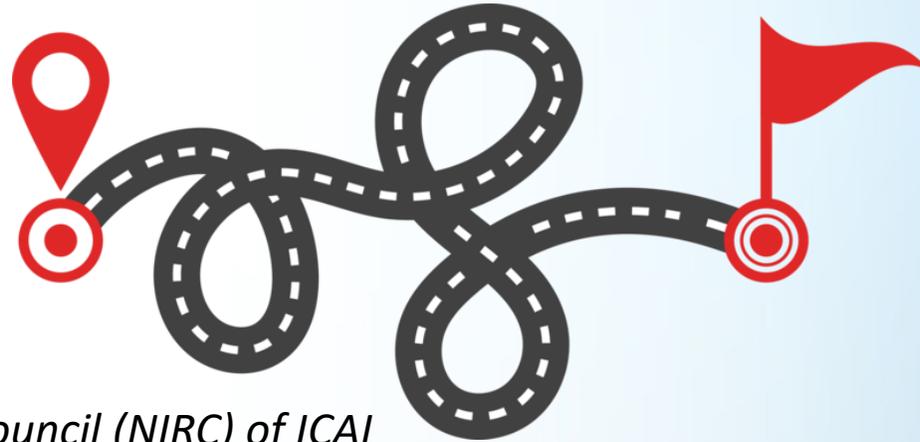


How to Handle Regulatory Risk of Action by NFRA, SFIO, ED, SEBI or CBI

Responsibility of Auditors - Expectations GAP



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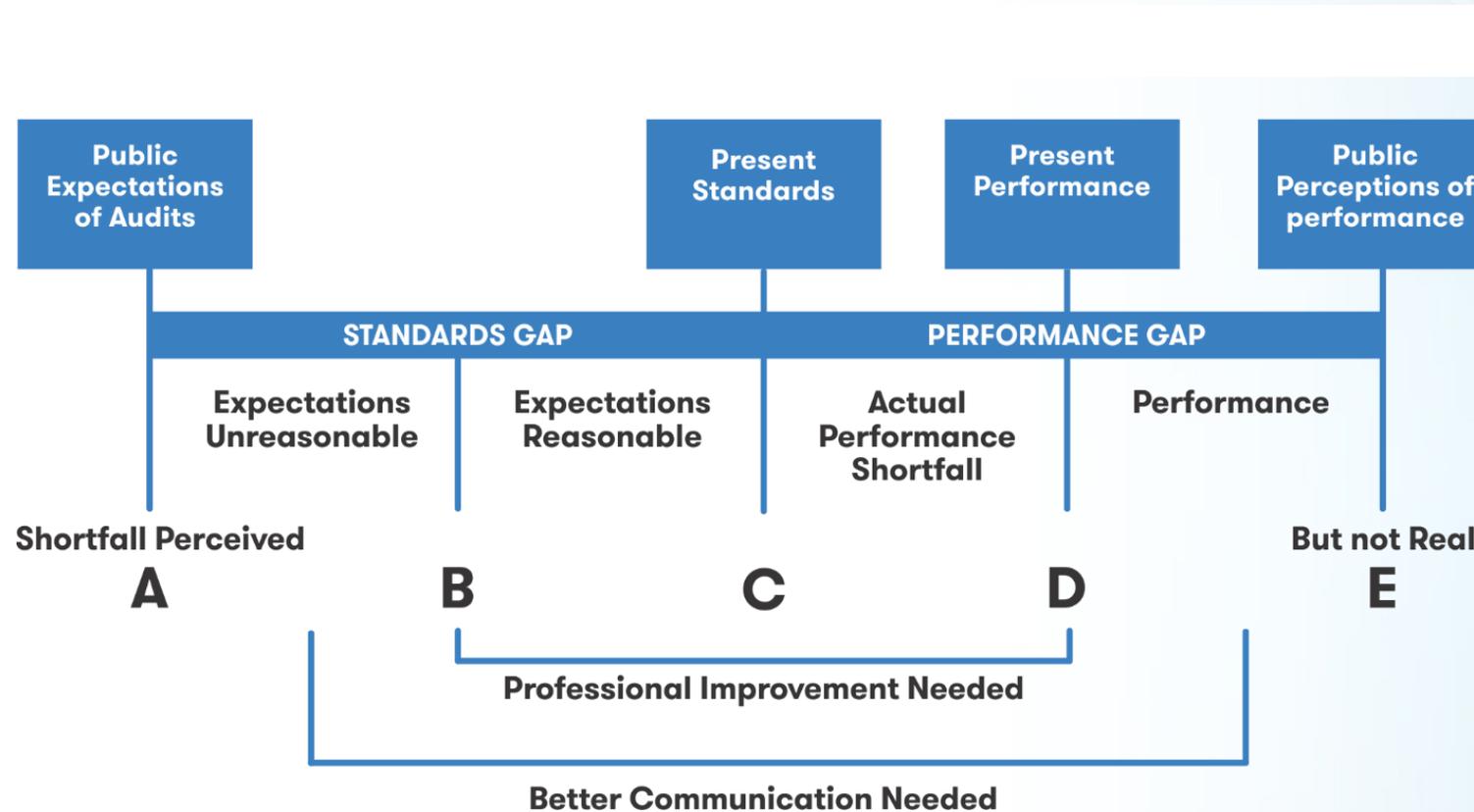
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Components of the **Audit Expectations Gap**



- The figure represents the full gap possible between the highest expectations of audits (point A) to public perceptions of what audits actually seem to provide (point E)
- Point C represents auditor performance and financial information quality called for by present standards
- The line segment A to C represents public expectations that go beyond existing auditing and accounting standards
- The line segment C to E represents public perceptions that auditor performance or audited financial information falls short of what is required by existing standards



