



# Do's and Don't in Company Audits



CA. Vishal P. Doshi

# Before the audit



Appointment letter & ADT – 1



Communication with previous auditor (if required)



Engagement letter



Memorandum & articles of association



Materiality limits



Compliance checklist

# During the audit



 Accounting Standards – recognition, measurement and disclosures

 Standards on Auditing – mandatory for auditor

 Compliance with Companies Act, 2013 & related rules

 Verifying provisions of Income Tax Act, 1961

 Labour law compliances

 Internal Financial Controls over Financial Reporting



## Schedule III

- » Division I - Financial Statements for a company whose Financial Statements are required to comply with the ***Companies (Accounting Standards) Rules, 2006***
- » Division II - Financial Statements for a company whose financial statements are drawn up in compliance of the ***Companies (Indian Accounting Standards) Rules, 2015***
- » Division III - Financial Statements for a ***Non-Banking Financial Company (NBFC)*** whose financial statements are drawn up in compliance of the ***Companies (Indian Accounting Standards) Rules, 2015***

Requirements of the Act and/ or the notified Accounting Standards will prevail over the Schedule.

There is an explicit requirement to use the same unit of measurement uniformly throughout the Financial Statements and notes thereon.



# Small and Medium Companies

“Small and Medium Sized Company” (SMC) means, a company-

- i. whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;
- ii. which is not a bank, financial institution or an insurance company;
- iii. whose turnover (excluding other income) does not exceed rupees fifty crore in the immediately preceding accounting year;
- iv. which does not have borrowings (including public deposits) in excess of rupees ten crore at any time during the immediately preceding accounting year; and
- v. which is not a holding or subsidiary company of a company which is not a small and medium-sized company.



# Small and Medium Companies

- » An existing company, which was previously not SMC and **subsequently becomes SMC**, shall **not be qualified for exemption or relaxation** until the company **remains SMC for two consecutive accounting periods**.
- » SMC which does not disclose certain information pursuant to the exemptions or relaxations given to **it shall disclose (by way of a note to its financial statements) the following:**

“The Company is a Small and Medium Sized Company (SMC) as defined in the General Instructions in respect of Accounting Standards notified under the Companies Act, 1956. Accordingly, the Company has complied with the Accounting Standards as applicable to a Small and Medium Sized Company.”



# Initial Document Requirements

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Organogram / authorisation matrix / contact person(s)

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Update on products / locations / operations / capex

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Addition / liquidation / change in status of entities in the group

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Master data from MCA website

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Computation of total income & Income tax return for previous year

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Minutes of Board & General Meetings

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Statutory Registers

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MBP-1

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Trial Balance



# Forms filed during the year

CRL-1	Information to the Registrar by company regarding the number of layers of subsidiaries
CHG-1	Application for registration of creation, modification of charge (other than related to debentures)
CHG-4	Particulars for satisfaction of charge thereof
MSME	Half yearly return with the registrar in respect of outstanding payments to Micro or Small Enterprise
DPT-3	Return of deposits
PAS-3	Return of allotment
MGT-14	Filing of Resolutions and agreements to the Registrar
MGT-15	Form for filing Report on Annual General Meeting
AOC-5	Notice of address at which books of account are maintained
MR-1	Return of appointment of MD/WTD/Manager
MGT-4	Form for filing annual return by a company
AOC-4	Form for filing financial statement and other documents with the Registrar

# Current / Non-current classification

All items of inventory which may be consumed or realized within the company's normal operating cycle should be classified as current even if the same are not expected to be so consumed or realized within twelve months after the reporting date.

Any liability, pertaining to which the company does not have an unconditional right to defer its settlement for at least twelve months after the Balance Sheet/reporting date, will have to be classified as current.

A company also needs to classify its employee benefit obligations as current and non-current categories.

Capital advances should be treated as non-current assets irrespective of when the Property, Plant and Equipment and intangible assets are expected to be received and should not be classified as short term / current.



