



# C.V.O. CA'S

## NEWS & VIEWS

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CELEBRATING 50 YEARS OF PROFESSIONAL EXCELLENCE

*From President's Desk...*

**Dear Professional Colleagues and Readers,**

Let me take this as an opportunity to wish all the readers a happy 75<sup>th</sup> Independence day. This year our country celebrated "Azadi Ka Amrut Mahotsav" like never seen before. Many people enjoyed the long weekend with travel plans and many went to see the vibes and enthusiasm at various places locally.

I was wondering, what did we achieve over the last 75 years? We still have poverty, law and order issues, corruption etc. We still rank poor in ease and quality of life, quality of education. But then I read a very nice article on our achievements over past seven decades. I thought I should share a few of them with you all:

- At the time of independence, India's per capita income was merely INR 230 i.e. 2.9 USD. Since then we saw rapid industrialization, successful green – white – blue revolutions. From 2.9 USD, per capita income now has reached to ~2000 USD. This feat is more remarkable considering India was involved in 4 wars and many draughts and famines.
- The best achievement for India, in my view is, we kept ourselves united. India is home to more than 270 mother tongues, countless religion, number of tribes and autonomous regions. Many at the time of our Independence believed that India will not remain a single country and will see partition soon like Europe. India remained united and grew stronger and stronger.
- In 1947 average life expectancy in India was mere 32 years. In those years, almost 20% of the Indian population was suffering from Malaria. Today life expectancy has improved to ~70 years. We had worlds biggest polio vaccination drive and today India is a polio free country. Today, India's polio eradication is a case study of health care success for the world. From where we started in 1947 till now, our achievement seems astonishing. Today we proudly call ourselves worlds pharmacy.
- India's space success does not need any introduction. From first rocket launch in 1963, India now is eyeing missions on Moon, Mars.

There are numerous such achievement in last 75 years, but it barely gets it's due recognition. Our success story might be far from perfect, yet India has delivered and has face all its challenges with strength to strength.

We are also going to celebrate our own holy festival Paryushan. The festival is celebrated as festival of forgiveness. Word Paryushan means; "Pari" which means to recollect yourself and "Vasan' which means at a place; Paryushan stand to know yourself or recollect yourself at a place in your spirit. This is the time for us to make up and clean the dirt, which is in the form of karma collected on our soul. Samayik and Pratikraman provide an opportunity to introspect and to follow the path of Tirthankara.

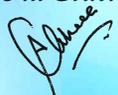
### Events in retrospect:

We held 2-day RRC on GST at Karjat on 5th – 6th August. Committee ensured apt topics for discussion. The presentation paper were an eye-opener.

We also held 2<sup>nd</sup> program on public awareness – financial literacy at Borivali jointly with Borivali KVO Mahajan. The program covered many important aspects such as succession as per the Hindu Succession Act, Joint ownership, HUF and importance of Will etc. The program was very well attended by around 185-190 participants. The program will be available on YouTube very soon.

I wish all the reader, a happy independence day and seek forgiveness. Michami Dukkadam.

*Thank you all..... Always in Gratitude*

  
CA Amit Chheda

September 1, 2022



# AUDIT

Cryptic Cryptos .....	CA Ketan Rambhia (Chairman Comm.).....	3
Challenges and Precautions in Tax Audit Report .....	CA Ami Chheda .....	5
Reporting Requirement Under Tax Audit (Clause 30 to Clause 44).....	CA Mahendra Gala .....	12
Challenges and Precautions While Preparing the Financial Statements for a Company Under Statutory Audit .....	CA Neel Shah..... CA Devangi Patel	31
Challenges and Precaution in Preparation of Statutory Audit Report While Dealing with Loans/Borrowings Under Companies Act 2013 and Under CARO 2020 .....	CA Mitesh Chheda.....	46
Events in Retrospect .....		51-52

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## CRYPTIC CRYPTOS



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### FROM THE DESK OF CHAIRMAN

In recent times, digital currency i.e. crypto currency has seen a lot of investment interest by people all over the world and gaining much popularity in younger generation. Naturally being technology driven, the so called currency is becoming more and more acceptable by young generation and increase in valuation in crypto currency has drawn much attention of investing fraternity.

History of crypto currency dates back to 1983, and then evolved into modern day virtual currency in later part of first decade of this Century. In fact the word "cryptocurrency" was added to the Merriam-Webster Dictionary as late as in March 2018. According to Jan Lansky (Ph.D. - working at the Department of Computer Science and Mathematics, The University of Finance and Administration - doing research in Cryptocurrencies, Databases, and Software Engineering), a cryptocurrency is a system which meets six conditions, i.e., (1) The system does not require a central authority; its state is maintained through distributed consensus (2) The system keeps an overview of cryptocurrency units and their ownership (3) The system defines whether new cryptocurrency units can be created. If new cryptocurrency units can be created, the system defines the circumstances of their origin and how to determine the ownership of these new units (4) Ownership of cryptocurrency units can be proved exclusively cryptographically (5) The system allows transactions to be performed in which ownership of the cryptographic units is changed. A transaction statement can only be issued by an entity proving the current ownership of these units (6) If two different instructions for changing the ownership of the same cryptographic units are simultaneously entered, the system performs at most one of them.

Having no physical existence and being technology driven, it is not very easy to understand how the crypto currency is generated, traded, kept, transacted, determination of value, even its technology architecture for layman or public at large. Interest it has drawn is mainly due to people considering it as an alternate investment opportunity. Interestingly, there are as many as 9000 different Cryptocurrencies presently available.

In simple terms, as we all understand, the cryptocurrency which is virtual and has no physical existence, largely it is not regulated, it is not recognized as official currency or legal tender by government authorities, it is difficult to trace, being virtual easy to store and provides privacy yet vulnerable to frauds.

The very fact that cryptocurrency cannot be regulated easily due to its inherent nature, governments world over are perplexed how to deal with it. Surely such currencies cannot be allowed to be parallel economies or it can ruin the economic system of any country, at least that is the fear and not without reason. The main reasons being secrecy behind dealings in cryptocurrency, no physical existence makes it really difficult to regulate it. Countries have though started introducing and increasing regulations in the dealings of cryptocurrency, yet a lot needs to be done in this direction. E.g. at present, India neither prohibits nor

allows investment in the cryptocurrency. In 2020, the Supreme Court of India had lifted the ban on cryptocurrency, which was imposed by the Reserve Bank of India. Since then the investment in cryptocurrency is considered legitimate in India though there is still ambiguity. Also India amended its tax laws to levy taxation of gains in transactions of crypto currency. However, taxability of any income or transaction does not automatically make the dealings legitimate. It is expected that the Indian Government will soon introduce specific law to either ban or regulate the cryptocurrency in India. But in absence any such law, people are increasingly investing or trading in cryptocurrency. On the other hand, China has completely banned and the Chinese government declared all cryptocurrency transactions of any kind illegal. Interestingly, however, China's central bank has been working on introducing an official digital currency of its own and, in September 2021, announced that it had completed pilot tests of its e-CNY digital currency in several cities. The e-CNY token has been developed to replace cash and coins and will be accepted as payment for goods, bills, transport fares, and tolls. In the USA, the cryptocurrency exchanges are legal and fall under regulatory scope of Bank Secrecy Act. Meanwhile, the US Securities and Exchange Commission (SEC) has indicated that it considers Cryptocurrencies to be securities, and applies securities laws comprehensively to digital wallets and exchanges. Cryptocurrencies are not legal tender in Canada but can be used to buy goods and services online or in stores that accept them. Canada has been fairly proactive in its treatment of Cryptocurrencies, primarily regulating them under provincial securities laws. Canada brought entities dealing in virtual currencies under the Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTFA) as early as 2014. Even in Singapore, Australia, Japan, South Korea, UK, etc. dealings in Cryptocurrencies are legal and regulated. But almost in all countries, cryptocurrency is not legal tender, with notable exceptions being El-Savador and The Central African Republic which have adopted Bit coin as legal tender. However, regulations in all the countries are evolving and there are going to be changes in regulatory aspects in the times to come.

One cannot deny the very nature of cryptos and dealing in the same being mysterious, uncertain, hard to understand and ambiguous. It goes without saying that dealing in any such virtual asset is highly risky when the same is largely unregulated or under-regulated. The opportunities cryptocurrency provides are largely clouded by inherent threats it has such as secrecy in its dealings leads to thefts, frauds and loss, volatility in its valuation is very high, cross border virtual transactions make it difficult to govern and trace in case of frauds, money laundering issues connected with its dealings are very high [according to block chain data company Chainalysis, criminals laundered US\$8,600,000,000 worth of cryptocurrency in 2021, up by 30% from the previous year], cybercrimes connected with it, speculative nature of the dealings and so on. All these aspects make it necessary to show restraint or show utmost care in dealings in cryptocurrency.

At the outset, on this pious occasion of Paryushan Mahaparva, I seek forgiveness from all of you with folded hands...

*Thank you all.... Always in Gratitude*

*CA Ketan Rambhia*



# CHALLENGES AND PRECAUTIONS IN TAX AUDIT REPORT



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## Introduction

The month full of tax audit reports and dealing with the challenges thereon! Many of the assesses receive intimations from tax department for the mismatches in the tax audit report and the income tax return filing, however when one looks into the matter it is quoted as ironical that the mismatch is only due to the lack of the transparency of the clauses between return and the tax audit report.

An auditor has to consider the following when carrying out the assignment of Tax Audit:

- Directions issued by Council including those relating to ethical requirements in regard to communication with previous auditor, limits for tax audit etc.
- Accounting Standards prescribed by ICAI (and notified standards under section 133 of the Companies Act 2013 in the case of Companies)
- Guidance Notes (G.N.) issued by ICAI

An attempt is made to discuss the challenges prevailing in tax audit report and the precautions to be taken thereon.

### **1. Use of Form 3CA or 3CB**

3CA – A taxpayer having business or profession and mandated to get his accounts audited under any other law (other than income tax)

Eg. Companies audited under Companies Act, 2013; LLPs audited under LLP Act, 2008

3CB - A taxpayer having business or profession and NOT required to get his accounts audited under any other law (other than income tax)

Eg. A proprietorship entity or partnership firm, having a turnover > 1 crore and not opting for presumptive income scheme, is not required to get its accounts audited under any other law except income tax. So, it will furnish Form 3CB.

### **2. Computation of total turnover for tax audit purpose**

- A. Where a person is carrying on 2 Business/2 Professions – the total turnover of both the businesses shall be clubbed together and tax audit shall be liable to be conducted if the Total Turnover exceeds Rs. 1 or 10 Crores / Rs. 50 Lakhs as the case may be.
- B. Where a person is carrying on business as well as profession and the Turnover of the business is Rs. 12 Crore and the Gross Receipts of the profession is Rs.48 Lakhs. In such a case, ICAI has clarified through a Guidance Note that the Assessee is liable to get the Tax Audit done of both the business as well as profession because the Gross Receipts from the business exceed the limit of Rs. 10 Crore. However, if his Total Turnover was Rs. 9 Crores and Gross Receipts from Profession was Rs. 48 Lakhs, he would not be required to get his Tax Audit done.

- C. In case where a person has a total turnover of Rs. 9.8 Crores and has received Rs. 80 Lakhs as remuneration from a partnership firm - In such a case, the total amount on adding up becomes Rs. 10.60Crores i.e. above Rs. 10 Crores. Confusion arose whether the person is liable to get an audit done in this case and ICAI in its Revised Guidance Note dated 14.08.2022 has clarified that the turnover will not include any amount of Interest, remuneration received by Partner from partnership firm in calculating total gross receipts in business for purpose of Sec 44AB.
- D. A person having a normal business and presumptive business-In such a case person needs to exclude the turnover of presumptive scheme from the total turnover in order to verify the normal business turnover. If in any case, the turnover limit for purpose of tax audit exceeds Rs. 10 crores / Rs. 2 crores, as the case may be, then the tax audit shall be liable to the assessee.

### 3. **CLAUSE 1, 2: Name of the Assessee, Address of the Assessee**

In case there is a change in the name / address of the Assessee between the last day of previous year and the date of tax audit report, both the names / addresses (old and new) shall be mentioned in the report.

A professional is obliged to provide / disclose all the details as on the date of tax audit report.

### 4. **CLAUSE 8: Reporting of the section under which the audit is being conducted**

#### Case 1:

Taxpayer = Individual with only business income

Turnover = 1.5 crore

Profit = Lower rate @ 1.5%

Not opted for presumptive scheme in past

Many professionals select Sec 44AB(e) as applicable in such a case.

Sec 44AB states

*“Every Person –*

*.....*

*(e) carrying on the business shall, if the provisions of sub-section (4) of section 44AD are applicable in his case and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year,”*

Sec 44AD(4) states

*Where an eligible assessee declares profit for any previous year in accordance with the provisions of this section and he declares profit for any of the five assessment years relevant to the previous year succeeding such previous year not in accordance with the provisions of sub-section (1), he shall not be eligible to claim the benefit of the provisions of this section for five assessment years subsequent to the assessment year relevant to the previous year in which the profit has not been declared in accordance with the provisions of sub-section (1).*

As per section 44AB(e), the conditions mentioned in the section 44AD(4) is to be satisfied and the income shall be greater than the maximum amount not chargeable to tax.

Here, the conditions mentioned in the sub-section 4 of the section 44AD is not satisfied since the taxpayer hasn't opted the presumptive scheme in past and hence the audit shall not be conducted under the section 44AB(e) instead shall be conducted under section 44AB(a).

Case 2:

Taxpayer = Individual with only business income  
 Turnover = 4 crore with 6% of cash payments  
 Profit = lower rate @ 5%  
 Taxpayer opts out of the presumptive scheme in 3<sup>rd</sup> year

Here, the taxpayer is eligible for tax audit by more than one section. Which section is to be selected for the purpose of Clause 8?

Eg. Sec 44AB(a) and 44AB(e)

Since the turnover of the Assessee is more than Rs. 1 crore but less than Rs. 10 crore and has more than 5% of cash receipts of the total receipts, taxpayer is liable to tax audit as per the proviso to Sec 44AB(a).