Components of the **Audit Expectations Gap**

Perceived performance ← **Gap** → Society's expectation of auditors

Performance gap	Standard gap	Reasonableness Gap
Reasonable expectation of auditor performance	Reasonable expectation of standard	Unreasonable expectations
Reasons of Audit Expectation Gap		
<ul style="list-style-type: none"> • Fraud Prevention • Check Fund Diversion • Check Misuse of Resources • Check Financial Mismanagement • Independence • No non-audit services • Integrity • Clear communication by auditors 	<ul style="list-style-type: none"> • To concentrate on substantive audit procedures • Documentation requirement to reduce substantially <ul style="list-style-type: none"> - hard copy of major audit evidences - soft copy additional • Rule based standard where principle based not working adequately e.i. sampling , confirmation • CFO/CEO to be responsible for efficacy of audit • Lack of sufficient standards • Existing insufficient/ inappropriate standards regarding Auditor responsibilities for detection of fraud and illegal acts 	<ul style="list-style-type: none"> A) Over-expectation of audit performance <ul style="list-style-type: none"> • Users' over expectation of Audit <ul style="list-style-type: none"> - Fraud cannot be 100% prevented - Auditors do not witness physical operations - Time, resources and cost constraint - rely on documents - huge data, widespread operations - Lack of Audit trail - software complexity and unintegrated modules B) Over - expectation of standards <ul style="list-style-type: none"> • Over expectations of users to auditor performances • Users unawareness of audit responsibilities and limitations C) Miscommunication of users <ul style="list-style-type: none"> • Misunderstanding of users • Accounting disclosures and notes to accounts are complex for most of the stakeholders • Misinterpretation of users

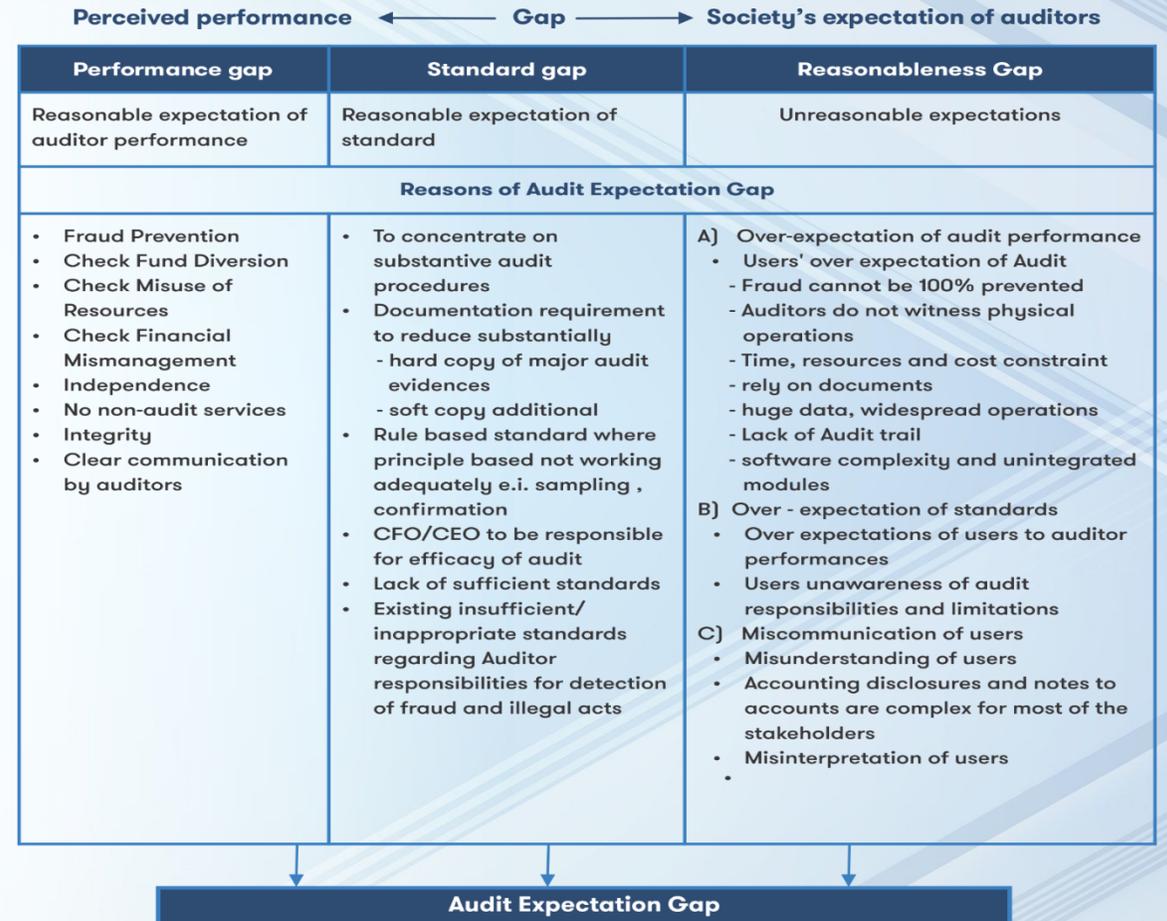
↓ ↓ ↓
Audit Expectation Gap



Performance Gap - Reasonable Expectation of Auditor Performance

Reasons of Audit Expectation Gap

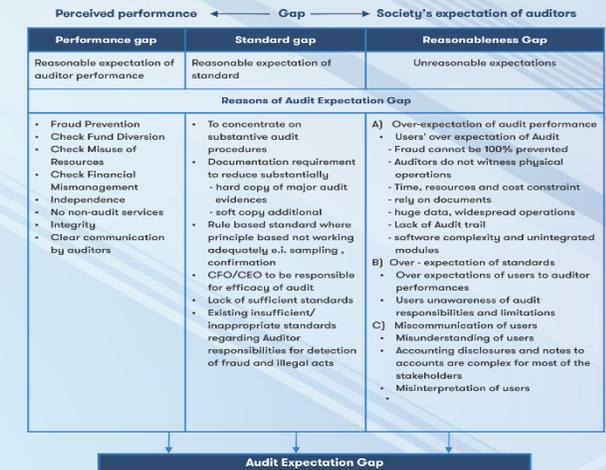
- Fraud Prevention
- Check Fund Diversion
- Check Misuse of Resources
- Check Financial Mismanagement
- Independence
- No non-audit services
- Integrity
- Clear communication by auditors