# Share Application Money

- » Share Application money pending allotment is to be disclosed as a separate line item on the face of Balance Sheet **between “Shareholders’ Funds” and “Non-current Liabilities”**.
- » Share application money **not exceeding the issued capital** and to the extent **not refundable** is to be disclosed under this line item.
- » If the company’s **issued capital is more than the authorized capital** and **approval of increase in authorized capital is pending**, the amount of share application money received **over and above the authorized capital** should be shown under the head **“Other Current Liabilities”**.
- » Various disclosure requirements (under Equity or Current Liabilities)



# Share Application Money

- » To allot the securities against the Share Application money received **within 60 days**, else the whole application money is required to be **refunded within 15 days** from the date of completion of 60 days failing which it shall be liable to repay that money with interest @ 12% p.a. from the expiry of the 60<sup>th</sup> day.
- » Further as per **Companies (Acceptance of Deposit) Rules, 2014**, from the 76<sup>th</sup> day **such amount shall be treated as a deposit** under these rules.
- » **Any adjustment of the amount for any other purpose shall not be treated as refund.**



# Borrowings

- » Schedule III stipulates that the nature of security shall be **specified separately in each case**. A **blanket disclosure of different securities covering all loans classified** under the same head such as 'All Term loans from banks' **will not suffice**.
- » Where **one security is given for multiple loans**, the same may be **clubbed together** for disclosure purposes with adequate details or cross referencing.
- » When promoters, other shareholders or any third party have given any personal security for any borrowing, such as shares or other assets held by them, **disclosure should be made thereof**, though such **security does not result in the classification of such borrowing as secured**.



# Borrowings

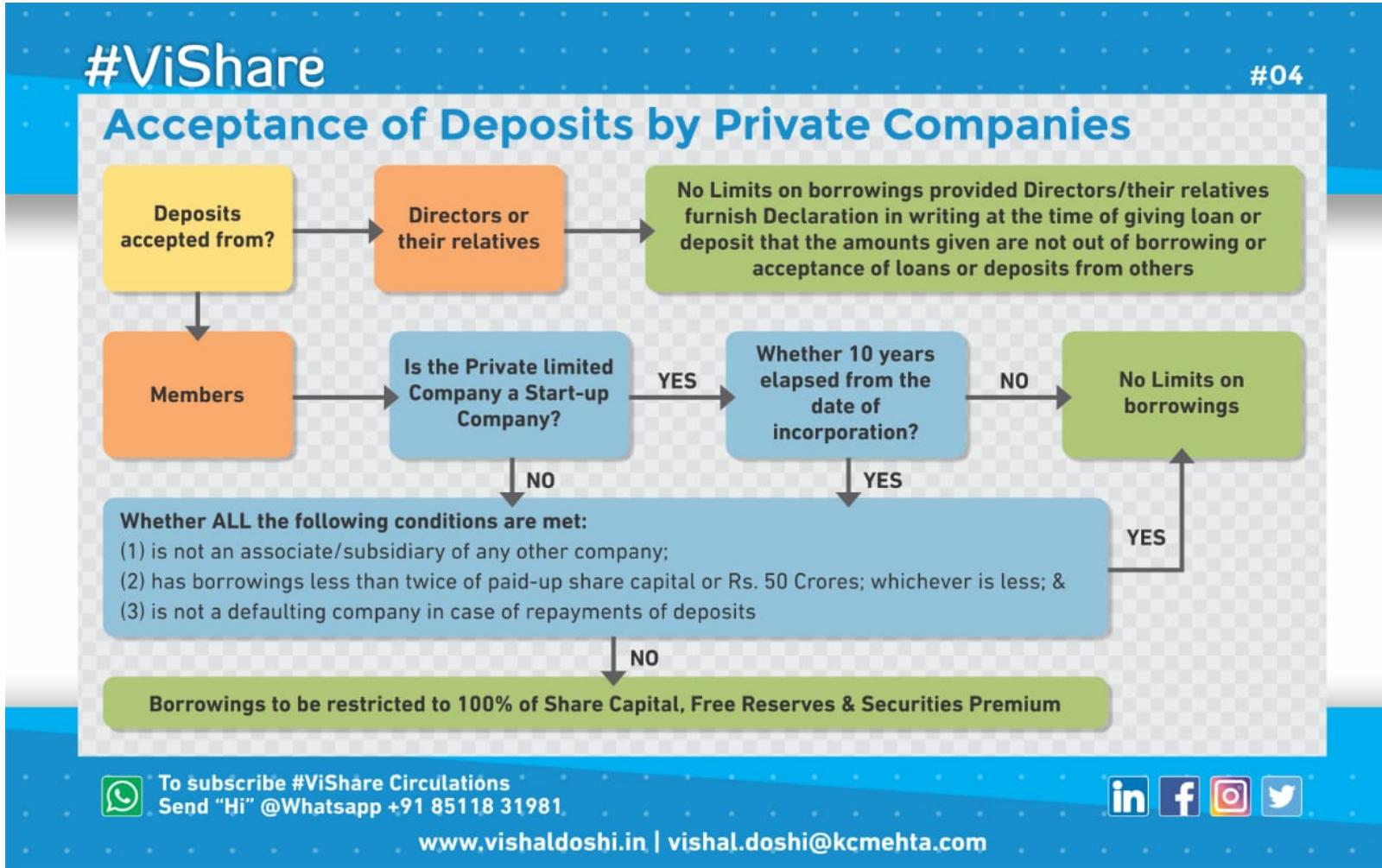
- » **Disclosure of repayment terms** should include the period of maturity with respect to the Balance Sheet date, number and amount of instalments due, the applicable rate of interest and other significant relevant terms if any.
  - » **In case of prepayments, disclosure can be made as per sanctioned terms**
- » A company **need not disclose** information for **defaults other than** in respect of repayment of **loan and interest**.
- » **Details of any default** in repayment of loan and interest **existing as on the Balance Sheet date** needs to be disclosed. Any default that had occurred during the year and **was subsequently made good before the end of the year** does not need to be disclosed.