Also, the taxpayer withdraws from presumptive scheme in the 3<sup>rd</sup> year of the previous year in which he opted into the scheme. As per the conditions held in sec 44AD(4) and total income being more than the threshold limit, the taxpayer is liable to tax audit under sec 44AB(e).

In my view, Section 44AB(c) to 44AB(e) are specific provisions. If the Assessee does not fall under the purview of the same, he shall be liable to tax audit as per the provisions of Sec 44AB(a) or (b) after meeting the conditions of applicability.

#### **5. CLAUSE 8a – Opting for taxation u/s 115BA/115BAA/115BAB/115BAC/115BAD**

The said clause requires reporting of the Section under which the assessee has opted the taxation, if any. If the assessee has not chosen any of the new tax regime as the case may be, then the same needs to be mentioned accordingly.

Here, the tax audit report shall be uploaded before the income tax return which has its due date lying in the subsequent month. There are chances of change in the stand taken by the assessee while opting for tax regimes.

Given a case, at the time of filing tax audit report, the assessee opts for the new tax regime u/s 115BAA. Thereafter, while filing the income tax return, the Assessee changes its view and does not opt for the new tax regime instead remains in the old tax regime. There are intimations flowing from the department for the mismatch in the tax calculation due to change in the tax regimes opted. In such a case, the tax auditor shall get a written representation from the assessee clarifying its view as on the date of the tax audit report in order to avoid any miscommunications thereon.

Alternatively, revising the tax audit report by the tax auditor shall invite doubts and notices from the department and also affect the normal practice of the professional. It is advisable to avoid revision in such a case.

#### **6. CLAUSE 9(a) – Names of partners/members of firm or association of persons and their profit-sharing ratios**

If a partner is a partner in representative capacity, then name of the beneficial partner should also be indicated.

Since the Profit sharing ratio also includes loss sharing ratio, and if loss sharing ratio is different from the profit sharing ratio – both should be mentioned

## **7. CLAUSE 9(b) - Change in partners/ members of firm/ AOP**

An AOP covers a society or a trust, etc. Usually there are various AOPs where the share of the members is indeterminate.

In such a case, the same shall be disclaimed in the para 3 (Form 3CA) or para 5 (Form 3CB) of the report.

## **8. CLAUSE 11 - Address at which Books of Accounts are maintained**

Under clause 11 the Taxpayer is required to mention the address under which the books of the accounts are kept.

It is highly advisable not to mention the residential address of the taxpayer as section 132 of the act states that the Authorised Officer can enter any building or the place where the books of the accounts are kept in case any search and survey is being conducted pursuant to the section 132 and the section 133A.

## **9. CLAUSE 12 - Whether P & L a/c includes profits assessable on presumptive basis?**

Reporting is for amounts included in P & L a/c. If 2 or more business exist and presumptive section is applicable for some businesses, allocation of expenses may become necessary if common books are maintained.

In this case, it is duty of the auditor to confirm whether any of the businesses fall under this category, to confirm and verify whether common or separate books is maintained for such businesses.

If amount included in P & L a/c does not match the amount assessable under the presumptive section, note may be added to that effect.

## **10. CLAUSE 14 - Reporting of the valuation of the closing stock**

Sub Clause (a) of clause 14 requires for the reporting of the closing stock valuation which includes the finished goods and raw materials valuation as per the section 145A. It mandates that the valuation should be done as per the cost or the net realisable value whichever is lower.

Sub Clause (b) states that if there is any deviation from the prescribed method then its effect on the profit and loss should be evaluated.

Method employed for valuation of closing stock shall be ascertained with reference made to the Annual Financial Statements (SAP) or a management representation may be obtained after duly satisfying himself regarding the method of valuation of closing stock.

The issue for the consideration is that as per the **AS 2**, the raw materials should be evaluated at the cost except in the circumstances as prescribed, but section 145A r.w. ICDS mandates that the stock which includes the raw materials should be evaluated as per the methodology stated above.

In my view, if the value of the raw materials is below its cost, then its effect on the profit and loss should be reported and if the same cannot be evaluated then it is advisable to qualify our report in the para 3 (Form 3CA) or para 5 (Form 3CB) of the report.

## 11. CLAUSE 16 – Amounts not credited to the profit and loss account

This clause is the most recently triggered clause in every intimations received by the Assessee. The wordings of the above clause 16(d) are – “16. Amounts not credited to the profit and loss account, being – (d) any other item of income”. The income reported in the above clause are mainly (i) salary / remuneration from other concerns (ii) rental income (iii) remuneration / interest / profit share from partnership firm etc. (vi) other interest etc. other source income (v) agricultural income (vi) other exempt income etc. The above list is only illustrative list.

The above incomes are mainly those incomes which are not related to the business (of whose accounts are being audited) but have been recorded in the books of account of the business under audit. Since they are not related to the above business they are not credited to the profit and loss account but are credited directly to the capital account.

Eg. If the auditor has reported 'remuneration from partnership firm' at clause no. 16(d) of Form no. 3CD, and also mentioned in Point no. 24(a) in Schedule BP. However, nothing has been mentioned at point no. 5(d) of Schedule Part A : OI Other Information since the same shall be taxed under the head 'Income from Business or Profession'.

Income Tax department started issuing notices as below:

Particulars: There is inconsistency in amount mentioned in return at Sl. No. 5(d) of Part A OI 'Any other item of income' and Tax Audit report

Rs. xxxx Amount mentioned in Form Annexure 3CD (b)	Rs. 0 Amount mentioned in Income tax return (a)	Rs. xxxx Variance (b)-(a)
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Departments are adding the said income again under point 23 of Schedule BP – 'Any Other item or items of addition under section 28 to 44DA' leading to double income being taxed.

Many professionals are revising the tax audit by removing the disclosure done in Clause 16(d) of Form 3CD. This is not advisable since the said disclosure is not incorrect to be revised. If such documents are revised casually and in large nos. then it may lose its reliability in the eyes of the government, authorities and ordinary public. So, its frequent and casual revision should be avoided.

In present condition, the initial step to be taken by the auditors is to file rectification u/s 154 of the Act. Since the said issue shall still prevail as long as IT Dept update their systems for better clarity, the taxpayer shall file appeal against the intimation notice received u/s 143(1) or 143(1a).

## 12. CLAUSE18 – Depreciation

The purchase dates and the put to use dates of the assets shall not necessarily be the same. It is deemed to verify the working condition of the assets and whether it is put to use in the current year. Many of the professionals rely on the dates given by the management as purchase dates being the assets put to use. Since the same may be materially affecting the depreciation calculated on the same, it is advisable to take a certification done by the management with regards to the dates of the assets put to use.

Additionally, the auditor is required to check if payment for the acquisition of any asset is in violation of the proviso to section 43(1), the expenditure should be excluded from the actual cost.

**13. CLAUSE 19 - Amounts admissible under various sections**

Here there are 2 separate columns specifying the details of amounts debited to profit and loss a/c and amount admissible as per the provisions of the IT Act, 1961.

An Auditor should indicate the amount debited to the Profit & Loss Account and the amount actually admissible in accordance with the said sections. Also, amounts not debited to Profit & Loss Account but admissible under any sections mentioned in the clause have to be stated.

Various provisions of sections require fulfilment of prescribed conditions based on which the amount is admissible as per IT Act. While reporting, the auditor should verify the documents and records in support of the various payments/contributions made and deductions claimed and also conditions of allowability of various deductions.

If a separate audit report has been obtained, a reference to that report is to be made.

However, if condition under relevant sections is not fulfilled then they are treated as deemed profits & gains of business and are taxable in certain cases and the same should be reported under clause 24 of Form 3CD.

Generally, the amount covered by these sections is debited to P&L, but in certain sections, a deduction is based on capital expenditure, these are treated as an asset and thus not debited to profit and loss accounts. In such a case auditor should ensure it is stated either Nil/NA under the second column of the table in which amount admissible is to be mentioned.

**14. CLAUSE 23 - Payments made to persons specified u/s 40A(2)(b)**

Tax Auditor has to report payments made by the Assessee to their Related Parties. It may be noticed that relationships/parties covered under AS-18 are not identical.

After scrutinizing all the payments made to the related parties, tax auditor is required to report / disclose all the payments made irrespective of the fact whether the same is reasonable in the eye of law. The Tax Auditor is not required to comment on the reasonableness or otherwise of such payments. The same is dealt with by the Assessing Officer and questioned accordingly.

In case of voluminous transactions, grouping the similar transaction based on their nature and disclosure of such consolidated information as per their nature individual party wise may be considered.

**15. CLAUSE 26 - Certain deductions to be only on actual payment**

Where taxes, duties, etc. referred to in Sec 43B are paid after tax audit reporting date but before the due date of filing return (or actual date of filing return), there is a mismatch in the allowability of the taxes paid within the return filing date.

In this case, the tax auditor is liable to opine on the allowability on the taxes, duties paid as on tax audit reporting date.

Sec 43B states that:

*Notwithstanding anything contained in any other provision of this Act, a deduction otherwise allowable under this Act in respect of –*

- (a) *any sum payable by the assessee by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force, or*

.....

*shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him) only in computing the income referred to in section 28 of that previous year in which such sum is actually paid by him:*

*Provided that nothing contained in this section shall apply in relation to any sum which is **actually paid** by the assessee **on or before the due date applicable** in his case for furnishing the return of income **under sub-section (1) of section 139** in respect of the previous year in which the liability to pay such sum was incurred as aforesaid and the evidence of such payment is furnished by the assessee along with such return.*

Hence, if the taxes are paid after the date of tax audit report and within the return filing due date, the same is practically allowed u/s 43B leading to a mismatch in the reporting done by the tax auditor. Thereafter, the bunch of intimations for such mismatches are received by the Assessee.

Practically, sometimes, the systems in the department do not work logically and hence it is advisable to take a consistent stand in both the reporting and the return filings in order to avoid a series of rectification and replies against the intimations received. If the taxes or duties, etc are unpaid up till the date tax audit report, then the same shall be disallowed in the returns to be filed on a later date. However, the same can be allowed in the subsequent year of payment.

Alternatively, the original tax audit report filed can be revised on a later date but within the return filing due date, once the tax payable is paid by the assessee. The same is not allowed as per the Income Tax laws but the same is practically allowed on the Income Tax Portal.

There can be individual views taken on the same.

#### **16. CLAUSE 27 - Details of CENVAT credits availed and utilised and its treatment in P&L A/c**

The requirement of the clause is to factually report about the amount of CENVAT credits availed of or utilized during the year as well as its treatment in profit and loss account and treatment of outstanding CENVAT credits in the accounts.

The revised Guidance note on Tax Audit dated 14.08.2022 still states about reporting of CENVAT and not the Input Tax Credit (ITC) of GST. There is an ambiguity in the applicability of the said clause for the reporting requirement of ITC of GST.

However, the income tax schema of Tax Audit Report specifies the words ITC under the said clause.

Many professionals take a view of not reporting the ITC of GST availed and utilised under the said clause whereas some practitioners declare the same under this clause.

According to the schema available on the Income tax portal, it is advisable to report the Input Tax Credit of GST and also disclaim our report in the para 3 (Form 3CA) or para 5 (Form 3CB) of the report.

#### **17. CLAUSE 28 - Purchase of shares of company for inadequate consideration**

This clause shall also attract Standards on Auditing – 620 “Using the work of an Auditor's expert” incase a valuation report is obtained to determine the FMV of the shares in case of unquoted instruments.

When the shares are issued for no consideration, then the Tax Auditor can verify the same by share certificates, demat account statements etc. as the same will not be reflected in the books of accounts.

### **Conclusion**

The above issues are inclusive list of the challenges faced by the tax auditor while filing the tax audit report. It is important to take precautions while giving opinion in the report, hence I have tried to list down few in the respective clauses. The readers may note that proper disclosures and disclaimers are mandatory as a measure of precautions from the prevailing challenges.



## REPORTING REQUIREMENT UNDER TAX AUDIT (CLAUSE 30 TO CLAUSE 44)



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### INTRODUCTION

The reporting requirement under tax audit can be traced back to Finance Bill 1984, which is as old as more than 3 decades. The reporting requirement during its age has been amendment time and again with minimum reporting requirement of 13 Clauses in initial days to now at 44 Clauses in Form 3CD that to, with many sub - clauses there under, with a primary objective to facilitate the administration of tax laws by proper presentation of accounts before the tax authorities.

### SCOPE

The scope of this article ranges from Clause 30 to Clause 44 of Form 3CD. The clauses are discussed in the following paragraphs, considering its importance and looking at the wide range of its applicability.

### CLAUSE - 30 DETAILS OF AMOUNT BORROWED OR REPAID ON HUNDI AND INTEREST THEREON [SEC. 69D]

- This clause requires auditor to report on the amount borrowed or repaid on hundi loans otherwise than through account payee cheque. The auditor is also required to report the amount of interest thereon.
- The CBDT has issued Circular No. 208 dated 15.11.1976 and Circular No. 221 dated 06.06.1977 explaining provisions of Sec. 69D vide Appendix XVII.

### CLAUSE - 30A SECONDARY ADJUSTMENT TO TRANSFER PRISING

- This clause does not requires auditor to report secondary adjustment under Sec. 92CE if -
  - (1) The amount of primary adjustment made in any previous year does not exceed Rs. 1Crore; or
  - (2) The primary adjustment is made in respect of an assessment year commencing on or before the 1st day of April, 2016.

Note: AY 2017-18 onwards, to ascertain applicability of these conditions, both the above conditions should be satisfied.

- In case there is secondary adjustment, the auditor is further required to report under which of the following clauses of Sec. 92CE(1) such adjustment relates to -
  - (1) Primary adjustment to transfer price has been made suo motu by the assessee or
  - (2) Primary adjustment to transfer price has been made by the Assessing Officer or
  - (3) Primary adjustment to transfer price has been made due to Advance Pricing Agreement (APA) entered into by the assessee under Sec. 92CC (on or after the 1st day of April, 2017) or

- (4) Primary adjustment to transfer price has been made as per Safe Harbour Rules framed under Sec. 92CB or
- (5) Primary adjustment to transfer price has been made as a result of resolution of an assessment by way of the Mutual Agreement Procedure (MAP) under an agreement entered into under Sec. 90 or Sec. 90A for avoidance of double taxation.