Standard Gap - Reasonable expectation of Standards

Reasons of Audit Expectation Gap

- To concentrate on substantive audit procedures
- Documentation requirement to reduce substantially
- Hard copy of major audit evidences
- Soft copy additional
- Rule based standard where principle based not working adequately i.e., sampling, confirmation
- CFO/CEO to be responsible for efficacy of audit
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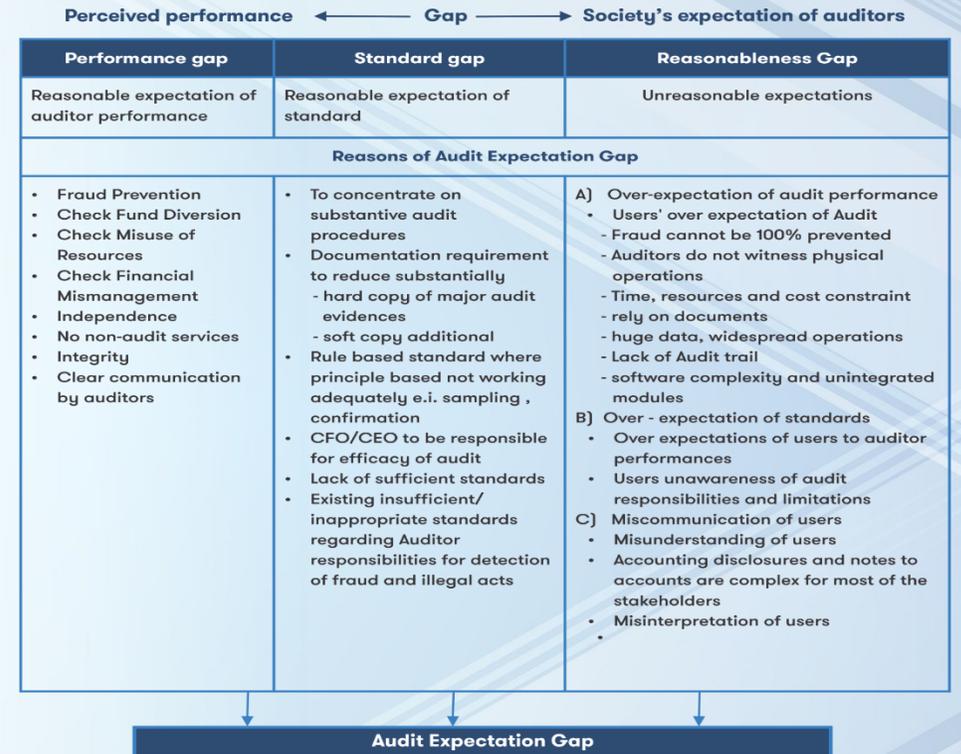


Reasonableness Gap- Unreasonable expectations

Reasons of Audit Expectation Gap

A. Over-expectation of audit performance

- User's over expectation of Audit
- Fraud cannot be 100% prevented
- Auditors do not witness physical operations
- Time, resources and cost constraint
- Rely on documents
- Huge data, widespread operations
- Lack of Audit trail
- Software complexity and unintegrated modules



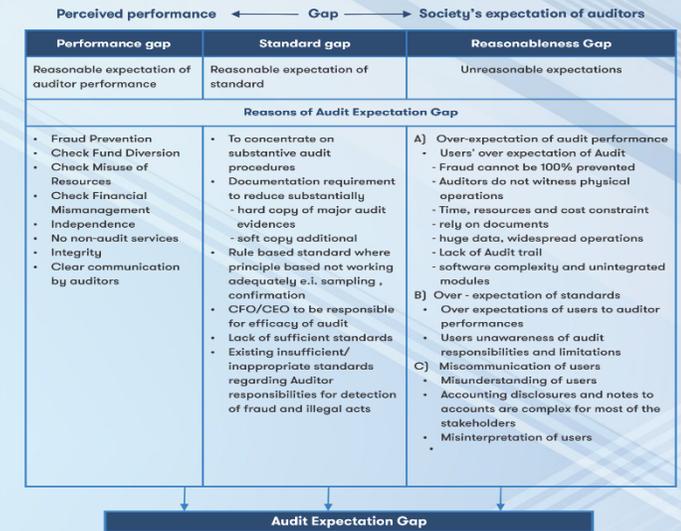
Reasonableness Gap- **Unreasonable expectations**

B. Over-expectation of standards

- Over Expectations of users to auditor performances
- Users unawareness of audit responsibilities and limitations

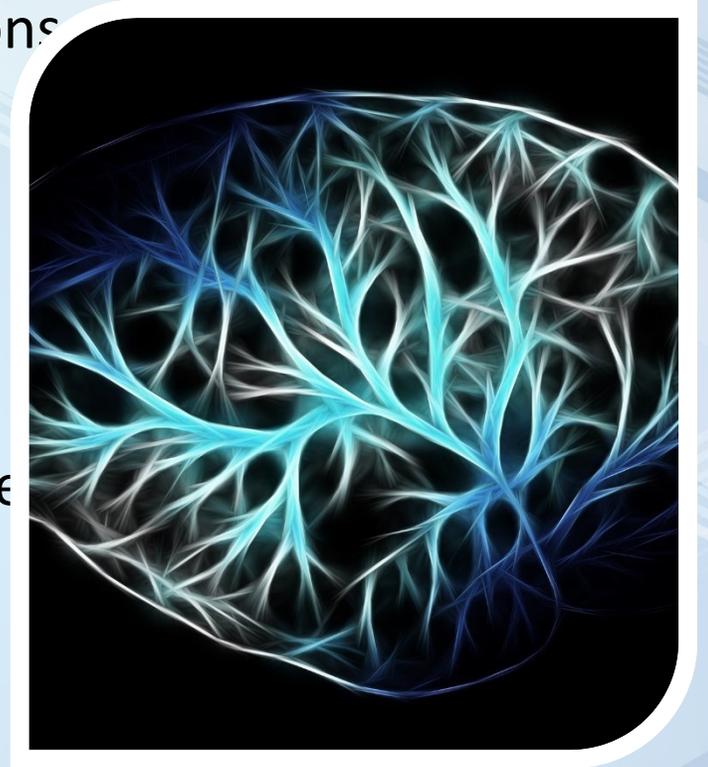
C. Miscommunication of users

- Misunderstanding of users
- Accounting disclosures and notes to accounts are complex for most of the stakeholders
- Misinterpretation of users