# Exempted Deposits

- » Company from any other company (such as ICD)
- » Receipts of amount from Director/ Relative of director out of own fund
- » Compulsorily convertible debenture which are convertible within 10 years (unsecured)
- » Secured debentures (including optionally, compulsory and Non convertible) are not deposits
- » Promoters of the company by way of unsecured loan -stipulation of any lending financial institution or a bank
  - » exemption shall be available only till the loans of financial institution or bank are repaid and not thereafter
- » Business Advance/ Deposit
  - » Advance for supply of good or services - supplied within 365 days
  - » Against immovable property - adjusted against such property in accordance with terms of agreement
  - » Security deposit for the performance of the contract
  - » Advance under long term projects for supply of capital goods

# Deposits by Private Companies

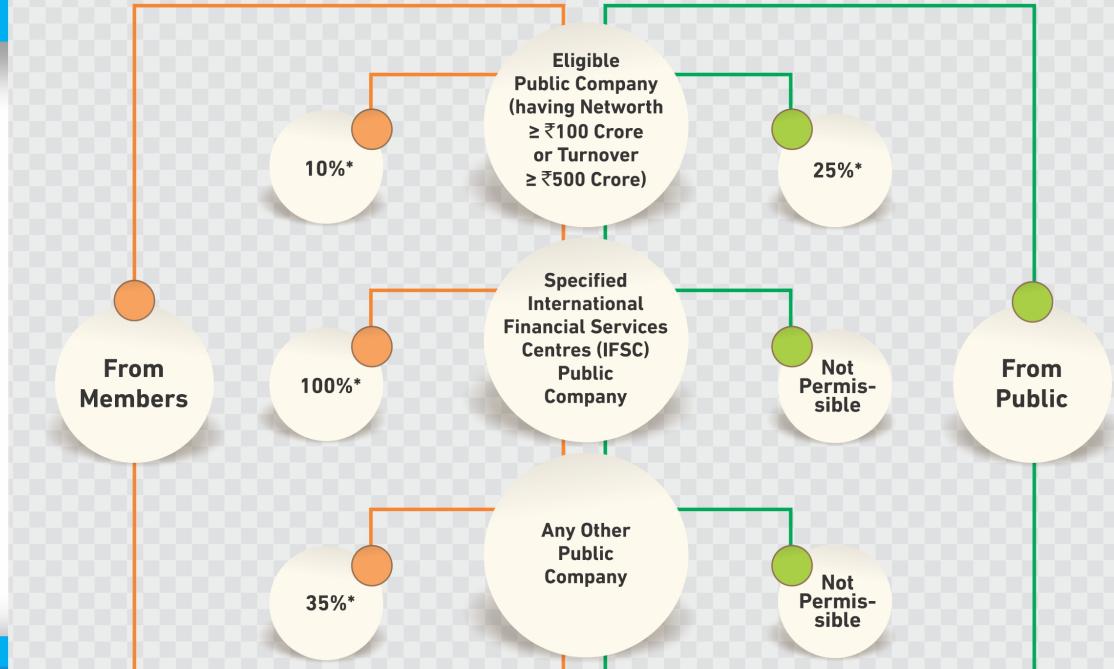


# Deposits by Public Companies

#ViShare

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## Acceptance of Deposits by Public Companies



\*Maximum permissible - of Paid-up Share Capital, Free Reserves & Securities Premium

In all Public Companies, Deposits can be accepted from Directors without any limits provided Directors furnish Declaration in writing at the time of giving loan or deposit that the amounts given are not out of borrowing or acceptance of loans or deposits from others



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# Provision vs. Liability

- » A provision is a liability which can be measured only by using a substantial degree of estimation.
- » A liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.
- » Provisions can be distinguished from other liabilities such as trade payables and accruals because in the measurement of provisions substantial degree of estimation is involved with regard to the future expenditure required in settlement.
- » For each class of provision, an enterprise should disclose:
  - (a) the carrying amount at the beginning and end of the period;
  - (b) additional provisions made in the period, including increases to existing provisions;
  - (c) amounts used (i.e. incurred and charged against the provision) during the period; and
  - (d) unused amounts reversed during the period.

A Small and Medium-sized Company, may not comply with paragraph above.

# Provision vs. Liability

Provision for	Classification
Audit fees	Current Liability
Expenses	Current Liability
Warranty	Current / Non-current Provision
Bonus	Current Liability
Leave / gratuity	Current / Non-current Provision
Doubtful debts	Adjust against Trade Receivable
Income tax	Current Liability



# Fixed Assets Property, Plant and Equipment

- » A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions... through business combinations and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.  
...the corresponding amounts (comparatives) for the immediately preceding reporting period for all items shown in the Financial Statements including notes shall also be given.
- » AS 6, Depreciation Accounting, has been withdrawn on 30/03/2016.
- » Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item should be depreciated separately.



# Investments

- » Non-current investments shall be classified as trade investments and other investments and further classified into investment property, investment in equity investments, preference shares, government or trust securities, debentures or bonds, mutual funds, partnership firms.
- » The term “trade investments” is defined neither in Schedule III nor in Accounting Standards. The term "trade investment" is, however, normally understood as an investment made by a company in shares or debentures of another company, to promote the trade or business of the first company.
- » Under each classification, details shall be given of names of the bodies corporate (indicating separately whether such bodies are (i) subsidiaries, (ii) associates, (iii) joint ventures, or (iv) controlled special purpose entities) in whom investments have been made.
- » In regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner) shall be given.



# Loans and Advances

- » Capital Advances are not be classified under Capital Work in Progress, since they are specifically to be disclosed under this para.
- » Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.
- » Other loans and advances should include all other items in the nature of advances recoverable in cash or kind such as Prepaid expenses, Advance tax, CENVAT / VAT / Service tax / GST credit receivable, etc. which are not expected to be realized within the next twelve months or operating cycle whichever is longer, from the Balance Sheet date.