*However, it may be noted that the primary adjustments for earlier years prior to AY 2017-18, or primary adjustments totaling less than Rs. 1 Crore for a previous year, which do not warrant a secondary adjustment, should also be reported under clause 30A(a).*

- The auditor is required to report the amount of primary adjustment made under any of the above referred clauses and whether the excess money available with the associated enterprise, if any, is repatriated to India as per Sec. 92CE (2) and within prescribe time of ninety days (Rule 10CB).
- It is pertinent to note that, if the said amount is not repatriated within the prescribed time, it shall be deemed as an advance to the associated enterprise and the auditor is also required to report the amount of interest as computed as per Rule 10CB.

**CLAUSE- 30B DISALLOWANCE OF INTEREST OR OF SIMILAR NATURE EXCEEDING RS. 1 CRORE AS PER SEC. 94B**

- The auditor is required to report, if the assessee has incurred any disallowance on account of any interest expenditure or similar expenditure over and above Rs. 1 Core, as provided under Sec. 94B.
- Expenditure of similar nature should be read in the context of 'debt' as defined in Sec. 94B(5)(ii).
- Further, interest and expenditure of similar nature which is deductible while computing income under the head 'Profits and Gains of Business or Profession' should be considered, and not interest deductible under any other head of income or interest which is otherwise not deductible.
- In such consideration, there are two views as to whether it is the aggregate of all interest paid or payable to all Non-Resident AEs which is to be considered for the limit of Rs. 1 crore, or whether interest paid or payable to each Non-Resident AE is to be examined vis-a-vis the limit of Rs. 1 crore. Based on the view taken by the assessee, appropriate disclosure should be made in Form No 3CD.
- The following details need to be reported under this clause –
  - (1) Amount of Interest expenditure or similar expenditure
  - (2) Amount of EDITDA (Earnings before interest, tax, depreciation and amortization)
  - (3) Amount of interest expenditure or similar expenditure in excess of 30% of EDITDA
  - (4) Details of interest expenditure or similar expenditure brought forwarded as per Sec. 94B(4)
  - (5) Details of interest expenditure or similar expenditure carried forwarded as per Sec. 94B(4) for eight assessment years immediately succeeding the assessment year for which the excess interest expenditure was first computed.

**CLAUSE-30C REPORTING OF GENERAL ANTI AVOIDANCE RULES (GAAR)**

- The provisions of General Anti -Avoidance Rule (GAAR) are contained in Chapter X-A comprising of Sec. 95 to Sec. 102 and the procedural provisions relating to mechanism for invocation of GAAR and passing of the assessment order in consequence thereof are contained in Sec. 144BA. Rules 10U to 10UF have been prescribed by the Central Government in respect of GAAR. The Board has issued certain clarifications on queries about implementation of GAAR vide Circular No. 7 of 2017 dated 27.01.2017
- It may be noted that, the provisions are complex and before an arrangement can be considered to be an Impermissible Avoidance Agreement (IAA), one of the main purpose is to obtain 'tax benefit' as defined u/s.102 (as explained here below) AND the condition as specified u/s. 96 have to be satisfied, which are....
  - Arrangement creates rights/ obligations which are not ordinarily created between persons dealing at arm's length,
  - Arrangement results, directly or indirectly, in misuse or abuse of the provisions of the Act,
  - Arrangement lacks commercial substance or is deemed to lack commercial substance, by virtue of fiction created by Sec. 97, or
  - Arrangement entered into or is carried out, by means, or in a manner, which are not ordinarily employed for bonafide purposes.

As per Sec. 102(10) 'tax benefit' includes, –

- a reduction or avoidance or deferral of tax or other amount payable under this Act; or
- an increase in a refund of tax or other amount under this Act; or
- a reduction or avoidance or deferral of tax or other amount that would be payable under this Act, as a result of a tax treaty; or
- an increase in a refund of tax or other amount under this Act as a result of a tax treaty; or
- a reduction in total income; or
- an increase in loss,
  - in the relevant previous year or any other previous year;
- The auditor is required to report, if the assessee has entered into an Impermissible Avoidance Arrangement as per Sec. 96 and does not fall within the exclusions as stated in Rule 10U of Chapter X-A. However, in case the transaction is covered by exclusions provided in the Rule, the auditor may put a clarificatory note stating that the reporting requirement does not apply.
- If the assessee falls within the provisions of Sec. 96, the auditor is required to report the Nature of such arrangement along with the amount of tax benefit as per Sec. 102, arising in aggregate, to all the parties to the arrangement.
- It may be noted that the reporting under this clause is applicable when the tax benefit in aggregate to all parties to the agreement exceeds Rs. 3 Crore.

- In case, if any arrangement has been declared to be an IAA in any earlier previous year, the tax auditor should further examine if any transaction in connection with such declared IAA has taken place during the previous year under the audit. In such a case, the tax auditor is expected to report this fact and the tax benefit arising from such transaction to all the parties to the arrangement.
- If due to elaborate investigation process and due to lack of access to the books of account and other records of other parties to the arrangement, the Tax Auditor is unable to come to a conclusion which he can certify any arrangement to be 'True and Correct', he should make an appropriate disclaimer in respect of reporting under this clause in Form 3CA / 3CB.

### **CLAUSE - 31 REPORTING U/S. 269SS, 269ST AND 269T**

Clause 31 requires to provide particular of each loan or deposit taken or accepted for an amount exceeding the limit specified u/s.269SS, repayment of loan or deposit exceeding the limit specified u/s.269T and also requires to provide particulars of each transaction of receipt or payment above the limit specified u/s 269ST, when such transaction is done otherwise than the specified mode of payment.

- This clause requires to include certain specified sum or specified advance related to transfer of an immovable property as specified u/s.269SS and u/s.269ST respectively, irrespective of whether or not the transfer takes place. The said amendment is introduced w.e.f. 19<sup>th</sup> July, 2017.
- This clause further requires to include each receipt or payment of an amount exceeding limit specified of the transactions as specified mentioned u/s.269ST (presently the said limit in aggregate is Rs. 2 lakhs). The said amendment is introduced w.e.f. 20<sup>th</sup> Aug, 2018.
- Section 269ST as it is there on statute is .....

*“No person shall receive an amount of two lakh rupees or more –*

- (a) In aggregate from a person in a day; or*
- (b) In respect of a single transaction; or*
- (c) In respect of transactions relating to one event or occasion from a person,*

*Otherwise than by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account [or through such other electronic mode as may be prescribed];”*

Further, proviso to section specifies certain exclusions, like receipt by Govt, any Banking company, Post Office savings bank or co-operative bank, etc.

- Section 269ST, prohibits receipts of an amount in aggregate of Rs.2 lakhs or more, from a person otherwise than account payee cheque/ draft/ electronic clearing system, in a day, or in respect of single transaction, or transactions relating to one event or occasion.
- Let us understand the terms used u/s.269ST and it's reporting.
  - a. 'In aggregate from a person in a day'* – this will include the different transaction with same person totaling to Rs. 2 lakhs or more in a day, and payment thereof is not in the specified mode. Eg. Sales through different bills to a person totaling to Rs. 2 lakhs or more in a day will be covered, if the receipt of payment is not through specified mode as prescribed u/s.269ST.

**'b. In respect of single transaction'** – this will include a transaction of Rs. 2 lakhs or more even when the receipts of such transaction is in different days and may be less than Rs 2 lakhs on each such day,

**'c. In respect of transaction relating to one event or occasion from a person'** – this will cover when payment is received of Rs. 2 lakhs or more from same person in cash, (a) in respect of a single event or (b) for different type of product or services for the same occasion.

The above mentions transactions need to be reported under this clause.

- Now, let us understand the reporting requirement under following different typical situations.

a) Whether the transaction by 'journal entries' are covered for reporting under section 269ST?

In my view, auditor needs to give suitable note on such transaction of journal entries and need not necessarily to be reported, as such journal entries are neither receipt nor payment u/s.269ST.

b) Cash brought in by a partner as capital contribution of an amount of Rs.2 lakhs or more to be reported u/s.269ST?

In my view, going by literal interpretation of the section 269ST, the said transaction will have to be reported, as the section requires to include every receipt irrespective of its nature or relationship between the parties.

c) Whether 269ST applies to revenue transaction or capital transaction?

In my view, in the absence of any clarification both of above type of transaction, whether revenue or capital, needs to be reported under this clause.

- Circular No. 22 dated 3<sup>rd</sup> July, 2017 gives relaxation to NBFCs and Housing Finance Companies, whereby it is clarified by CBDT that the receipt of each installment by such companies be considered as separate transaction instead of aggregating the same for the year for the purpose of calculating the limit specified u/s.269ST.

### **CLAUSE-32 DETAILS OF BROUGHT FORWARD LOSS OR DEPRECIATION ALLOWANCE**

- Format of Reporting is as follows:

Sr. No.	Assessment year	Nature of loss/ allowance (in rupees)	Amount as returned* (in rupees)	All losses/ allowances not allowed under section 115BAA/ 115BAC/ 115BAD	Amount as adjusted by withdrawal of additional depreciation on account of opting for taxation under section 115BAC/x115BAD <sup>^</sup>	Amount as assessed (give reference to relevant order)	Remarks
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)

- Points to remember.....
  - ❖ As per Finance Act, 2021 by amendment u/s. 32(1)(ii), depreciation on goodwill is not allowable w.e.f. 01-04-2021 and therefore auditor needs to verify that no provision for depreciation on goodwill is made for F.Y. 2020-21 onwards.
  - ❖ A question arises as to which loss is to be taken while reporting under this clause? Whether the loss as per books of accounts or assessed, and when there is no appeal pending?
    - It is needless to say that loss as per books of accounts will be reported till it is been assessed, with suitable remark by an auditor. However, once it is assessed, then to follow the loss as assessed. Also, in case when there is appeal pending against assessed loss, a suitable note in the remark column should be given by the auditor and in case when loss is disallowed and no appeal is pending, the said loss will not be carried forward.
  - ❖ As per Sec. 80 for the purpose of carry forward and set off of losses specified u/s. 139(3), those loss returns necessarily be filed within the time prescribed u/s. 139(1).
  - ❖ It may be noted that Section 78 prescribes certain restrictions regarding carry forward and set off of losses in case of change in constitution of firm or on succession.
- This clause further requires reporting of brought forward losses or depreciation allowance vis-a-vis change in shareholding of the company and impact on carry forward and set off of losses w.r.to Sec.79.
- The provision of Sec.79 was introduced to check misuse of covering of losses in a company to reduce the incoming shareholders tax liability. Companies affected by Sec. 79(1) are not allowed to carry forward past years losses to future years.

However, it is important to note that expression not less than 51% of voting power used in section 79 indicates that in order to invoke provisions of said section, only voting power is relevant and not shareholding pattern. Therefore, change of shareholding between the existing shareholders inter-se does not attract Section 79. [CIT vs. Amco Power Systems Ltd (62 Taxman.com 350)(Kar)].

- It may further be noted that as per proviso to sec. 79(1), in case of eligible start-ups as refer to in Section 80-IAC. The above condition of 51% of voting power is relaxed for first 7 years from the date of incorporation of the company. Also, Sec. 79(2) provides for certain exclusions to the condition of 51% of voting power, as provided u/s. 79(1).

(Sec. 79(2)(e) and (f) are brought in w.e.f. FY 2021-22).

- As per Finance Act 2022, effective from AY-2022-23 (FY-2021-22), Sec.79A is newly inserted which state's that in case of Search u/s.132 or a requisition u/s.132A or a survey u/s.133A, not being u/s. 133A(2A), when there is any undisclosed income in previous year of any assessee due to such search or survey, then no set off of losses would be allowed of any brought forward of losses or any unabsorbed depreciation while computing its total income of such previous year.

- Question may arise, whether in case of carry forward of losses which includes unabsorbed depreciation, the said unabsorbed depreciation will also not be allowed to be carried forward, if there is a change in voting power of shareholders of the company, as stated u/s. 79?
  - Here, it may be noted that the unabsorbed depreciation carried forward by such company is governed by sec. 32(2) and not by sec. 72 as business loss.

Section 79 of the I. T. Act reads as.....

Notwithstanding anything contained in this Chapter.....”

- Further, this clause requires reporting of speculation business loss to be done as per Section.73. It may be noted that speculation losses will be allowed to be set off only against speculation income.
- Now, let us understand the reporting requirement under following different typical situations.
  - a) Whether single transaction of speculation nature will constitute of a “Business” to say it is “Speculative business”?
 

It is really a challenge for the tax auditor to report such a single transaction, considering it as business or not? In my view, it will not constitute a `speculative business' and therefore, one may take a view, not to report the same.
  - b) There are certain exclusions to 'speculative transaction' as defined under proviso to Sec. 43(5). For example, hedging transaction, etc.
 

These transactions do not constitute speculative business and therefore, those are excluded from speculative transactions and should not be reported under this clause.
  - c) Whether same speculation business is must to be continued to set off its loss of earlier years against profit of same speculation business?
 

It is not necessary to continue same speculation business (where loss was incurred) for setting off of brought forward of speculation business loss.

### **CLAUSE - 33 SECTION-WISE DETAILS OF DEDUCTIONS, IF ANY, ADMISSIBLE UNDER CHAPTER VIA OR CHAPTER III (SECTION 10A AND SECTION 10AA)**

- Under this clause, section-wise deduction under chapter VIA and exemption u/s.10A & u/s. 10AA under chapter III is required to be reported.
- The tax audit is to be conducted of business or profession, therefore, deduction or exemption to be reported will be based on books of accounts audited of business or profession (i-e, Qua-business). In case of audit of any branch/ unit the deduction or exemption is to be reported from books of branch/ unit with suitable note thereto, and in case when auditor is to issue report regarding tax audit of head office, then the auditor will have to consolidate all the branches or units reports, as well as to include books of head office while reporting the deduction or exemption.