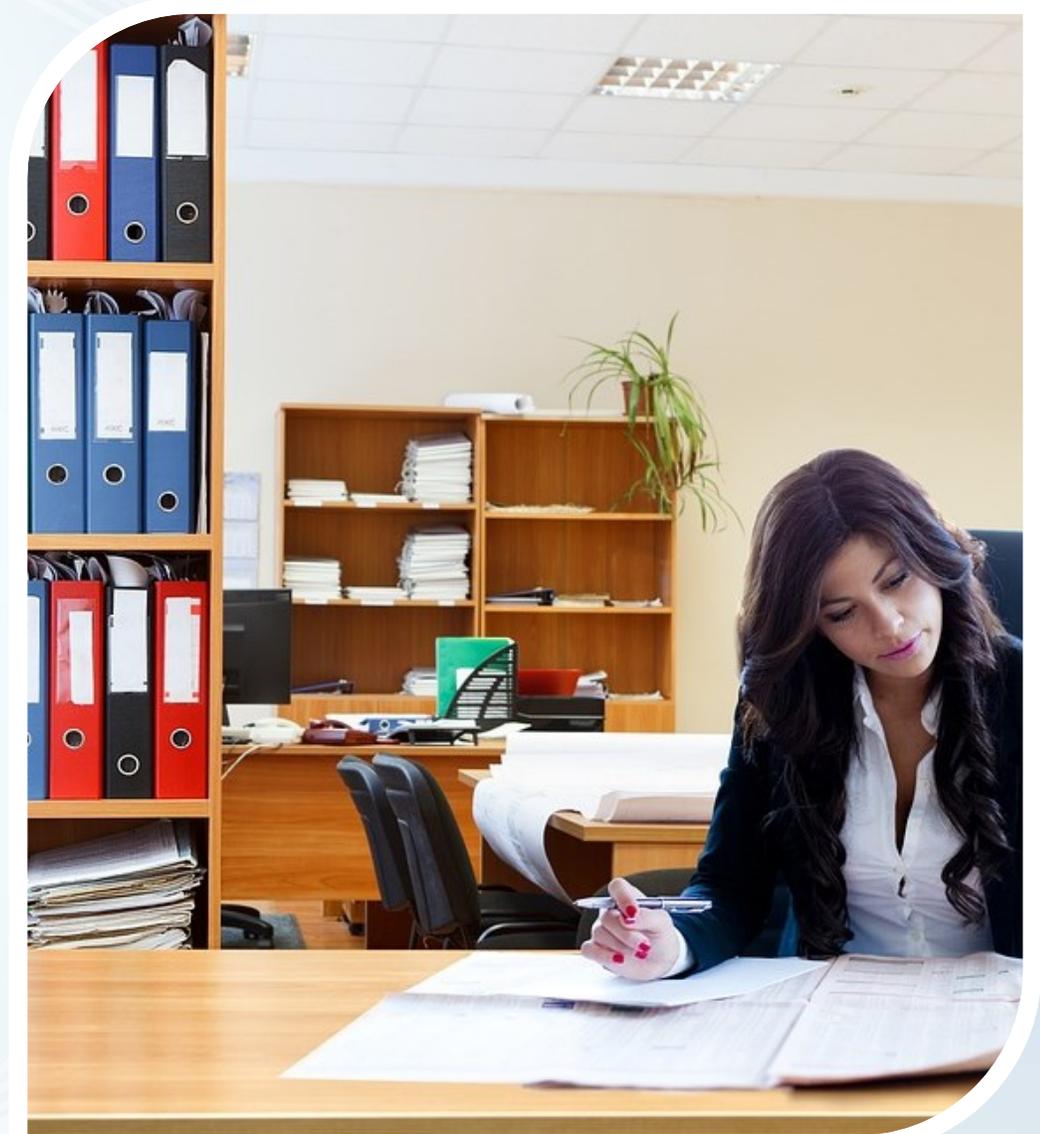
Audit - Important Areas of Concern

- ❖ Loans and Advances to related parties- other transactions
- ❖ Existence and realisable value
 - Debtors
 - Fixed Assets
 - Inventories
 - Investments- Substantial erosion of value by investee
 - Loans and advances
- ❖ Fraud by the company management
- ❖ Diversion of funds and resources
- ❖ Non provision of liabilities (claimed as contingent) and non disclosure of Commitments
- ❖ Extending of Unsecured loan- with or without interest



Audit - Important Areas of Concern

- ❖ Investment in companies do not have any connection with business of the investing company
- ❖ Unsupported expenses
- ❖ Inflated sale and Purchases
- ❖ Financial Mismanagement- Overleverage, Debt equity ratio to consider investment made
- ❖ Management Judgment on various business and operational decisions
- ❖ Lack of integrity and commitment to fairness



Government Expectations

❖ 1st July, 2017 at ICAI Event, Prime Minister Shri Narendra Modi pointed out expectations:

- CA is Responsible for economic health of the society and country
- Needs Innovation in technology and audit tools
- Training to excel beyond Global Benchmarks
- Live for country, society and not for client only
- Encourage clients to be fair, honest and deal with stakeholders with integrity
- To isolate and facilitate punishment to manipulators and to those who support them
- Educate clients to achieve growth and prosperity being on right path
- Audit report not to hide important facts- to report clearly without fear or favour
- Manipulators dupe investors and depositors- Audit to check - to perform diligently
- Duty at the right time, in the right manner and right direction
- Strong businesses lead to sustained growth and a strong economy.

❖ 21st November, 2019 at CAG Event: Core values of audit to be preserved - Latest audit software and tools – to be efficient and effective



What is Audit?

An audit is an independent examination of financial information of any entity , whether profit oriented or not, and irrespective of its size and legal form, when such an examination is conducted with a view to express an opinion thereon.

Auditor to conduct audit in accordance with the Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013.

As part of an audit in accordance with SAs, auditor exercise professional judgment and maintain professional skepticism throughout the audit. Auditor also:

- ❖ Identify and assess the risks of **material misstatement** of the financial statements, whether due to fraud or error,
- ❖ Design and perform **audit procedures** responsive to those risks, and
- ❖ Obtain **audit evidence** that is sufficient and appropriate to provide a basis for opinion.
- ❖ Obtain an **understanding of internal control** relevant to the audit in order to design audit procedures that are appropriate in the circumstances.
- ❖ Test **adequacy and operating effectiveness** of internal financial controls with reference to financial statements.



