Items in Audit Report:** The following is the sequence of preparing an Audit Report:

- First**, the comments, if any, u/s 143(1) shall be given,
- Second**, the comments under CARO,
- Thirdly**, the Report u/s 143(2), (3), (4).

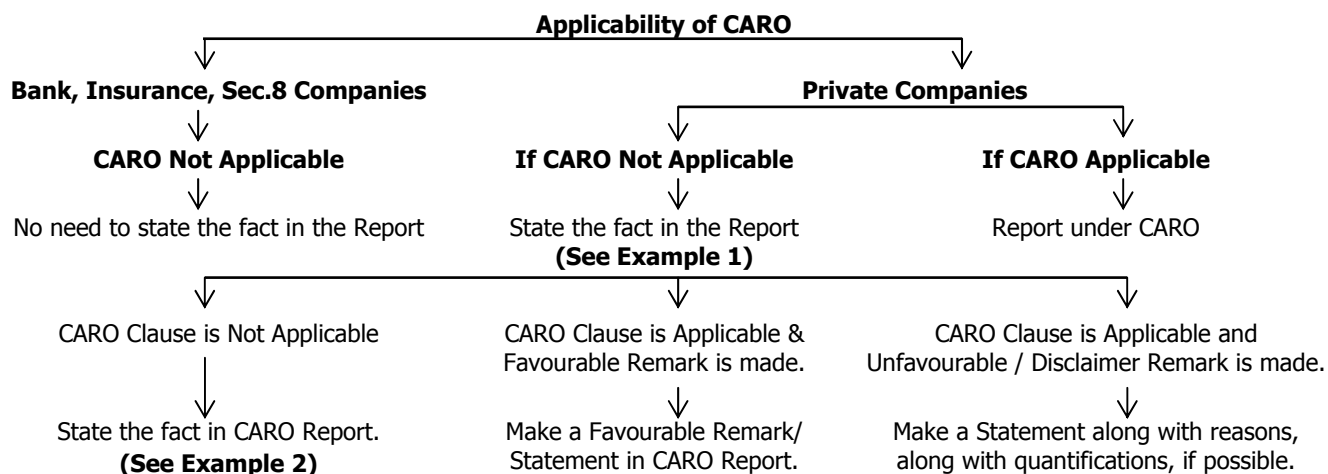
Note:

- Annexure:** The comments under CARO may, alternatively, be given in the form of an Annexure to the Report. However, when the comments are given in an Annexure, it is necessary to refer to the Annexure in the Main Report and it is advisable to sign the Annexure in addition to signing the Main Report.
- Order of Qualification:** Where there is a Qualification both u/s 143(1) and in CARO, it is suggested that the Qualification u/s 143(1) shall precede the Qualification under CARO.

54. Is the Board of Directors required to disclose their explanations in Director's Report on the Auditor's comments and remarks under CARO?

- Responsibilities of BOD:** Sec.134 requires that the Board shall be bound to give in its Report, the fullest information & explanations regarding every reservation, qualification or adverse remark contained in the Auditor's Report. In this regard, Audit Report includes CARO and hence the Board's responsibility is extended to this.
- Consensus-ad-idem:** The Auditor's comments in CARO may be in respect of Matters of Fact or they may be an Expression of Opinion. It is necessary that there should be no inconsistency in the facts as stated by the Auditor and as explained in the Board's Report. It is, therefore, suggested that wherever possible, a Draft Report should be submitted to the Board to verify and confirm the facts stated therein.
- Difference of opinion:** It is, however, possible that, on the same facts, there may be a genuine difference of opinion between the Auditor and the Board. In such a case, each is entitled to hold his or its view. Therefore, the expression of a different opinion in the Board's Report should not be regarded as any reflection on the Opinion expressed by Auditor.
- Inclusion in Audit Report:** It is not necessary that the Management's Explanation for any matter on which he makes an Adverse Comment be included in the Audit Report. However in the following cases, the same may be included–
 - To make the comment more meaningful and complete.** (e.g. Physical Verification of Inventories, though planned, may not have been carried out because of a Strike or a Lockout. An Adverse Comment without this explanation would be misleading.)
 - To explain the fact** why in spite of an Adverse Comment, the **True and Fair view** of the Financial Statements is **not vitiated** (e.g. Physical Verification of a part of the Inventories at the year-end may not have been carried out, but there is sufficient other evidence produced by the Management which satisfies the Auditor regarding the existence, condition and value of the Inventories).

55. Summarise the reporting requirements in case of CARO Applicability and its Clause Applicability or Non-Applicability.



Example 1 Format: This Report does not include a Statement on the matters specified in Para 3 of CARO, 2016, issued by the Department of Company Affairs, in terms of Sec.143(11) of the Companies Act, 2013, since in our opinion & according to the information and explanations given to us, the said Order is not applicable to the Company.

Example 2 Format: The Central Government has not prescribed maintenance of Cost Records u/s 148(1) of the Companies Act, 2013 for any of the products of the Company.