- In case when deduction or exemption is based on judicial pronouncement, than the said facts should be reported appropriately by the auditor.
- The tax auditor should consider the audit report or certificate issued by self or by any other auditor, u/s.80-IA,80-IB,80-IC,80-JJA, etc. while reporting under this clause.
- It is important to verify clause 8(a) of Form 3CD to check whether taxpayer is claiming benefit u/s.115BA/ 115BAA/ 115BAB/ 115BAC/ 115BAD. In case the benefit is claimed, than it may be noted that taxpayer will not be entitled to claim any deduction under chapter VIA and under chapter III (Sec. 10A & 10AA) except deduction u/s.80M and/or u/s.80JJAA.

### **CLAUSE-34 REPORTING OF TAX DEDUCTED AT SOURCE AND TAX COLLECTED AT SOURCE (TDS AND TCS)**

- Format of Reporting is as follows:

Tax deduction and collection Account Number (TAN)	Section	Nature of payment	Total amount of payment or receipt of the nature specified in column (3)	Total amount on which tax was required to be deducted or collected out of (4)	Total amount on which tax was deducted or collected at specified rate out of (5)	Amount of tax deducted or collected out of (6)	Total amount on which tax was deducted or collected at less than specified rate out of (7)	Amount of tax deducted or collected on (8)	Amount of tax deducted or collected not deposited to the credit of the Central Government out of (6) and (8)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)

- Primary responsibility to provide details in form 3CD is of the taxpayer, an auditor has to verify the same and give their opinion on the same. In case of voluminous transactions the Auditor can apply test checks with appropriate remark.
- While reporting under this clause, auditor has to verify not only the expenses debited to P&L account and TDS/ TCS returns filed by the taxpayer, but also advance payment made in certain circumstances (as TDS/ TCS liability arises on accrual or payment basis, whichever is earlier) and therefore auditor is to verify advances given by the taxpayer, while reporting under this clause.
- In case of non-resident, as per Sec. 2(37A), rate of tax deduction will have to be read with DTAA (Double Taxation Avoidance Agreement).
- Auditor will have to take into account Lower TDS Certificate issued U/s. 197 while reporting as this will be useful to report the specified rate of tax deduction applicable.
- In case lesser deduction the same is to be reported under column 8 of the table and TDS deducted but not paid is to be reported in Column 10 of the table, as given in this clause. However, TDS deducted but deposited late to the Government, will not be reported under this clause.

- It may be noted that U/s. 194Q the transactions of purchase of goods requires deduction of tax at source w.e.f. 01.07.2021. One may refer CBDT Circular No. 13/2021 dated 30/06/2021, giving guidelines on this subject. At the same time, U/s. 206C (1H) every seller has to collect TCS on receipt of amount as consideration for sale of any goods unless TDS U/s. 194Q is done by the buyer.
- The tax auditor should also consider applicability of higher rate of TDS / TCS under certain circumstances like non furnishing of PAN, non-filers of return as provided in Section 206AA/ 206AB/ 206CC/ 206CCA.
- The details given under this clause should be reconciled with the disallowance reported U/s. 40(a) in Clause 21(b), to the extent possible, to cross match the reporting.
- It may be noted that after the amendment of clause 34(b), now the tax auditor is required to furnish a list of transactions which are not reported in the statement of TDS/ TCS filed, after taking into consideration provisions of the law, notifications, circulars and various judicial pronouncements on the subject. In case of huge volume, reporting may be done of significant deficiencies with appropriate remarks in Form 3CA/ 3CB.
- In case of difference of opinion between taxpayer and auditor, a suitable note in the form of observation is to be given in Form 3CA/ 3CB along with both the views.
- Under clause 34(c), the tax auditor is to report about liability of the assessee to pay interest U/s. 201(1A) or 206C (7).
- Under mercantile system of accounting, if interest is not paid till 31<sup>st</sup> March or no provision is made in this regard and when amount is material, the impact on the 'true and fair view' should be considered.

### **CLAUSE-35 QUANTITATIVE DETAILS OF STOCK**

- This clause requires reporting on quantitative details of 'principal items', in case of the traders, goods traded and in case of manufacturers, the reporting should include details of raw materials, finished products and by-products. Normally, the items having 10% of aggregate value constitutes principal items.
- While reporting under this clause, auditor should take into consideration clause 10 of the report, to identify the nature and type of business taxpayer is engaged into.
- The information about 'Yield' 'Percentage of Yield' and 'Shortage / Excess' is also required to be reported. Further, details of 'By-product' should be reported and if marketable by itself or by converting into sellable product, the auditor needs to identify and verify the same as to how those are accounted in the books of accounts.

### **CLAUSE-36 DETAILS OF TAX ON DISTRIBUTED PROFITS U/S 115-O OF A DOMESTIC COMPANY**

- This clause is omitted w.e.f. 01.04.2021.

**CLAUSE-37 AND 38 COST AUDIT / AUDIT UNDER CENTRAL EXCISE ACT, 1944 AND REPORTING ON DISQUALIFICATION OR DISAGREEMENT ON ANY MATTER/ ITEM/ VALUE/ QUANTITY**

- The Tax Auditor should ascertain from the management whether Cost Audit / Audit under Central Excise Act, 1944 was carried out and if yes, a copy of the same should be obtained from the assessee, there is no need to make detailed study of the report and not required to express any opinion on the same.
- The tax auditor is to report disqualification or disagreement on any matter/ item/ value/ quantity as may be reported/ identified by the Cost Auditor / Auditor under Central Excise Act, 1944.
- In cases where Cost Audit / Audit under Central Excise Act, 1944 have been ordered and not completed till the date of issuance of Tax Audit Report, the tax auditor has to report as to audit report 'not available' with the assessee.

**CLAUSE-39 AUDIT UNDER SERVICE TAX AND REPORTING ON DISQUALIFICATION OR DISAGREEMENT ON ANY MATTER/ITEM/VALUE/QUANTITY**

- Since service tax is not applicable for AY 2022-23 (i-e, FY 2021-22), so no reporting is to be done under this clause.

**CLAUSE-40 DETAILS REGARDING TURNOVER, GROSS PROFIT, ETC., FOR THE PREVIOUS YEAR AND PRECEDING PREVIOUS YEAR**

- Format of Reporting is as follows:

Sr. No.	Particulars	Previous year	Preceding previous year
1.	Total turnover of the assessee		
2.	Gross profit / turnover		
3.	Net profit / turnover		
4.	Stock-in-trade / turnover		
5.	Material consumed / finished goods		

(The details required to be furnished for principal items of goods traded or manufactured or services rendered)

- While calculating these ratios, the tax auditor should assign a meaning to the terms used in the above ratios having due regard to the generally accepted accounting principles (GAAP).
- There should be consistency between the numerator and the denominator while calculating the ratios.
- The term "stock-in-trade" would include only finished goods and would not include the stock of raw material and work-in-progress since the objective here is to compute the stock- turnover ratio.
- In case of Manufacturers, material consumed would, apart from raw material consumed, include stores, spare parts, loose tools, etc.

- In case the preceding previous year is not subject to audit, nothing should be mentioned in the in the previous year column.

**CLAUSE-41 DETAILS OF DEMAND RAISED OR REFUND ISSUED DURING THE PREVIOUS YEAR UNDER ANY TAX LAWS OTHER THAN I. T. ACT AND W. T. ACT WITH DETAILS OF RELEVANT PROCEEDINGS**

- Format of Reporting is as follows:

Sr. No.	Financial Year to which the Demand/ refund relates	Name of the applicable Act	Demand/ Refund Order No., if any	Date of Demand raised/ refund issued	Amount of demand raised/refund issued	Remarks
1	2	3	4	5	6	7

- The auditor should obtain a copy of all the demand/ refund orders issued by the governmental authorities during the previous year and received by the assessee up to the date of audit, also to cross verify the from online portal of the respective department and to report any adjustment of refund against any demand.
- It may be noted that the cess or duty like Marketing Cess, Cess on Royalty, Octroi Duty, Entry Tax etc. would not be covered under other tax laws.
- The auditor may check the said details with the disclosures of contingent liabilities in the audited financials, disclosures in Statutory Auditor's Report pursuant to CARO, if applicable.
- The tax auditor also requires details of relevant proceedings. This information should be furnished in remarks column by stating the authority before which the matter is pending.
- The tax auditor should ensure that penalties reported under clause 21 reconciles with the amount stated in this clause.

**CLAUSE-42 REQUIREMENT FOR FURNISHING OF STATEMENT IN FORM NO.61/61A/61B**

- Format of Reporting is as follows:

Sr. No.	Income-tax Department Reporting Entity Identification Number	Type of Form	Due date for furnishing	Date of furnishing	Whether the Form contains information about all details/transactions which are required to be reported.	If not, please furnish list of the details/transactions which are not reported.
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- Clause 42(a) requires tax auditor to state whether the assessee is required to furnish Form No. 61, Form No. 61A or Form No. 61B

➤ The reporting in above forms can be understood from following Table

Form No.	Section & Rule	Conditions
61	Section 139A(5)(c),	<p>Form No. 61 is to be filed by certain persons who have received any declaration in Form No. 60. Persons who have to file Form No. 61 are persons referred to in:</p> <p>(i) Rule 114C(1)(a) to (k), and</p> <p>(ii) Following persons who are required to get their accounts audited under section 44AB of the Act:</p> <ul style="list-style-type: none"> <li>- persons raising bill in respect of payment made in cash for amount exceeding Rs. 50,000 to a hotel or restaurant,</li> <li>- persons raising bill in connection with foreign travel or purchase of foreign currency payment for which payment is made in cash for an amount exceeding Rs. 50,000, and</li> <li>- person raising bill in respect of transactions of sale or purchase of goods or services other than those specified at serial numbers 1 to 17 of the Table in Rule 114B where value of the transaction exceeds Rs. 2 lakhs per transaction.</li> </ul>
61A	Section 285BA, Rule 114E	Rule 114E(2) provides the nature and value of transaction in respect of which the statement is required to be filed and persons who are required to file the statement
61B	Rule 114F, 114G and 114H	Rule 114F defines various terms, Rule 114G prescribes the information to be maintained and reported and Rule 114H prescribes the due diligence requirements.

➤ Due dates for furnishing the form/s are as under:

Form No.	Particulars	Due Date
61	(a) Where declarations in Form No. 60 have been received by 30 <sup>th</sup> September;	31 <sup>st</sup> October of that year.
	(b) Where declarations in Form No. 60 have been received by 31 <sup>st</sup> March.	30 <sup>th</sup> April of the Financial Year immediately following FY in which the form is received.
61A	Annual Information Return or Statement of Financial Transactions U/s 285BA(1) of I. T. Act, 1961.	31 <sup>st</sup> May of the Financial Year immediately following FY in which the form is received.
61B	Statement of Reportable Account U/s 285BA(1) of I. T. Act, 1961.	31 <sup>st</sup> May of the Financial Year immediately following FY in which the form is received.

- Every reporting financial institution has to communicate to the Principal Director General of Income-tax (Systems) the name, designation and communication details of the Designated Director and the Principal Officer and obtain a registration number. This registration number is to be quoted in the Form 61B. Once registered, I T dept. will issue ITDREIN (Income-tax Department Reporting Entity Identification Number) and the same is required to be mentioned in Form 61B.
- Form No. 61, 61A and 61B uploaded on the income tax portal should be examined by the tax auditor for purpose of reporting.

#### **CLAUSE-43 DETAILS W.R.T. COUNTRY-BY-COUNTRY REPORTING BY INTERNATIONAL GROUP AS REQUIRED U/S.286**

- The reporting under this clause is to be done based on accounting year, where the total consolidated group revenue reflected in the consolidated financial statement for the accounting year preceding such accounting year exceeds Rs.6,400 crores (Rule 10DB).
- Every constituent entity resident in India if it is a constituent of an international group and the parent entity of which is not resident in India, has to notify the prescribed income tax authority in Form No. 3CEAC whether it is the alternate reporting entity of the international group; or the details of the parent entity or the alternate reporting entity, if any, of the international group, and the country or territory of which the said entities are resident.

Term 'international group' to mean 'which carries on any business through a permanent establishment in other countries or territories'.

- Clause 43(a) requires the auditor to state whether the assessee or its parent entity or alternate reporting entity is liable to furnish the report referred to in section 286(2). In case liable to report, following information has to be furnished:

- (i) Whether report has been furnished by the assessee or its parent entity or an alternate reporting entity.
  - (ii) Name of parent entity
  - (iii) Name of alternate reporting entity (if applicable)
  - (iv) Date of furnishing of report
- If the assessee has filed a report, the tax auditor should verify acknowledgement for furnishing the same.