What is **Audit**?

- ❖ Evaluate the appropriateness of **accounting policies** used and the reasonableness of accounting **estimates** and related disclosures made by management.
- ❖ Conclude on the appropriateness of management's use of the **going concern** basis of accounting.
- ❖ Assess whether a **material uncertainty** exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern.
- ❖ Evaluate the overall **presentation, structure and content** of the financial statements, including the disclosures,
- ❖ Evaluate whether the financial statements represent the **underlying transactions and events** in a manner that achieves fair presentation.
- ❖ Complied with relevant **ethical requirements** regarding independence.
- ❖ **Communicate with management** about all relationships and other matters that may reasonably be thought to bear on independence, and where applicable, related safeguards.



Role of Auditors - **A factual brief**

As per Auditing Standards (which are mandatory in terms of the Companies Act, 2013 and are based on the International Standards on Auditing)

- ❖ Auditor is a **watch dog** and not a blood hound and is required to rely on documents and the submissions made, with professional scepticism unless he has reason to believe otherwise.
- ❖ **Test Check** of transactions- not expected to check 100 percent transactions.
- ❖ Financial Statements reflect **True and Fair view** and are free from material Misstatement.
- ❖ Examination and testing of **Internal Control**.
- ❖ Observe and verify **Documents and Facts**.
- ❖ **No physical Access** to Third parties- no physical access to suppliers, customers and other stakeholders records except to the extent available with the entity being subject to Audit.
- ❖ Auditors are **not expected to question the judgment** or management style or various business and operational **decisions**.
- ❖ The Auditors do ensure that books of accounts are reconciled with the returns filed with tax departments.



.....contd.

Role of Auditors - **A factual brief**

- ❖ **Physical Operations:** Auditors cannot physically verify the actual level of physical operations, movements of goods and services except to the extent those are recorded. The transactions or operations or facts which are not brought on record may not even come to the notice of Auditors except when he is able to have access to third party records and banking and other transactions undertaken by third parties.
- ❖ While Audit ensures substantial improvement in financial and fiscal discipline, Auditors can only report on efficacy of internal financial controls, even operations and operational controls are outside their ambit. The Auditors can review standard operating procedures and delegation of financial powers; however, the Audit presently can only suggest improvements and point out weaknesses in such control aspects.
- ❖ Auditor has to rely on agreements, invoices, entries in stock records, transactions as recorded for consumption and production, dispatch and different vouchers, supporting documents, explanations and books of accounts and records unless he has reason to believe otherwise. “Auditor is a watch dog and not a blood hound” and is required to rely on the submissions as made, with professional skepticism.



.....contd.

Role of Auditors - **A factual brief**

- ❖ The Audit is different as compared to investigation or Forensic undertaken by investigative agencies that work in the environment of suspicion and have to challenge each and every document or basis.
- ❖ Auditor has no access to how the goods or services or funds given or received from third parties are dealt with by the third parties in their books of accounts or businesses and the apparent agreement and purpose as on record of the client is actually final as far as Auditors are concerned. Auditor is actually required to undertake only a cold review and not a hot review by interacting with third parties or with their bankers and other stake holders.
- ❖ The Events occurring after the balance sheet date including the developments and facts arising later are not in the knowledge of the auditors at the time of audit.



Auditor's Ethical **Responsibility**

Integrity



**Professional
Competence
and Due Care**



**Professional
Approach
and behavior**



Objectivity



Confidentiality



Independence



Auditor Responsibility in **Code of Ethics**

Identification of Threats and Safeguards

- ❖ **Self-interest threats**- which may occur as a result of the financial or other interests of a professional accountant or of a relative;
- ❖ **Self-review threats**- which may occur when a previous judgment needs to be re- evaluated by the professional accountant responsible for that judgment;
- ❖ **Advocacy threats**- which may occur when a professional accountant promotes a position or opinion to the point that subsequent objectivity may be compromised;
- ❖ **Familiarity threats**- which may occur when, because of a relationship, a professional accountant becomes too sympathetic to the interests of others; and
- ❖ **Intimidation threats**- which may occur when a professional accountant may be deterred from acting objectively by threats, actual or perceived.



Auditor Responsibility towards **Independence**

Independence requires:

❖ **Independence of Mind-**

The state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

❖ **Independence in Appearance**

The avoidance of facts and circumstances that are so significant that a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised.

❖ **Conflict of Interest**

The significance of economic, financial and other relationships should also be evaluated in the light of what a reasonable and informed third party having knowledge of all relevant information would reasonably conclude to be unacceptable.

❖ members of **assurance teams**, firms and, when applicable, **network firms** be independent of assurance clients.



Auditor Responsibility As per **Companies Act**

Section 143(1)

Inquire into the following matters, namely:—

- whether **loans and advances** made by the company on the basis of security have been **properly secured** and whether the terms on which they have been made are prejudicial to the interests of the company or its members;
- whether transactions of the company which are represented **merely** by **book entries** are prejudicial to the interests of the company;
- where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other **securities** have been **sold** at a price less than that at which they were purchased by the company;
- whether loans and advances made by the company have been shown as **deposits**;
- whether **personal expenses** have been charged to revenue account;
- where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no **cash has actually been so received**, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading:

.....contd.



Auditor Responsibility As per **Companies Act**

Section 143(2)

The auditor shall make a **report** to the members of the company

- ❖ On the accounts examined by him and on every **financial statements**
- ❖ and to the best of his information and knowledge, the said accounts, financial statements give a **true and fair view** of the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year
- ❖ And such other matters as may be prescribed.

.....contd.



Auditor Responsibility As per **Companies Act**

Section 143(3)

The auditor's report shall also state—

- ❖ whether he has sought and obtained all the **information and explanations** which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;
- ❖ whether, in his opinion, **proper books of account** as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him
- ❖ whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;
- ❖ whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;
- ❖ whether, in his opinion, the financial statements **comply** with the **accounting standards**;
- ❖ the observations or comments of the auditors on **financial transactions** or matters which have any **adverse effect on the functioning of the company**;

.....contd.



Auditor Responsibility As per **Companies Act**

Section 143(3)

- ❖ whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;
- ❖ any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;
- ❖ whether the company has adequate **internal financial controls system** in place and the operating effectiveness of such controls;
- ❖ whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement
- ❖ whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;
- ❖ whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.