# Loan to Directors

No company shall, directly or indirectly,

- » *Advance any loan, including any loan represented by a book debt, to any of its directors or to any other person in whom the director is interested or*
- » *Give any guarantee or*
- » *Provide any security in connection with any loan taken by him or such other person.*

Strict prohibition in case of the following individuals and firms:

- » *Any director of the company; or*
- » *Any director of its holding company; or*
- » *Any partner of any such director; or*
- » *Relative of any such director;*
- » *Any firm in which any such director is a partner; or*
- » *Any firm in which the relative of any such director is a partner*



# Loans to Directors

If

- a) A special resolution is passed by the Company in general meeting; and
- b) The loans are utilised by the borrowing company for its principal business activities.

then a Company *can advance any loan or give any guarantee or provide any security in connection with any loan taken by*

- (a) *any private company of which any such director is a director or member;*
- (b) *any body corporate at a general meeting of which not less than 25% of the total voting power may be exercised or controlled by any such director, or by two or more such directors, together; or*
- (c) *any body corporate, the Board of directors, managing director or manager, whereof is accustomed to act in accordance with the directions or instructions of the Board or any director or directors, of the lending company.*



# Loan and Investment by Company

No company shall directly or indirectly —

- (a) give any loan to any person or other body corporate;
- (b) give any guarantee or provide security in connection with a loan to any other body corporate or person; and
- (c) acquire by way of subscription, purchase or otherwise, the securities of any other body corporate,

exceeding sixty per cent of its paid-up share capital, free reserves and securities premium account or one hundred per cent of its free reserves and securities premium account, whichever is more.



# Revenue

- » Revenue from operations needs to be disclosed separately as revenue from (a) sale of products, (b) sale of services and (c) other operating revenues.
- » Other operating revenue would include Revenue arising from a company's operating activities, i.e., either its principal or ancillary revenue-generating activities, but which is not revenue arising from the sale of products or rendering of services.
  - » profit on sale of Property, Plant and Equipment should be classified as other income
  - » sale of manufacturing scrap arising from operations for a manufacturing company should be treated as other operating revenue since the same arises on account of the company's main operating activity.
  - » net foreign exchange gain should be classified as Other Income because such gain or loss arises purely on account of fluctuation in exchange rates and not on account of sale of products or services rendered, unless the business of the company is to deal in foreign exchange.

'Other Income' shall be classified as: (a) Interest Income (in case of a company other than a finance company); (b) Dividend Income; (c) Net gain / loss on sale of investments; (d) Other non-operating income (net of expenses directly attributable to such income).



# Unbilled revenue vs. WIP

- » Applicable to contracts where revenue is recognised
  - » over time (PoCM)
  - » at fixed intervals but not coinciding with period end
- » Unbilled revenue if any of the following is satisfied:
  - » the customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs;
  - » the entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or
  - » the entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date.
  - » if an entity determines that another entity would not need to substantially re-perform the work that the entity has completed to date if that other entity were to fulfil the remaining performance obligation to the customer.
- » Unbilled revenue with profit / WIP at lower of cost or NRV



# Incoterms 2020

EXW – Ex works	FCA – Free Carrier FAS – Free Alongside Ship FOB – Free On Board	CFR – Cost and Freight CIF – Cost, Insurance and Freight CPT – Carriage Paid To CIP – Carriage & and Insurance Paid	DAP – Delivered At Place DPU – Delivered at Place Unloaded DDP – Delivered Duty Paid
<ul style="list-style-type: none"><li>Seller makes the goods available to the Buyer at the delivery point indicated by the Seller</li><li>Seller is not obligated to perform customs or export clearance and does not bear the risk and costs of loading</li></ul>	<ul style="list-style-type: none"><li>Seller is responsible for export customs clearance</li><li>Seller does not pay transportation and insurance costs</li></ul>	<ul style="list-style-type: none"><li>Seller is responsible for export customs clearance</li><li>Seller arranges the transport contract with the forwarder</li><li>All costs after loading are the responsibility of the Buyer</li></ul>	<ul style="list-style-type: none"><li>Seller is obligated to deliver the goods to a specific place on the Buyer's side after the port of destination</li></ul>

# Transfer of risk

## Incoterms 2020



# #ViShare

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## Cut off Procedures

### Purchase of Goods

Goods received after end of year/period  
(Inco-Terms: EXW, FCA, FAS, FOB, CFR, CIF, CIP, CPT)