### **CLAUSE-44 BREAK-UP OF TOTAL EXPENDITURE AS RD & URD IN GST**

- Format of Reporting is as follows:

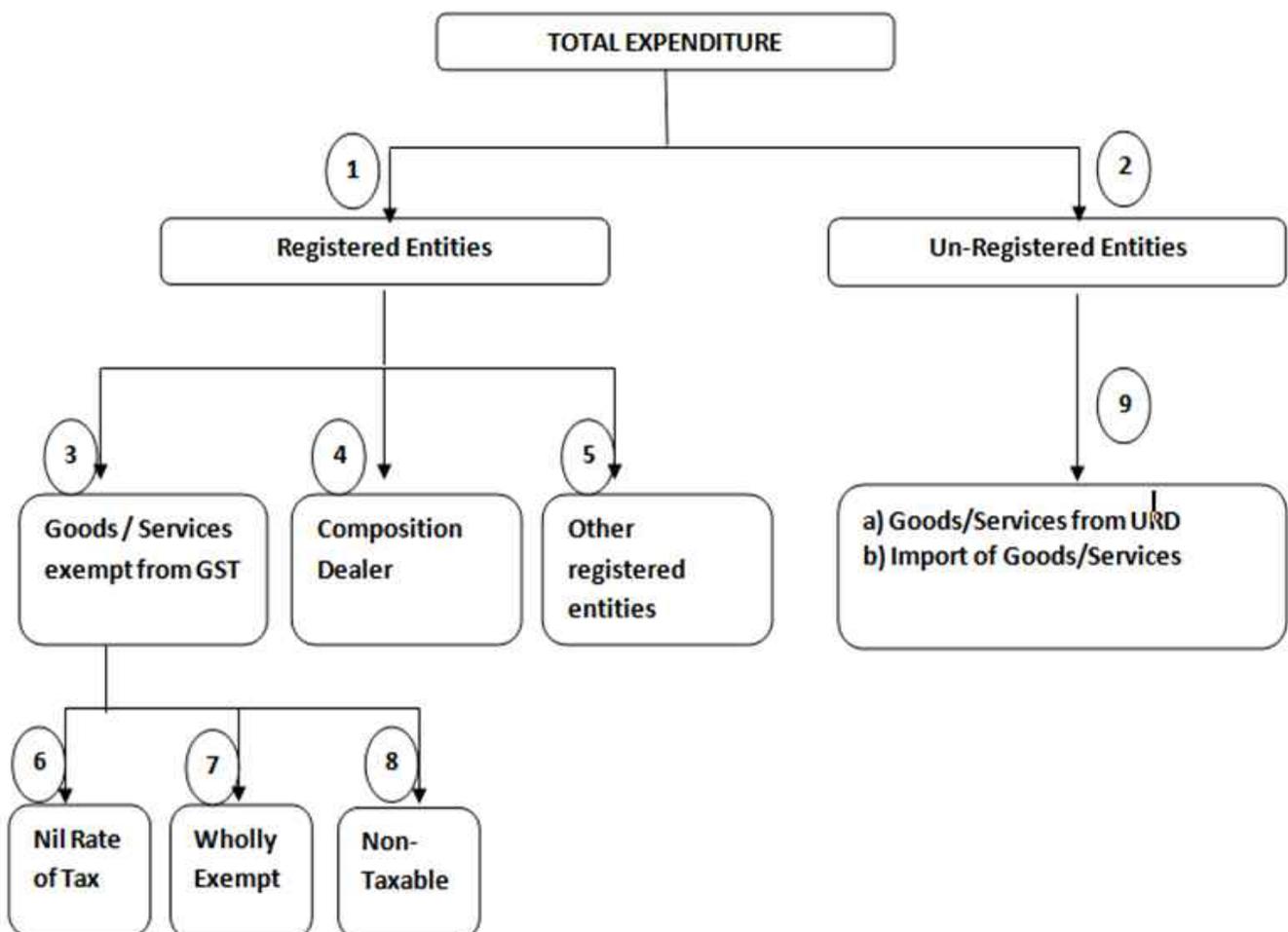
Sr. No.	Total amount of Expenditure incurred during the year	Expenditure in respect of entities registered under GST				Expenditure relating to entities not registered under GST
		Relating to goods or services exempt from GST	Relating to entities falling under composition scheme	Relating to other registered entities	# Total payment to registered entities	
(1)	(2)	(3)	(4)	(5)	(6)	(7)

# Here total payment to registered entities should be read as Total of the Expenditure.

- **IS THERE ANY REQUIREMENT TO MAINTAIN BOOKS OF ACCOUNTS UNDER GST, AND BY WHOM?**
  - There is requirement to maintain Books of Accounts, by entity registered under GST Law. The books of accounts to be maintained is specified under section 35 read with rule 56 of the CGST Act. This will help the Auditor to get the details to be reported under this clause.
- **LET US UNDERSTAND, WHAT CONSTITUTES 'EXPENDITURE'? WHETHER REVENUE EXPENDITURE OR CAPITAL EXPENDITURE?**
  - Following states what constitutes expenditure to be included for the purpose of reporting, which includes Revenue expenditure and Capital expenditure.

<u>EXPENDITURE TYPE</u>	<u>INCLUDE / EXCLUDE</u>
Purchases	Include (as Revenue Expenditure)
Expenses (of Revenue Nature)	Include (as Revenue Expenditure)
Asset Purchase (Capital Expenditure)	Include (as Capital Expenditure)
Provisions	Exclude
Depreciation/ Bad Debts etc.	Exclude (as Not a Supply)

- **TOTAL EXPENDITURE V/S. HEADWISE EXPENDITURE - WHAT IS TO BE INCLUDED IN THE REPORT?**
  - As per Guidance Note of ICAI, it is clarified that **TOTAL** of all the heads of expenditure is to be provided under clause 44 of Form 3CD and it is not expected to report head wise expenditure.
- **LET US UNDERSTAND WHAT CONSTITUTES 'TOTAL EXPENDITURE'**



➤ The terms specified in the above chart are explained herein below:-

SR.	PARTICULARS	EXPLANATION
1	Registered Entities	Any Person or entity having GST Number can be termed as Registered Entity.
2	Un-Registered Entities	Any other person or entity not falling under registered entities can be termed as Un-Registered Entities
3	Goods / Services exempt from GST	Section 2(47) of CGST Act, defines 'Exempt Supply'
4	Composition Dealer	<p>➤ A composition dealer cannot charge GST in the invoices and not issue a tax invoice but to issue 'bill of supply'.</p> <p>➤ A composition dealer cannot make inter-State supply</p> <p>➤ The composition dealer should have mentioned "Composition taxable person, not eligible to collect tax on supplies" at the top of the 'bill of supply' issued by them.</p> <p><u>Who cannot opt for composition scheme?</u></p> <p>➤ Manufacturers of ice cream, pan masala, or tobacco</p> <p>➤ Person engaged in the supply of non-taxable goods under the GST law (Petrol, Diesel, Natural Gas, Alcohol)</p>
5	Other registered entities	Any Registered entity not under Composition Dealer and Supplier of Exempt products will be considered as other registered entity (Not covered under (3) and (4) above)
6	Nil Rate of Tax	As per Section 11(1) of CGST Act and Section 6(1) of IGST Act, certain goods or services are notified as Nil rated.
7	Wholly Exempt	As per Section 11(1) of CGST Act and Section 6(1) of IGST Act, certain goods or services are notified as Wholly Exempt from tax.
8	Non-Taxable	Section 2(78) of the CGST Act, 2017 defines 'Non-Taxable Supply'.

SR.	PARTICULARS	EXPLANATION
9	Unregistered (URD) Expense	<ul style="list-style-type: none"> <li>➤ The value of inward supply of goods and/or services <u>received from unregistered persons</u> should be reported.</li> <li>➤ <u>Import of Goods and/or Services</u>, which are leviable to GST, should also be included here</li> <li>➤ <u>Schedule III Transactions</u> (These transactions are not included in any of the above categories, hence considered as URD supplies) <ul style="list-style-type: none"> <li>➤ Sale of Land</li> <li>➤ Sale of completed building</li> <li>➤ Salary to employees</li> <li>➤ High Seas Purchase</li> <li>➤ Purchase of Goods within Customs Warehouse</li> <li>➤ Actionable claims other than lottery, betting and gambling</li> <li>➤ Money or Securities [U/s. 2(52)]</li> </ul> </li> </ul>

Thus, the total of amounts in Column 3, Column 4 and Column 5 should match with total of amounts in Column 6 of the report.

• **PRACTICAL DILEMMA AS TO EXPENDITURE TO BE CLASSIFIED IN REGISTERED OR NOT REGISTERED COLUMN?**

- There is a practical difficulty when Small and Medium Size Dealer does not mention the GSTIN in their accounting software or books of accounts maintained. Therefore, it becomes difficult to identify each supplier under specified category namely registered dealer, composition dealer, unregistered dealer etc.
- In above circumstances, expenditure which may be treated as from unregistered person, but in fact those may be from registered persons., one will have to find out and identify the category of the suppliers as mentioned in the following chart, and then to decide whether to include under registered or not registered column:

SECTION	NATURE OF EXPENDITURE	POSSIBLE SOLUTION
17(5)	Block Credit – ITC not allowed and GST booked with expenses	Verify:GSTR-2A reconciliation & GSTR-3B item at Table 4D(1)
9(3)	Supplies under RCM -	For Registered : Verify GSTR-2A. For Unregistered : Verify RCM Invoice / Purchase Invoice - Sec 31(3)(f)
10/11	Composition Supplier Exempt Supplies from Registered Dealer	Verify GSTR-3B item at Table 5
GSTIN of Auditee not mentioned	ITC not claimed and tax booked with expense / expense incurred in cash	Only possible to verify from supplier master (in case properly maintained by the auditee) or vouching.

It may thus be noted that the total of amounts in Column 6 and Column 7 should match with total of amounts in Column 2 of the report.

● **REPORTING REQUIREMENT**

➤ An appropriate disclosure should be made by the Tax auditor in Form 3CA/3CB, as the case may be, for the view taken by the assessee in relation to the.....

1. Meaning of "Total expenditure" and
2. The method of filling up the appropriate columns.

➤ If the assessee is not in a position to give the details as required in clause 44, an appropriate disclosure/ disclaimer may be made by the auditor in Form 3CA/3CB.

● **DISCLOSURE / DISCLAIMER SPECIMENS:**

➤ **Non-maintenance of information required by this clause:**

We have been informed by the assessee that the information required under this clause has not been maintained by them, in absence of any information available, we are unable to report the same under this clause.

➤ **Inadequate or insufficient maintenance of information required by this clause:**

- It is not possible for us to determine the breakup of total expenditure of entities registered or not under the GST, as necessary information is not maintained by the assessee in its books of accounts, or

- The standard accounting software used by the assessee is not configured to generate any report in respect of required data in this clause, or
- We are unable to verify and report the desired information in this clause, or
- In absence of the proper system of assessee, we are unable to comment and give the details as required in Clause 44.

*Presently, due to technological reforms, the data with various departments is readily available and can be easily inter-linked and co-related. Therefore, the amounts reported under Clause 44 should thus be reconcilable with the amounts specified in Table 6 of GST Annual Return [Form GSTR-9] as well as Table 12 & Table 14 of GST Audit Report [Form GSTR-9C].*

*It is strongly recommended that, each of these GST reporting requirements may be prepared simultaneously and reconciled, before reporting under this clause, to avoid future difficulties and discrepancies.*



## CHALLENGES AND PRECAUTIONS WHILE PREPARING THE FINANCIAL STATEMENTS FOR A COMPANY UNDER STATUTORY AUDIT



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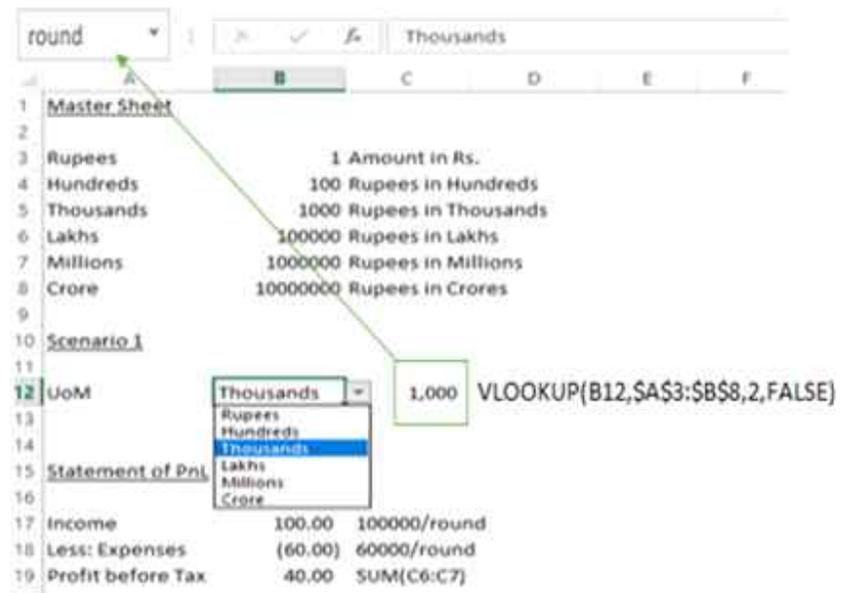
Financial Statements (FS) provide a snapshot of a Company's financial health, performance, insights on the operations and cash flow that help stakeholders in decision making. Considering the ever increasing corporate failures, rising NPAs in banks and non-banking financial institutions, diversion of public funds, MCA has amended Schedule III to the Companies Act, 2013 to enhance transparency and to ensure credibility and accountability of FS. This article pertains to the challenges faced and precautions to be followed by the management of the Company in preparation and presentation of Division - I FS for the purpose of statutory audit and the corresponding audit procedures to be followed, observations and documentation to be maintained by the statutory auditor of the Company.

### 1. Mandatory Rounding off requirement

Precautions	Challenges
<ul style="list-style-type: none"> <li>• Common unit of measurement (UoM) to be applied across the complete set of FS including Annual Report and must be categorically disclosed.</li> <li>• Ensure there are no casting errors</li> <li>• Appropriate disclosure to be given in places where the rounded off amount is less than UoM applied. E.g. Asterisk (*) indicates amount less than UoM applied</li> <li>• Rounding off to be applied only on amounts / value and not on quantity. (E.g. Number of shares should not be rounded off). However, earnings per share shall not be rounded off.</li> </ul>	<ul style="list-style-type: none"> <li>• Maintain two sets of FS               <ul style="list-style-type: none"> <li>□ one set of FS in absolute numbers for ITR and/or ROC purpose</li> <li>□ other set of FS in rounded off</li> </ul> </li> <li>• User readability of FS for its comparability and analysis across sectors / industries</li> <li>• In case of consolidation, practical challenge is faced when various entities within the Group follow different UoM. <u>Authors' View:</u> Common UoM can be followed within the Group to ensure hassle-free process of consolidation.</li> </ul>

**Let's make it Simple!**

- Management can make use of Microsoft Excel to optimize its time and efforts in rounding off the FS, in cases where the ERP software does not give such facility.
- A separate sheet can be created in the FS workbook wherein a cell can be defined say, "round" instead of "C12", as depicted in snapshot and all the amounts / values in the FS can be divided with "round". Basis the selection of UoM, the values shall change in the FS.



**Auditor's procedures, considerations and documentations:**

- Amounts reported in the audit report must also be rounded off using the same UoM as applied for preparation and presentation of the FS.