Auditor Responsibility As per **CARO**

Matters included

- ❖ Fixed Asset [clause 3 (i)]
- ❖ Inventory [clause 3 (ii)]
- ❖ Loan given by Company [Clause 3 (iii)]
- ❖ Loan to director and investment by the company [Clause 3 (iv)]
- ❖ Deposits [Clause 3 (v)]
- ❖ Cost Records [Clause 3 (vi)]
- ❖ Statutory Dues [Clause 3 (vii)]
- ❖ Repayment of Loan [Clause 3 (viii)]
- ❖ Utilization of IPO and further public offer [Clause 3 (ix)]
- ❖ Reporting of Fraud [Clause 3 (x)]
- ❖ Approval of managerial remuneration [Clause 3 (xi)]
- ❖ Nidhi Company [Clause 3 (xii)]
- ❖ Related Party Transaction [Clause 3 (xiii)]
- ❖ Preferential Allotment or Private Placement of shares or fully or partly convertible debentures [Clause 3 (xiv)]
- ❖ Non Cash Transaction [Clause 3 (xv)]
- ❖ NBFC Registration [Clause 3 (xvi)]



Auditor Responsibility As per **Standards on Auditing**

SA 200 - Overall Objective of the Independent Auditor and the conduct of an Audit in accordance with Standards on Auditing

In conducting an audit of financial statements, the overall objective of the auditor are:

- ❖ To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.
- ❖ To report on the financial statements, and communicate as required by the SA's, in accordance with the auditor's findings.

.....contd.



Auditor Responsibility As per **Standards on Auditing**

SA 700 – Forming an Opinion and Reporting on Financial Statements

Auditor objectives are

- ❖ To obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and
- ❖ To issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Auditor to conduct audit in accordance with the Standards on Auditing (SAs) specified under section 143(10) of the Companies Act, 2013.

As part of an audit in accordance with SAs, auditor exercise professional judgment and maintain professional skepticism throughout the audit. Auditor also:

- ❖ **Identify and assess the risks of material misstatement** of the financial statements, whether due to fraud or error,
- ❖ Design and perform audit procedures responsive to those risks, and
- ❖ Obtain audit evidence that is sufficient and appropriate to provide a basis for opinion.

.....contd.



Auditor Responsibility As per **Standard on Quality Control**

The firm should establish a system of quality control designed to provide:-

- ❖ Reasonable assurance that the firm and its personnel comply with professional standards and regulatory and legal requirements, and
- ❖ That reports issued by the firm or engagement partner(s) are appropriate in the circumstances.

Elements of a System of Quality Control:-

- ❖ Leadership responsibilities for quality within the firm.
- ❖ Ethical requirements.
- ❖ Acceptance and continuance of client relationships and specific engagements.
- ❖ Human resources.
- ❖ Engagement performance.
- ❖ Monitoring.

The quality control policies and procedures should be documented and communicated to the firm's personnel.



National Financial Reporting Authority

The National Financial Reporting Authority (NFRA) was constituted on 01st October, 2018 by the Government of India under Sub Section (1) of section 132 of the Companies Act, 2013

- ❖ An independent regulatory body for carrying out the functions *inter alia* monitoring compliance of accounting and auditing standards,
- ❖ Oversee the quality of service of the professions associated with ensuring compliance with such standards, suggest measures required for improvement in quality of service.
- ❖ It is a quasi-judicial body constituted under the provision of section 132 of the Act.

Functions and Duties of NFRA

- ❖ To make recommendation to the Central Government on **formulation of accounting/auditing policies/standards;**
- ❖ To monitor and **enforce the accounting and auditing standards compliance;**
- ❖ To **oversee the quality of service of the associated professions** ensuring compliance with such standards and suggesting improvement measures if required;
- ❖ Performing such other functions related to above functions.
- ❖ Power to investigate and disciplinary proceedings.
- ❖ Punishment for non compliance



Entities Governed by **NFRA**

- ❖ Companies whose securities are listed on any stock exchange in India or outside India;
- ❖ Unlisted public companies fulfilling any of the following criteria as on the 31st March of immediately preceding Financial Year:
 - having paid-up capital of not less than Rs. 500 crores; or
 - having annual turnover of not less than Rs. 1000 crores; or
 - having, in aggregate, outstanding loans, debentures and deposits of not less than Rs. 500 crores.
- ❖ Insurance companies, banking companies, companies engaged in the generation or supply of electricity
- ❖ Body corporate/companies/persons or any class of them referred by Central Government to the Authority in public interest;
- ❖ Foreign subsidiary(ies) and associate(s) of:
 - of the company or body corporate registered in India as referred in point (1) to (4) above; and
 - income or net worth exceeds 20% of the consolidated income or consolidated net worth of such company or the body corporate.



Powers of **NFRA**

- ❖ **Investigating into professional/other misconduct** committed by any member/firm of Chartered Accountants;
- ❖ **Power to impose penalty or debarring the auditors** or audit firm for minimum 6 months and up to 10 years from practicing audit profession;
- ❖ Same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit;
- ❖ The Authority may require the personal presence of the officers of the company or body corporate and its auditor in connection with the review of the financial statements.



NFRA Latest Action

Audit Quality Review

National Financial Reporting Authority has issued its Audit Quality Review Report (AQR) on statutory audit of ILFS Financial Services Limited (IFIN) for the financial year 2017-18 carried out by Auditors.

- ❖ The independence of the auditor was compromised by the provision of non-audit services for substantial fees.
- ❖ The Engagement Partner had signed the Audit Report without discharging most of the important duties.
- ❖ Professional scepticism is missing.
- ❖ Failed to appropriately deal with identification, categorization and minimization of Engagement risk.
- ❖ Accepted the explanations of the management which were clearly contrary to law.
- ❖ Did not adequately question the going concern assumption.
- ❖ Did not question the management and challenge the inflation of profit.
- ❖ Did not communicate any matter arising out of the audit.
- ❖ Engagement Quality Control Review has been shown to have been a complete sham.

NFRA has started examination of audit of all major companies where auditors have resigned.