**Recognition in Balance Sheet**

- ✓ 01 Inventory as Raw Material / Traded Goods in Transit
- ✓ 02 Trade Payables / Creditors

**Measurement**

- ✓ 01 Invoice Value (in case of imports: foreign currency translated into INR)  
+  
All directly attributable costs from seller's premises / port to location of consignment on cut-off date
- ✓ 02 Lower of Cost or Net Realisable Value (subject to Para 24 of AS-2 and Para 32 of Ind AS 2)

Impact on Profit or Loss will be Nil

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## Cut off Procedures

### Sale of Goods

Bill of Lading / receipt of goods after end of year/period  
(Inco-Terms: FCA, FAS, FOB, CFR, CIF, CIP, CPT)

**Recognition in Balance Sheet**

- ✓ 01 Inventory as Finished Goods in Transit
- ✓ 02 Reversal of Trade Receivables / Debtors (if sale has been recognized)

**Measurement**

- ✓ 01 At manufacturing cost similar to other Finished Goods  
+  
All directly attributable costs from factory / warehouse to location of goods on cut off date (already debited to Statement of Profit & Loss)
- ✓ 02 Lower of Cost or Net Realisable Value

- If inventory has already been recognized at cost, there will be no impact on Profit or Loss
- If sales has been recognized, then sale and profit / loss thereon will be derecognized



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# Current tax

- » Any interest on shortfall in payment of advance income-tax is in the nature of finance cost and hence should not be clubbed with the Current tax. The same should be classified as Interest expense under finance costs. However, such amount should be separately disclosed.
- » Any penalties levied under Income tax laws should not be classified as Current tax. Penalties which are compensatory in nature should be treated as interest and disclosed in the manner explained above. Other tax penalties should be classified under other expenses.
- » Excess/Short provision of tax relating to earlier years should be separately disclosed.

The Micro, Small and Medium Enterprise Development (MSMED) Act, 2006 contains provisions of Delayed Payment to Micro and Small Enterprise (MSEs). (Section 15- 24).

»

As per section 15 & 16 of the above act

»

**Liability of buyer to make payment** -Where any supplier supplies any goods or renders any services to any buyer, the buyer shall make payment therefor on or before the date agreed upon between him and the supplier in writing or, where there is no agreement in this behalf, before the appointed day:

Provided that in no case the period agreed upon between the supplier and the buyer in writing shall exceed forty-five days from the day of acceptance or the day of deemed acceptance.

»

**Date from which and rate at which interest is payable** - Where any buyer fails to make payment of the amount to the supplier, as required under section 15, the buyer shall, not notwithstanding anything contained in any agreement between the buyer and the supplier or in any law for the time being in force, be liable to pay compound interest with monthly rests to the supplier on that amount from the appointed day or, as the case may be, from the date immediately following the date agreed upon, at three times of the bank rate notified by the Reserve Bank.

»

- » **Appointed date** means means the day following immediately after the expiry of the period of fifteen days from the day of acceptance or the day of deemed acceptance of any goods or any services by a buyer from a supplier.
- » **The day of acceptance** means,—
  - » (a) the day of the actual delivery of goods or the rendering of services; or
  - » (b) where any objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of the delivery of goods or the rendering of services, the day on which such objection is removed by the supplier;
- » **The day of deemed acceptance** means, where no objection is made in writing by the buyer regarding acceptance of goods or services within fifteen days from the day of the delivery of goods or the rendering of services, the day of the actual delivery of goods or the rendering of services;



# Other Important matters

- » Reclassification of exchange loss as borrowing cost in case of foreign currency borrowings
- » Restatement of advances in foreign currency
- » Scrutiny of legal & professional expenses
- » Balance of borrowings vis-à-vis finance cost
- » Payments are bill by bill or lumpsum / on account
- » External confirmations & subsequent collections
- » Credit amounts in debit ledgers & vice-versa
- » ICDS impact & adjustments
- » Cash Flow Statement
- » Tax Reconciliation

# After the audit



Obtain Management Representation Letter



Generate UDIN (preferably on same day)



Scan all important documents



Keep original financial statements in permanent file



Raise invoice



Collect fees



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