**2. Share Capital**

Precautions	Challenges
<ul style="list-style-type: none"> <li>• Ensure adequate disclosure vis-à-vis Share Capital, terms and rights, reconciliation, promoter shareholding, more than 5% shareholding, etc. is provided for every class of equity and preference shares separately.</li> <li>• Details of promoters shareholding in FS shall be in sync with Annual Return (Form MGT-7/ MGT-7A).</li> <li>• In case of newly incorporated companies, change in promoters shareholding shall be calculated from date of initial subscription.</li> <li>• Employee Share-based Payments, Stock Options Outstanding Account should be disclosed as a separate line-item. The Schedule III requires this item to be shown as a part of 'Reserve and Surplus'.</li> </ul>	<ul style="list-style-type: none"> <li>• Disclosure in authorised share capital wherein:                             <ul style="list-style-type: none"> <li>□ Resolution for change in authorised share capital has been passed before reporting date. However, Form SH-7 is filed subsequently i.e. after reporting date <u>Authors' view:</u> Since the resolution has already been passed, revised share capital to be disclosed.</li> </ul> </li> <li>• Disclosure in issued, subscribed, paid up share capital for a newly incorporated company wherein:                             <ul style="list-style-type: none"> <li>□ Only part subscription amount is received before reporting date; balance amount is received subsequently i.e. after reporting date <u>Authors' view:</u> Total amount of subscription must be disclosed as per Memorandum of Association; irrespective of amount actually received before reporting date.</li> </ul> </li> </ul>

Precautions	Challenges
<ul style="list-style-type: none"> <li>In case of any change in authorised capital, ensure Memorandum of Association (MoA) is amended to give effect thereof.</li> <li>In case of private placement of shares, ensure funds are collected in a separate bank account and are not utilised until return of allotment in Form PAS-3 is filed with ROC.</li> </ul>	<ul style="list-style-type: none"> <li>Disclosure in case of merger/ de-merger: <ul style="list-style-type: none"> <li>In case where the scheme of merger/ de-merger is approved before the reporting date; however, shares are issued subsequent to the reporting date <u>Authors' view:</u> Issued shares to be disclosed as 'Share Suspense' as a separate line item after Share capital but before Reserves &amp; Surplus.</li> </ul> </li> </ul>

### **Auditor's procedures, considerations and documentations:**

- Auditor shall refer to the Articles of Association (AOA) and MoA of the Company, altered AOA and MOA, if any and master records from MCA website.
- Auditor must verify whether the promoter shareholding disclosed is in accordance with the term 'Promoters' as defined in the Companies Act, 2013.
- Alternatively, the auditor can refer to the Annual Return i.e. Form MGT-7/ MGT-7A filed by the Company for the previous reporting period.
- Review the minutes of board and shareholders' meeting for the interim changes, if any.
- The auditor must obtain management representation stating the shareholding of each class of shares along with promoter details.
- Valuation report where shares are issued on private placement.

### **3. Borrowings (Current & Non-Current)**

Precautions	Challenges
<ul style="list-style-type: none"> <li>The classification of loans between current and non-current shall be predominantly on the basis of loan agreement.</li> <li>Nature of security shall be specified separately in every borrowing..</li> </ul>	<ul style="list-style-type: none"> <li>Classification of a particular loan as a term loan: <u>Authors' view:</u> Term loans normally have a fixed or pre-determined maturity period or a repayment schedule and need not be restricted to a period of 36 months which is otherwise defined as 36 months in CARO 2020.</li> </ul>

Precautions	Challenges
<ul style="list-style-type: none"> <li>• Terms of repayment of term loans and other loans shall be disclosed in FS.</li> <li>• Period and amount of continuing default (for principal and interest) as on the reporting date shall be specified separately in each case.</li> <li>• Current maturities of all long-term borrowings will be disclosed under 'short-term borrowings'.</li> <li>• Reporting disclosure for utilisation of amount raised from banks and financial institutions must be based on the overall position of balance sheet at the reporting period. <ul style="list-style-type: none"> <li>• Ensuring that all related details pertaining to utilisation and methodology adopted along with necessary workings prepared by the management are available for auditor's verification.</li> </ul> </li> <li>• Details of charge (creation/modification/satisfaction) against borrowings to be disclosed and the same must be registered with ROC within the stipulated time. If not registered within stipulated time, separate disclosure is required.</li> <li>• Quarterly reconciliation of security-wise and lender-wise disclosure between the amounts reported in quarterly statements and amounts reflected in books of accounts for borrowings sanctioned by banks and / or financial institutions on the basis of security of only current assets. <ul style="list-style-type: none"> <li>□ These borrowings may be during any point of time of the year.</li> <li>□ Sanction should include fresh sanction, limits renewed as well as limits due for renewal during the reporting period.</li> <li>□ Disclosure is required for both fund based/ non-fund based credit facilities.</li> </ul> </li> <li>• Interest accrued and due/ Interest accrued but not due on borrowings must be separately disclosed under Other Current Liabilities.</li> </ul>	<ul style="list-style-type: none"> <li>• Ensuring appropriate utilisation of long term borrowings for long term purposes and specified borrowings for specified purposes. Authors' Comment: Where the funds are received in a common bank account, management can analyse the movement/ utilisation of funds based on the overall position of balance sheet at the reporting period and maintain adequate documentation. Onus will be on the Company to prove that funds were utilized for the purpose of borrowing.</li> <li>• Disclosure requirement if the funds were parked temporarily until the actual utilization of funds raised from banks and financial institutions Authors' view: The same shall be construed as borrowings not utilised for specific purposes and details of investment must be specified.</li> <li>• Obtaining data for disclosures pertaining to wilful defaulter. The same is available from RBI website. Alternatively, the company can obtain CIBIL report at the end of reporting period.</li> <li>• Utilisation of borrowed funds and share premium by way of an investment or providing guarantee or security or advancement of loan to Ultimate beneficiary through an Intermediary. <ul style="list-style-type: none"> <li>□ Tracking of money trail will be complex where the entities are not related.</li> <li>□ Disclosure is required for each level of intermediary making it all the way more tedious and time consuming exercise</li> <li>□ Obtaining declarations from each such intermediary that they are compliant with PMLA and FEMA, if applicable.</li> </ul> </li> </ul>

**Auditor's procedures, considerations and documentations:**

- The auditor shall verify the above judgement, estimates and assumptions made by the management for various disclosures as covered above.
- The auditor shall duly verify all the loan agreements; Form CHG-1, Form CHG-4, details of moratorium and accounting thereof (including the TDS implications during moratorium, if any)
- If the company has defaulted in repayments of loans or borrowings, it shall report the same in its Audit Report in the prescribed format.
- Care must be taken that this reporting is applicable for all types of lenders and not restricted to banks and financial institutions
- Where a loan is borrowed from any entity or a person to meet the obligations of its subsidiaries, associates or joint ventures, the auditor must ensure that the funds have been utilized for the said purpose by obtaining a CA certificate (preferably statutory auditor) from such subsidiaries, associates or joint ventures.
- The auditor shall verify the “nature of security” as per the sanctioned loan agreement or term sheet along with the physical verification of security certificates, where investment in securities of its subsidiaries, joint ventures or associate companies is pledged for obtaining any loans.
- The auditor shall adhere to SA 505 “External Confirmations”
- It must be ensured that the loans obtained are within the borrowing powers of the entity by complying with the provisions of Companies Act, 2013 and rules thereof [Section 180(1)(c), where applicable].

**4. Trade Payables (Current & Non-Current)**

Precautions	Challenges
<ul style="list-style-type: none"> <li>• The amounts due under contractual obligations cannot be included within Trade payables. Such contractual obligations may include dues payables in respect of statutory obligations like contribution to provident fund, purchase of Property, Plant and Equipment, Intangible Assets, etc.</li> <li>• MSME disclosure: The disclosure is only for micro and small enterprises and not for medium enterprises.</li> </ul>	<ul style="list-style-type: none"> <li>• Information of vendors registered as Micro and Small Enterprise.</li> <li>• Rate of Interest on delayed payments (beyond 45 days) = 3 times the Bank rate notified by RBI <u>Authors' Comment:</u> RBI Bank rate can be obtained by selecting the appropriate week and referring the “Ratios and Rates” file from the following RBI website: <a href="https://www.rbi.org.in/Scripts/BS_ViewWss.aspx">https://www.rbi.org.in/Scripts/BS_ViewWss.aspx</a></li> </ul>

Precautions	Challenges
<ul style="list-style-type: none"> <li>• Ageing details: Disclosure for ageing analysis is broadly categorised into: outstanding amounts which are unbilled, not due and due over specified periods; and classified between disputed and undisputed dues.               <ul style="list-style-type: none"> <li>□ Even though the disclosure requirements states amount due to MSME, the disclosure must be only for Micro and Small Enterprises.</li> <li>□ In case of amalgamation/merger - Original date will be considered for the purpose of giving information. If such information is not available, the fact should be so stated.</li> <li>□ In case due date for payment to vendors is not maintained in the accounting software, transaction date i.e. date of recognising liability in books of accounts can be considered as the due date for payment.</li> </ul> </li> <li>• Ageing Schedule shall anchor as an indicator for accounting of write backs, if any. In case of any write backs, corresponding effect of reversal of indirect</li> </ul>	<ul style="list-style-type: none"> <li>• Provision of interest in cases where the payment was outstanding for a period more than 45 days, but not outstanding as on the reporting date.</li> <li>• Whether the balance confirmation obtained from MSME vendors would suffice in case interest is not accounted for in the FS where the payment was due for more than 45 days? <u>Authors' View:</u> If the management categorically mentions the fact that interest is not provided and the party confirms the same, the management shall disclose this fact in FS for not providing such interest, else it may have to disclose the same as a contingent liability.</li> <li>• Ageing Details               <ul style="list-style-type: none"> <li>□ Whether amounts outstanding for a substantially long period of time are to be disclosed as disputed or not? <u>Authors' View:</u> In cases where evidence can corroborate the fact of existence of a dispute, only then the same must be disclosed as disputed dues.</li> </ul> </li> </ul>

#### **Auditor's procedures, considerations and documentations:**

- Evaluate internal control procedures viz. quotations for purchase orders, walk through process for purchases accounting, credit period policy from different vendors, etc.
- The auditor shall perform cut-off procedures to confirm that all the transaction for the year under review have been duly accounted.
- The auditor shall obtain external confirmations for the type of vendor i.e. whether registered as MSME, the amount outstanding as on the reporting date. In case of any discrepancy in the balance confirmation, the auditor shall verify how the un-reconciling items are dealt by the management in its FS.
- The auditor can verify the parameters captured for generating the Ageing report from the ERP system on test check basis.
- Based on ageing analysis, the auditor shall conduct enquiry with the management regarding the payment plan and/or any write backs, if any.
- In case of disputed dues, the auditor may obtain the necessary documentary evidence to verify the claim of the management and simultaneously verify contingent liability, if any.

## 5. Property, Plant and Equipment and Intangible Assets

Precautions	Challenges
<ul style="list-style-type: none"> <li>• A separate disclosure is required for all leased assets.</li> <li>• Reconciliation of gross and net carrying amounts of each class of assets indicating additions, disposals, acquisitions through business combinations, amount of change due to revaluation and other adjustments (As per AS-11/ AS-16) and the related depreciation and impairment losses/reversals is to be provided.               <ul style="list-style-type: none"> <li>□ Any adjustments due to business combinations/ demergers, must be separately disclosed.</li> </ul> </li> <li>• Separate disclosure is required in cases where title deeds of immovable property are not held in the name of the Company as on the reporting date.               <ul style="list-style-type: none"> <li>□ These could be cases where documents are under preparation or registration process of transfer of name is in progress or due to a dispute, or on account of merger/ demerger/ conversion.</li> <li>□ If such property is jointly owned, disclosure will only be to the extent of company's share.</li> </ul> </li> <li>• Benami property shall be separate disclosed.</li> <li>• Impairment of property, plant and equipment and Intangible Assets must be tested</li> </ul>	<ul style="list-style-type: none"> <li>• Whether disclosure is required where immovable property is held as inventory but not in the name of the Company. Eg. Real estate business <u>Authors' View:</u> No such disclosure is required.</li> <li>• Benami property held by the Company               <ul style="list-style-type: none"> <li>□ Beneficiary details may not be easily available</li> <li>□ There would be practical challenge in identifying a property if the same is not maintained in the books of accounts.</li> </ul> </li> <li>• Disclosure requirements in case of revaluation:               <ul style="list-style-type: none"> <li>□ Schedule III requires separate disclosure if revaluation change is 10% or more in aggregate of the net carrying value of each class of Property, Plant and Equipment. However, AS 10 requires separate disclosure irrespective of % change in revaluation.</li> <li>□ Further, this disclosure is required to be stated for a period of five years as per Schedule III. However, AS 10 stipulates this disclosure requirement as long as the asset is held by the company.</li> <li>□ In such conflicting cases, AS shall prevail over Schedule III.</li> </ul> </li> </ul>

### Auditor's procedures, considerations and documentations:

- The auditor should verify the records with reference to the documentary evidence such as orders, invoices, receiving reports, title deeds, applicable GST documents, lease or hire purchase agreements, minutes of the Board meeting and by evaluation of internal controls.
- The auditor must obtain and make a sanity check of the valuation report in case of revaluation.
- Auditor shall verify the impact of revaluation of assets on deferred tax, if any .

- Auditor must be vigilant while performing verification for identifying benami property, if any by adopting additional procedures viz. reviewing the minutes of the meeting, any unusual legal or professional charges incurred, any expenditure pertaining to maintenance charges for a property which is neither owned nor rented, inquiries from the management, etc.
- Auditor must review the certificate obtained by the management from technical expert in cases where useful life or residual value estimated by the management differs from the details prescribed under Schedule II of the Companies Act, 2013.
- In cases of business combination/ amalgamation/ de-merger, auditor must verify the scheme of arrangement to assert the correctness, accuracy and valuation at which assets are accounted for in the books of accounts. Further, in case if title deeds are not registered in the name of the resultant entity, the auditor will have to disclose the relevant details in his audit report.
- Auditor must verify the FAR maintained by the management and must ensure physical verification of such assets to assert on the existence and accuracy via observation or re-performance followed by annual impairment testing.