Securities Appellate Tribunal's **Latest Action**

- ❖ The SEBI slapped a two-year ban on Price Waterhouse (PwC), from auditing any listed company in connection with PwC's role in the Satyam scam.
- ❖ Later, SECURITIES APPELLATE TRIBUNAL (SAT) quashed SEBI order and observed

.....“Therefore, the measure to be adopted by SEBI is remedial and not punitive”.....

.....“but in our view, banning an audit firm or an auditor from auditing the books of a listed Company or from certifying any report of a listed Company cannot be justified.”.....

.....“We may further point out that ICAI had initiated proceedings against the auditors under the CA Act and cancelled their license to practice as CA. Once their license has been cancelled, there was no need for SEBI to issue an order of debarment.”.....

- ❖ Supreme Court of India has stayed the Para 78 of the order containing aforesaid observations.



SEBI Latest Circular on **Resignation of Auditor**

The conditions to be complied with upon resignation of the statutory auditor of a listed entity/material subsidiary w.r.t. limited review / audit report as per SEBI LODR Regulations, are as under:-

- ❖ All listed entities/material subsidiaries shall ensure compliance with the following conditions while appointing/re-appointing an auditor:
 - If the auditor resigns within 45 days from the end of a quarter of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for such quarter.
 - If the auditor resigns after 45 days from the end of a quarter of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for such quarter as well as the next quarter.
 - Notwithstanding the above, if the auditor has signed the limited review/ audit report for the first three quarters of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for the last quarter of such financial year as well as the audit report for such financial year.

.....contd.



SEBI Latest Circular on **Resignation of Auditor**

Other conditions relating to resignation shall include:

- ❖ Reporting of concerns with respect to the listed entity/its material subsidiary to the Audit Committee:
 - In case of any concern with the management of the listed entity/material subsidiary such as non-availability of information / non-cooperation by the management which may hamper the audit process, the auditor shall approach the Chairman of the Audit Committee of the listed entity and the Audit Committee shall receive such concern directly and immediately without specifically waiting for the quarterly Audit Committee meetings.
 - In case the auditor proposes to resign, all concerns with respect to the proposed resignation, along with relevant documents shall be brought to the notice of the Audit Committee. In cases where the proposed resignation is due to non-receipt of information / explanation from the company, the auditor shall inform the Audit Committee of the details of information / explanation sought and not provided by the management, as applicable.

.....contd.



SEBI Latest Circular on **Resignation of Auditor**

Disclaimer in case of non-receipt of information:

- In case the listed entity/ its material subsidiary does not provide information required by the auditor, to that extent, the auditor shall provide an appropriate disclaimer in the audit report, which may be in accordance with the Standards of Auditing as specified by ICAI / NFRA.

In case the auditor is rendered disqualified due to operation of any condition mentioned in Section 141 of the Companies Act, 2013, then the provisions of this Circular shall not apply.



Bank Audit - Expectation from ICAI and RBI

- ❖ Number of Audited branches - Advances less than Rs. 20 crores- should be audited at least once in 2 years (not 5 years).
- ❖ Appointment for 5 years on the lines of Companies Act.
- ❖ Communication of Appointment - on conclusion of AGM –
- ❖ Scope of audit need to be substantially upgraded and expanded
 - Loan sanctioning and monitoring
 - Funds management
 - Fraud prevention
 - Borrower credibility and business review
 - Internal controls
 - NPA monitoring and restructuring,
 - Operational controls
 - A detailed transaction audit using audit software tools and analysis of exceptions reporting using software
- ❖ Auditor to formulate special audit methodology and sampling techniques.
- ❖ Audit in phases- interim reviews covering substantive testing of all areas and final audit covering both substantive and non-substantive testing procedures.
- ❖ Audit Fees- no rise in Bank Audit Fee for last over 10 years.
 - The fees for bank audit should be increased by 10% - 15% every year (including for the backlog period) to ensure that adequate qualitative time is spent.
 - The increase in scope also be considered for fee.



Bank Audit - **Expectation from ICAI and RBI**

- ❖ Basis of fee determination- deposits and non-fund based credit facility to be included as it causing lack of attention in these areas.
- ❖ Scope to Branch Auditor reporting to be enlarged.
- ❖ Branch Auditor role in monitoring of existence and realisibility of Stock, Debtors, advances and Fixed Assets of borrowers
- ❖ Team of 2-4 RBI Nodal Officers should be appointed in all banks to supervise audit activity on annual basis and contact information of same should be available to all auditors.
- ❖ Identification of manual activities having financial implications and its integration with Core Banking Solutions (CBS).
- ❖ Reporting provisions of Companies Act 2013 which are applicable to private banking companies, should be made applicable to nationalized banks, State Bank of India and Regional Rural Banks.
- ❖ The quality review board should review work of central statutory auditors on a mandatory basis at least once in three years. The cost of such review should be borne by Banks.
- ❖ Long Form Audit Report important points to be published.



Companies Comes Under The Ambit of - **NFRA**

- ❖ **Rule 3(1)(a):** companies whose securities are listed on any stock exchange in India or outside India;
- ❖ **Rule 3(1)(b):** unlisted public companies having paid-up capital of not less than rupees five hundred crores or having annual turnover of not less than rupees one thousand crores or having, in aggregate, outstanding loans, debentures and deposits of not less than rupees five hundred crores as on the 31st March of immediately preceding financial year;
- ❖ **Rule 3(1)(c):** Insurance companies, banking companies, companies engaged in the generation or supply of electricity, companies governed by any special Act for the time being in force or bodies corporate incorporated by an Act in accordance with clauses (b), (c), (d), (e) and (f) of sub-section (4) of section 1 of the Act;
- ❖ **Rule 3(1)(d):** Any body corporate or company or person, or any class of bodies corporate or companies or persons, on a reference made to the Authority by the Central Government in public interest;
- ❖ **Rule 3(1)(e):** a body corporate incorporated or registered outside India, which is a subsidiary or associate company of any company or body corporate incorporated or registered in India as referred to in clauses (a) to (d), if the income or net worth of such subsidiary or associate company exceeds twenty per cent. of the consolidated income or consolidated net worth of such company or the body corporate, as the case may be, referred to in clauses (a) to (d).