#### 6. Capital Work-in-Progress (CWIP) and Intangible Assets under Development (IAD)

Precautions	Challenges
<ul style="list-style-type: none"> <li>• Capital advances should be included under Long-term loans and advances and not under capital work-in-progress.</li> <li>• Ageing Schedule to be provided duly classified between projects in progress and projects temporarily suspended as on each reporting date. <ul style="list-style-type: none"> <li>□ Classification of projects temporarily suspended must be in sync with AS 16 and corresponding capitalisation of borrowing costs on such projects must be suspended.</li> <li>□ In case of amalgamation/merger - Original date will be considered for the purpose of giving information. If such information is not available, the fact should be so stated.</li> </ul> </li> <li>• Project-wise completion schedule to be disclosed where period was overdue or cost was over-run as compared to the original plan.</li> <li>• Impairment must be tested annually.</li> </ul>	<ul style="list-style-type: none"> <li>• What constitutes a Project? <u>Authors' Comment:</u> The term project is subjective and management may exercise its best judgement in identification of a Project. The methodology once adopted must be consistently followed.</li> <li>• Whether previous year's amounts to be re-classified in case if a project was classified as work-in-progress in the previous year; but was temporarily suspended during the year? <u>Authors' Comment:</u> No. Amounts of previous year to be continued as work-in-progress; whereas current year amounts will be disclosed as progress under temporary suspension.</li> <li>• Original plan vs. revised plan <u>Authors' View:</u> Plans shall include management's estimates and assumptions w.r.t future business, economy / industry and regulatory environments and such assumptions may be subject to change from time to time resulting in a 'revised plan'. Management shall apply judgement in determining whether such revisions are in the nature of a fresh 'Original Plan' or simply an update of estimates and assumptions.</li> </ul>

**Auditor's procedures, considerations and documentations:**

- The auditor must obtain an understanding of how the management has derived in identification of a project.
- Auditor must inquire with the management for future viability of the CWIP that are overdue in period or where there is cost over-run.
- There may be instances of difference in opinion between auditor and management with respect to whether a project is in progress or is temporarily suspended. In such cases, depending on facts and circumstances of the case, auditor may provide a modified opinion in his audit report.

**7. Investments (Non-Current and Current)**

Precautions	Challenges
<ul style="list-style-type: none"> <li>• Valuation of investment:               <ul style="list-style-type: none"> <li>□ Non-current investments must be valued at cost in accordance with AS-13 unless there is a decline in the value of a long-term investment being other than temporary decline. Diminution in the value of investments must be disclosed under the relevant heads separately.</li> <li>□ If non-current investments are valued at other than cost, the basis of valuation for each individual investment should be disclosed.</li> <li>□ Current investments must be carried at lower of cost or fair value in accordance with AS-13 which is determined either by category of investment or on an individual investment basis. However, the valuation must not be on an overall basis.</li> </ul> </li> <li>• Aggregate cost and market value of quoted Investments along with aggregate amount of diminution in value of investments must be disclosed.</li> <li>• In case of investment in partnership firm, details of partners' contribution and share must also be separately disclosed.</li> <li>• In case additional costs are incurred for acquiring such investments, the same must be added to the cost of investments.</li> </ul>	<ul style="list-style-type: none"> <li>• Valuation of current investments in an unlisted entity may pose to be a challenge, as fair value may not be readily available.</li> <li>• Identification whether decline in fair value of current investment is temporary in nature or otherwise could be a challenge. Mere de-listing of an investment may not tantamount to diminution in the value of investments. Various scenarios must be envisaged.</li> <li>• While acquiring an unlisted investment, management shall procure valuation report in accordance with the requirement stipulated under section 56(2)(x) of the Income Tax Act, 1961 as it may impact the computation of provision for current taxes.</li> <li>• In case where an investee entity viz. Company is subsequently converted into a LLP, what shall be the treatment for premium paid during original acquisition. <u>Authors' View:</u> The fixed capital contribution is restricted to the amount of face value of the share held in the erstwhile Company and the excess premium would be treated as a separate line item under Investment.</li> </ul>

**Auditor's procedures, considerations and documentations:**

- Auditor must verify all relevant documentation for asserting on the ownership and existence of the investment. Valuation report must also be verified where necessary. Auditor must obtain external confirmations in case of investment in partnership firms.
- In case of investment in a group entity, auditor shall test for impairment by calling for financial information of all such entities in the group
- Auditor must also ensure that the Company has complied with Section 186 and Section 188 of the Companies Act, 2013.
- Review the minutes of board and shareholders' meeting for the interim changes vis-à-vis investments, if any.

**8. Loans and Advances (Non-Current and Current)**

Precautions	Challenges
<ul style="list-style-type: none"> <li>• The company must disclose the relationship of the person to whom loans are advanced, if such person is a promoter, director, key managerial person or a related party. Such relationship must exist on the date of advancement of loan and not as on the reporting date.</li> <li>• The Company shall ensure that the loan agreement contains the purpose for advancing such loan along with the requirement of obtaining Annual Statutory Auditor's certificate for utilisation of such funds by the borrower.</li> <li>• Where the Company has advanced any loans, it shall ensure that the provisions of Section 185 and 186 of the Companies Act, 2013 and Section 2(22)(e) of the Income Tax Act, 1961 are duly complied with.</li> <li>• When a company not being a Non-Banking Financial Institution has advanced any loan it shall ensure that the provisions of Non-Banking Financial Institution norms are not violated i.e. it's             <ul style="list-style-type: none"> <li>□ Non-finance income does not exceed 50% of gross total income and</li> <li>□ Non-finance assets does not exceed 50% of it's total assets.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Can advances be interpreted as loan given? <u>Authors' View:</u> The interpretation of whether advances are in the nature of loans shall depend upon facts and circumstances of each case. Simply charging of interest on advances need not imply that advances are in the nature of loans.</li> <li>• Where the Company has advanced any loans to it's promoters, directors, key managerial persons or related parties which are either repayable on demand or where the agreement does not specify the relevant terms of loan, the said fact shall be disclosed separately group wise. <u>Authors' Comment :</u> In case director is also a promoter and / or KMP, management can follow hierarchy of command i.e. Promoter followed by director followed by KMP. In this case, it is recommended to disclose person as Promoter.</li> <li>• Where there are multiple advancement of loans to a single party and the relationship of such party has changed over the period from the date of advancement of loans upto the reporting date, identification of relationship at each point in time may prove to be a challenging and time-consuming task. In such case, the resultant disclosure may be absurd.</li> </ul>

Precautions	Challenges
<ul style="list-style-type: none"> <li>● In case of a Non-Banking Financial Institution where the loan has turned bad or doubtful, the Company shall comply with the IRAC Norms and disclose such assets as non-performing/ sub-standard/ doubtful or loss assets; and accordingly appropriate provisions must be accounted for.</li> <li>● Where the loan has turned bad or doubtful and interest income is accounted for on receipt basis, the fact must be appropriately disclosed under its significant accounting policy.</li> </ul>	<ul style="list-style-type: none"> <li>● Utilisation by the recipient of funds and share premium by way of further investment or providing guarantee or security or advancement of loan to ultimate beneficiary <ul style="list-style-type: none"> <li>□ Tracking of money trail will be complex where the entities are not related.</li> <li>□ Disclosure is required for each level of intermediary making it all the way more tedious and time consuming exercise</li> <li>□ Obtaining declarations from each such intermediary that they are compliant with PMLA and FEMA, if applicable.</li> </ul> </li> </ul>

**Auditor's procedures, considerations and documentations:**

- Obtain a list of related party relationship from the management with categorical bifurcation between promoter, director and key managerial personnel.
- Verify relevant loan agreements.
- The auditor must substantiate his audit procedures based on the end use certificate issued by a Chartered Accountant.
- Auditor must verify whether provisions for bad and doubtful loans and advances are appropriate.
- The auditor shall adhere to SA 505 "External Confirmations".
- Auditor must also ensure that the Company has complied with Section 185 and Section 186 of the Companies Act, 2013.
- Review the minutes of board and shareholders' meeting for the interim changes, if any.

## 9. Trade Receivables

Precautions	Challenges
<ul style="list-style-type: none"> <li>Ageing details: Disclosure for ageing analysis is broadly categorised into: outstanding amounts which are unbilled, not due and due over specified periods. The disclosure is further classified into:               <ul style="list-style-type: none"> <li>disputed / undisputed dues</li> <li>considered good/ doubtful</li> </ul> </li> <li>Ageing Schedule shall anchor as an indicator for accounting of provisions/ impairment, if any.</li> </ul>	<ul style="list-style-type: none"> <li>Ageing Details               <ul style="list-style-type: none"> <li>Whether amounts outstanding for a substantially long period of time are to be disclosed as disputed or not? <u>Authors' View:</u> In cases where evidence can corroborate the fact of existence of a dispute, only then the same must be disclosed as disputed dues.</li> <li>If due dates for receipt from customers are not maintained in accounting software <u>Authors' Comment:</u> The transaction date i.e. date of recognising income in books of accounts can be considered as the due date of payment.</li> </ul> </li> </ul>

### Auditor's procedures, considerations and documentations:

- Evaluate internal control procedures viz. walk through process for sales accounting, credit period policy for different customers, etc.
- Perform cut-off procedures to confirm all transaction for year under review have been duly accounted.
- Obtain external confirmations for amount outstanding as on reporting date. In case of any discrepancy in balance confirmation, auditor shall verify how un-reconciling items are dealt with by the management in its FS.
- The auditor can verify the parameters captured for generating the Ageing report from the ERP system on test check basis.
- Based on ageing analysis, the auditor shall conduct enquiry with the management regarding the collection and follow-up plan, ongoing legal cases and/or write offs, if any.

## 10. Relationship with Struck Off Companies

Precautions	Challenges
<ul style="list-style-type: none"> <li>Management shall disclose the name of struck off company, nature of transactions with such struck off company, balance outstanding as on reporting date and relationship with such companies, if any.</li> </ul>	<ul style="list-style-type: none"> <li>Gathering the data of struck off companies (from MCA database) is a tedious and time consuming process.</li> </ul>

Precautions	Challenges
<ul style="list-style-type: none"> <li>• The above disclosure is required even when the balance outstanding at the end of reporting period is Nil but the transaction with struck off company has occurred during the year.</li> <li>• Where the company is under insolvency process, the same shall not be disclosed as it cannot be considered as struck off company.</li> <li>• In case of change in relationship status, the status prevailing as at the end of the reporting period shall be disclosed.</li> <li>• Gross Carrying amount of transaction (without netting off provision for doubtful debts or impairment loss allowance) shall be</li> </ul>	<ul style="list-style-type: none"> <li>• What if company is struck off during the year but has been restored? <ul style="list-style-type: none"> <li>□ Disclosure is not required if it is restored before signing of FS.</li> </ul> </li> <li>• How to disclose comparative earlier year reporting period's figure, where the company is struck off during the reporting period? <ul style="list-style-type: none"> <li>□ "N.A." can be mentioned for the comparative previous year along with a note stating that "since the company was struck off during the current reporting period, there is no comparative figure of previous year disclosed".</li> </ul> </li> </ul>

#### **Auditor's procedures, considerations and documentations:**

- Inquire about the processes applied by the management in deriving the companies that are struck off and obtain necessary documentation (e.g. screenshots of MCA Company Master data of such parties) and ensure that reporting of such transactions is upto the date of signing FS and not as on the reporting date.
- Verify the implications of transaction entered with struck off companies and the corresponding implication on the existence of such asset or liability, as the case maybe, post conducting enquiry with the management (E.g. Check for impairment in case of any investments with struck off companies.)

#### **11. Analytical Ratios**

Precautions	Challenges
<ul style="list-style-type: none"> <li>• All ratios are applicable to all companies that are governed by the Companies Act, 2013, irrespective of any exemptions specified in any other laws.</li> <li>• The formulae prescribed in Guidance note on Schedule III is only recommendatory in nature. Management may adopt any other methodology in deriving the ratios by factoring in the company specific and industry specific nuances.</li> </ul>	<ul style="list-style-type: none"> <li>• Whether ratios must be disclosed as favourable/ adverse? <p><u>Authors' View:</u> Management may disclose ratios as favourable/ adverse. However, it is recommended that consistent method is followed for disclosing variance of each and every ratio i.e. Output of Current year's figures - Output of Previous year's figures or vice versa; without stating favourable / adverse remark.</p> </li> </ul>

Precautions	Challenges
<ul style="list-style-type: none"> <li>• There are ratios where average inventory, trade receivables, trade payables and working capital are required as denominator.               <ul style="list-style-type: none"> <li>□ In case of first year of the company, closing amounts needs to be used instead of average amounts; since average amounts will not be available.</li> <li>□ In second year, closing amounts must be used instead of average amounts; to enable comparability. Adequate disclosure must be provided indicating reason for using closing amounts instead of average amounts.</li> <li>□ From third year onwards, management can use average based formulae and provide an adequate disclosure stating previous year's</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• When numerator and denominator of a ratio are both in negatives, whether the ratio would be disclosed as positive/ negative? <u>Authors' View:</u> The ratio would be disclosed in negative.</li> <li>• Owing to complexity of formula for determining the return on investment that is prescribed in the Guidance note on Schedule III, it is recommended that Management shall make suitable adjustments to the formulae and make appropriate disclosures. e.g.: (Current value of investment – Initial Value of Investment)/ Initial Value of Investment x 100</li> </ul>

## 12. Other Points

- **Cash and Cash Balances:**

Cash and cash balances are broadly categorised into Cash and Cash Equivalents and Other Bank Balances as under:

- Cash on hand, cheques on hand, balance in banks that are free from lien: Cash and Cash Equivalents
- Bank balances that are held as margin money or security against borrowings: Other Bank Balances
- Unpaid dividend account: Other Bank Balances
- Bank deposits where:
  - Original maturity < 3 months: Cash and Cash Equivalents
  - Original maturity < 3 months but lien is marked: Other Bank Balances
  - Original maturity > 3 months but maturity is on or before 12 months from the Reporting date: Other Bank Balances
  - Maturity > 12 months from the Reporting date: Non-current Assets

- **Deferred Tax Asset / Liability:**

- Management shall ensure that the deferred tax assets and liabilities are measured using the tax rates and tax laws that have been enacted or substantively enacted as at the reporting date.

- Recognition of deferred tax assets (DTA):
  - In case an enterprise has unabsorbed depreciation or carry forward of losses under tax laws Recognition of DTA to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such DTA can be realised.
  - In any other cases Recognition of DTA to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.
- **Disclosure of Crypto Currency or Virtual Currency:**
  - In case the company has traded or invested in virtual currencies, it shall disclose:
    - Profit / loss on such transactions
    - INR amount of currency held at the reporting date
    - Deposits or advances from any person for the purpose of trading or investing in Crypto Currency / Virtual Currency
- **Undisclosed Income:**
  - Company shall disclose such income separately in FS where it has voluntarily admitted to the addition of erstwhile unrecorded income, which can be demonstrated on the basis of the search report.
  - In case the addition is made by the income tax authorities and the company has disputed such additions, the above disclosure shall not be applicable.
  - Even where the company chooses not to file an appeal, it cannot be presumed that the company has surrendered or disclosed the income.
  - In case of consolidated FS, the holding company shall disclose the names of each such subsidiary / group entity that has an undisclosed income. Further. if associate company has undisclosed income, then the Holding Company should disclose if such income is material to the group.
- **Corporate Social Responsibility:**
  - The reporting of Corporate Social Responsibility of the Company in the notes to accounts forming part of the FS must be in line with the reporting in Director's Report.
- **AS based and other disclosures (Illustrative list):**
  - AS-7, AS-15, AS-16, AS-17, AS-18, AS-19, AS-20, AS-29
  - Contingent liability and capital commitment
  - Earnings and expenditure in foreign currency

### **Conclusion:**

To sum up, all the amendments made in Schedule III are intended to increase transparency and reliability of FS to the users which is of paramount important considering the investor confidence in FS is dwindling due to an increase in instances of fraud and non-compliance.



## CHALLENGES AND PRECAUTION IN PREPARATION OF STATUTORY AUDIT REPORT WHILE DEALING WITH LOANS/BORROWINGS UNDER COMPANIES ACT 2013 AND UNDER CARO 2020



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The audit of liabilities is primarily directed at ensuring that all known liabilities have been properly accounted for since material omission or misstatement of liabilities vitiates the true and fair view of the financial statements.

One may adopt the following checklist for Audit of Loans & Borrowings:

1. Whether the following aspects of internal control relating to loans and borrowings properly reviewed?
  - a) the borrowing powers and limits;
  - b) persons authorized and competent to borrow;
  - c) terms of borrowings;
  - d) procedure for ensuring compliance with relevant legal requirements/internal regulations
  - e) Any variations in the terms of loans and borrowings are truly approved/ratified in writing by the competent authority
  - f) Security offered against loans and borrowings is properly recorded and periodically reviewed
  - g) The records and documents are kept in proper custody and reviewed periodically
  - h) The system brings out all cases of non-compliance with terms and conditions including amounts of principal and/or interest that have become overdue
  - i) Confirmation of balances is obtained at periodic intervals and the discrepancies, if any, are duly investigated and reconciled
  - j) There is a proper procedure for year-end valuation of loans and borrowings, especially for those designated in foreign currencies
2. Whether the loans obtained within the borrowing powers of the entity?

Section 179 provides power to the Board of Directors to exercise all such powers, and to do all such acts and things, as the Company is authorized to exercise and do and also gives prescribed powers which any general meeting of the Company cannot invalidate the prior act of the Board.

Whereas Section 180 provides restrictions on the Powers of the Board and the transactions given in this Section are only valid with the consent of the company by a special resolution. Form MGT – 14 has to be filed with the ROC.

In case of private Company this section shall not apply.

However, the special resolution passed by the Company in the General meeting shall specify the total amount up to which monies may be borrowed by the Board of Directors.

### 3. Review of operations:

Any transaction susceptible of fraud to be directly reported to the RBI by auditors

Auditor to scrutinize bank statements, account transfers, cheque returns, withdrawals/deposits of cash, turnover in account, transfers to sister concerns (diversion of funds) etc.

Auditor should compare movement of stock and book debts month-on-month with turnover in account. Compare it with audited/unaudited accounts. Book Debt statement should be certified by a CA on quarterly basis.

## **Borrowings under CARO 2020**

### **Introduction:**

The Central Government, in exercise of the powers conferred, under sub-section (11) of section 143 of the Companies Act, 2013 (Act), issued the Companies (Auditor's Report) Order, 2020, (CARO 2020/Order) vide Order number S.O. 849(E) dated 25th February 2020 and was subsequently amended vide number S.O. 1219 (E) dated 24th March 2020, and was again amended vide number S.O. 4588 (E) dated 17th December 2020 to be finally applicable from 1st April 2021)

CARO 2020 has included additional reporting requirements after consultations with the National Financial Reporting Authority (NFRA). NFRA is an independent regulatory body constituted under section 132 of the Companies Act, 2013, for regulating the audit and accounting profession in India. The aim of CARO 2020 is to enhance the overall quality of reporting by the company auditors

### **Clauses dealing with Borrowings**

#### **Clause 3(ix)(a)**

*Whether the company has defaulted in repayment of loans or other borrowings or in the payment of interest thereon to any lender, if yes, certain details to be reported. [Paragraph 3(ix)(a)]*

Minor addition made "or in the payment of interest thereon"

Borrowings do not include public deposits as the reporting on public deposits is covered by clause 3(v) of the Order. Even preference share capital should not be considered as borrowings

The format prescribed by this clause also requires reporting on default in repayment of loans or other borrowings taken from the Government and / or interest thereon. The term "Government" means the Central Government, a State Government and its departments and a Union Territory and its departments but does not include Government Company Public Sector Undertaking, Boards, Authority, Corporation and Foreign Government.

The auditor should obtain the confirmation of the concerned lender as to the status of the loan account including the overdue position as at the balance sheet date.

Cases where the company might have submitted application for reschedulement/restructuring proposals to the lenders, which may be in different stages of processing. Submission of application for reschedulement/restructuring does not mean that no default has occurred. Accordingly, in such situations also the auditor should report the period of default and the amount of default. Where reschedulement of loan has been approved subsequent to the balance sheet date, the auditor should report the defaults during the year. However, he may mention this fact in the remarks column.

*Where the company has adequate balance in its current account on the due date of repayment of loan or payment of interest, but such date is either a public holiday or a bank holiday.*

If debited next day the auditor should not consider the same as default.

The auditor may come across a situation where there may be disputes between the company and the lender on certain issues relating to repayments. In such situations, the auditor should consider the prevailing terms and conditions only. However, he may give a brief nature of the dispute while reporting under this clause.

*What if loans/borrowings and/or interest are repayable on demand and no repayment terms have been specified in the agreement.*

Obtain a management representation letter confirming that such loans/ borrowings and/ or interest have not been demanded for repayment. The auditor should mention the same in the audit report.

*Whether the company is a declared wilful defaulter by any bank or financial institution or other lender; [Paragraph 3(ix)(b)] New Clause.*

The term 'lender' appearing in the RBI Circular covers all banks/ financial institutions to which any amount is due, provided it is arising on account of any banking transaction, including off balance sheet transactions such as derivatives, guarantee and letter of credit.

The auditor is required to report whether the company has been declared as a wilful defaulter by any bank or financial institution or any other lender – restricted to the relevant financial year under audit till the date of audit report. Government or government authorities by virtue of their powers, may be in a position to declare any borrower as a wilful defaulter. Refer to Master Circular of RBI dated July1, 2014 as updated from time to time.

1. Unit has defaulted in meeting its payment / repayment obligations to the lender even when it has the capacity to Honour the said obligations.
2. The unit has defaulted in meeting its payment / repayment obligations to the lender and has not utilised the finance from the lender for the specific purposes for which finance was availed of but has diverted the funds for other purposes
3. The unit has defaulted in meeting its payment / repayment obligations to the lender and has siphoned off the funds
4. The unit has defaulted in meeting its payment / repayment obligations to the lender and has also disposed off or removed the movable or immovable property given by him or it for the purpose of securing a term loan without the knowledge of the bank/lender.

**Clause 3(ix)(c) New Clause**

*Whether term loans were applied for the purpose for which the loans were obtained; if not, the amount of loan so diverted and the purpose for which it is used may be reported; [Paragraph 3(ix)(c)]*

This clause is applicable to “term loan” -have a fixed or pre-determined repayment schedule. In the common parlance period beyond 36 months are usually known as term loans.

Cash credit, overdraft and call money accounts/deposits are therefore not covered by the expression “Term Loans”.

**Clause 3 (ix)(d)**

*Whether funds raised on short term basis have been utilised for long term purposes, if yes, the nature and amount to be indicated; [Paragraph 3(ix)(d)]*

Investing money from overdraft facilities in long-term investments in shares of subsidiaries/associates/joint ventures or investing money raised from public deposits due for repayment in three years in a project whose pay-back period is ten years. Ideal management of funds borrowed – short term or short term usage and long term borrowing for long term usage If funds raised for short term is used for long term it is not a prudent policy.

It is clarified that current maturities of long-term loans which are included as current liabilities as per Schedule III to the Act, are to be treated as long term sources of funds for the purpose of reporting under this clause

Long term applications of funds include investment in property, plant & equipment, intangible assets, long-term investments in shares, debentures and other securities and other assets of similar nature, repayment of long-term loans and advances or redemption of long-term debt or securities, etc. Application of funds which is not long-term may be categorized as short-term application.

If Loan Term Investment is < Long Term Fund it is an indication that short-term funds have been used to finance the long-term assets of the company Current Ration less than 1 is also an indication that short term funds have been used to finance long-term assets of the company.

The reporting under this clause may be as follows: According to the information and explanations given to us, and the procedures performed by us, and on an overall examination of the financial statements of the company, we report that no funds raised on short-term basis have been used for long-term purposes by the company. An example of unfavourable reporting under this clause is as follows: According to the information and explanations given to us, and the procedures performed by us, and on an overall examination of the financial statements of the company, we report that the company has used funds raised on short-term basis aggregating to Rs. X crores for long-term purposes.

**Clause 3(ix)(e) New Clause**

*Whether the company has taken any funds from any entity or person on account of or to meet the obligations of its subsidiaries, associates or joint ventures, if so, details thereof with nature of such transactions and the amount in each case; [Paragraph 3(ix)(e)]*

Funds will include both long term and short-term funds Reporting under this clause would normally be required when the company has taken any funds from any entity or any person and has also granted loans or advances in the nature of loans to its subsidiaries, associate companies or joint ventures or has made further investments in such subsidiaries, joint ventures, or associate companies.

The auditor needs to consider new loans or advances given during the year, meeting the obligations of subsidiaries, joint ventures, or associate companies during the year and new investments (equity or debt investment) made during the year for the purpose of reporting under this clause. Therefore, if there are no such transactions during the year, the auditor may conclude that the company has not taken any funds from any such entities.

The Act or the Order does not define the word “obligation” .- in normal parlance, obligation means a debt security (such as a mortgage or corporate bond) or a commitment to pay a particular sum of money. Obligation of subsidiary, joint venture or associate would mean the amounts that such subsidiaries, joint venture or associate companies are required to pay themselves either to their vendors, lenders, employees, or statutory authorities. When a company pays these amounts on behalf of its subsidiaries, joint ventures or associate companies, the amount so paid is generally treated as an asset either as loan, advance, or other current/ non-current assets in the financial statements of the company.

It is possible that the financial statements of subsidiaries, joint ventures, and associates are audited by another auditor. In such cases, the principal auditor may consider seeking specific information from the auditors of the components in accordance with the guidance given in SA 600, “Using the Work of Another Auditor” and Guidance Note on Audit of Consolidated Financial Statements to enable him to report under this clause.

### **Clause 3(ix)(f)**

*Whether the company has raised loans during the year on the pledge of securities held in its subsidiaries, joint ventures or associate companies, if so, give details thereof and also report if the company has defaulted in repayment of such loans raised; [Paragraph 3(ix)(f)]*

If yes, give details of such loans; and Report if the company has defaulted in repayment of such loans raised. –Yes or No – nothing else

As the defaults are in any case required to be reported under clause 3(ix)(a) for all lenders. All loans taken during the year even if these have been repaid during the year. Further, reporting is required only in case of loans taken during the year, Loans taken in earlier years and outstanding as at the balance sheet date need not be reported. Default will include both repayment of principal and payment of interest. Covers cases where the securities have been evoked.

Verify the form CHG 1 and CHG 4 lodged with the ROC \ MCA while creating and releasing the charge.

The reporting under this clause may be as follows: According to the information and explanations given to us and procedures performed by us, we report that the company has not raised loans during the year on the pledge of securities held in its subsidiaries, joint ventures or associate companies.



## EVENTS IN RETROSPECT

Day & Date	Committee	Program Name	Moderator / Speaker	Attendance / Views
Friday, 5th August 2022 to Saturday, 6th August 2022.	RRC & PD Committee	1st GST RRC	<ol style="list-style-type: none"> <li>1. Prosecution and Recovery Provisions under GST, Rights of the Taxpayers and Chartered Accountants - Adv Mayank Jain Partner, Khaitan &amp; Co</li> <li>2. Future of GST Practice and role of tax technology - Adv Sandeep Pareek - Partner, BDO India LLP</li> <li>3. Practice avenues in Allied Laws (Customs, FTP etc.) CA Asif Mansoor Principal Associate - Economic Laws Practice</li> <li>4. Assorted sector specific case studies - CA Sunil Gabhawalla</li> </ol>	35 participants



## EVENTS IN RETROSPECT

Day & Date	Committee	Program Name	Moderator / Speaker	Attendance / Views
Sunday, 21st August 2022	50Year Celebration Committee	Public Program on Will, Nomination and Succession Planning as part of Financial Awareness Mission jointly held with Shri KVO Borivali Jain Mahajan	CA Toral Shah, Partner at GBCA & Associates LLP	190