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

❖ **Mandatory Filing Compliance**

- **File NFRA-1:** NFRA Form 1 is an annual return form that is filed by the auditor of Indian body corporates or foreign companies that fall under rule number 3(3).
- **File NFRA-2:** Form NFRA-2 is an annual return that auditors of companies specified in Rule 3(1) of the National Financial Reporting Authority (NFRA) Rules, 2018, must file with NFRA, by November 30th of each year.



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

❖ **Strictly comply with Standards on Auditing and Accounting:**

- Maintain proper audit documentation.
- Perform sufficient audit procedures (NFRA checks audit working papers *in detail*).



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

❖ **Maintain detailed audit files:**

- Planning documents
- Risk assessments
- Materiality calculations
- Audit evidence collected
- Management representation letters
- Retention: Keep documents for at least 7 years.



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

Quality Review Systems

Implement internal quality control checks:

- EQCR: Engagement Quality Control Review for critical audits.
- Maintain an audit manual and peer review reports.



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

Transparency with NFRA

Respond properly to NFRA notices:

- Never ignore a NFRA email or notice.
- Respond professionally with proper explanations and documents.



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

Engagement Letter & Clear Communication

Always issue an Engagement Letter:

- Define the scope of work.
- Mention audit limitations clearly.
- **Communicate regularly** with Audit Committee/Board.



How Chartered Accountants Can Safeguard Against – **NFRA** **Actions**

Professional Skepticism

Apply "professional skepticism" genuinely:

- Question suspicious items.
- Document your concerns and how they were resolved.



Recommended **Course Of Action**

Extension of time whenever necessary:

It is always advisable to request an extension of time when required. This allows additional time to respond to allegations or to gather necessary information for a comprehensive and accurate reply.

Granting extensions ensures that the Noticee has a fair opportunity to present their case, promoting a thorough and just examination of the situation.



Recommended **Course Of Action**

Legal Validity to analyse the allegations:

One should assess the legal validity of the allegations made against them. It involves a careful examination of the legal grounds on which the accusations are based.

By scrutinizing the legal validity, the Noticee can identify any potential weaknesses in the allegations and formulate a well-founded response. It helps in building a strong defense against the charges.



Recommended **Course Of Action**

In case of NFRA, ask for stay orders

In the context of NFRA (National Financial Reporting Authority), the Noticee is recommended to seek stay orders. This involves requesting a temporary suspension or delay in the proceedings until certain conditions are met or issues are resolved.

Obtaining stay orders can provide the Noticee with a breathing space, allowing for a more thorough review of the case and preparation of a robust defense. It may prevent immediate adverse actions while the matter is being considered.



Recommended **Course Of Action**

Legal Consultancy:

The Noticee is advised to seek legal consultancy services. This involves obtaining professional legal advice from experts who can guide them through the complexities of the regulatory proceedings. Legal consultancy ensures that the Noticee has access to informed and expert guidance, helping them understand the legal implications of the allegations and navigate the regulatory process effectively.



Recommended **Course Of Action**

Internal Review and Remediation:

Conduct an internal review to identify any shortcomings in compliance and implement remedial actions or improvements to prevent future issues.

The internal review is a systematic examination of the organization's processes, practices, and documentation to identify any areas where compliance may have fallen short of regulatory requirements.



Recommended **Course Of Action**

Cooperate with Regulators

The Noticee should cooperate fully with the regulatory authorities during their investigation or inquiry or provide any additional information or clarification they may request.



Legal Provisions Relating To SFIO – Section 211 & Section 212 Of The Companies Act, 2013

Section 211 of the Companies Act, 2013 relates to the ***Establishment of Serious Fraud Investigation Office***. The section states that the SFIO is to be established by the Central Government for the purposes of investigating corporate frauds. The section also states that the office shall be led by a Director who shall at least be a Joint Secretary and must have expertise in corporate affairs. The section, further goes on to state that the Office shall include several experts of various fields such as banking, corporate affairs, taxation, forensic audits, capital markets, information technology, and law. These experts will also be appointed by the “Central Government”. The Government may hire other staff if needed.

Section 212 of the Companies Act, 2013 states that the Central Government has the authority to assign any investigation to SFIO on receipt of a report of Registrar, on intimation of special resolution passed by a company and its affairs are required to be investigated in public interest on request of any Department of the “Central Government”/ “State Government”.

Once assigned, no other agency can investigate the same case and they must send any related document to SFIO. SFIO, after investigation, must send a report to the Central Government within the specified time period. The section casts a duty upon the staff and the employees of the company investigated to provide all the necessary information. The section also authorizes the agency to arrest a person if suspected of committing the crime but he must be produced before the Magistrate within 24 hours. After investigation, SFIO is required to submit its findings to the “Central Government”, which can decide to take legal action against the company or its employees.



Legal Provisions Relating To SFIO – Section 211 & Section 212 Of The Companies Act, 2013

Potential Misuse Of The SFIO's Powers

- **The powers to SFIO are very wide.** The use of vague terms such as “**opinion**” or “**reason to believe**” makes the provisions vulnerable to misuse by the authorities. Such huge powers granted to SFIO have the potential to be misused for ulterior motives by the authorities. For example, under “Section 212” of “Companies Act”, it is the “opinion” of the “Central Government” that decides whether the case is to be assigned to SFIO or not. Mere opinion of the “Central Government” is enough to direct SFIO to investigate a case.
- It has also been pointed out that the power to arrest granted to the SFIO under Section 212(8) is also vulnerable to be misused. The investigation agency only has to have a “**reason to believe**” that the offence has been committed by such person to arrest him/her.



CIC Directs 'SFIO' To Publicly Disclose Entities And Individuals Approved For – **Action By MCA**

An RTI Applicant sought completed investigation reports and a list of companies subject to serious fraud investigations. The case revolves around the Right to Information Act (RTI Act) and Section 212(13) of the Companies Act, 2013.

The SFIO argues that the RTI request was too broad and did not specify the companies or the period for which information was sought. Also, the CPIO stated that SFIO submits its investigation report to the ministry, which then determines further action.

As per the Central Information Commission (CIC) Order dated March 5, 2025, The SFIO is directed to proactively disclose information regarding companies and individuals against whom the Ministry of Corporate Affairs (MCA) has approved action based on SFIO investigation reports. This information should be published on the SFIO website in accordance with Section 4 of the RTI Act.



For this Presentation and Other Presentations & Handbooks by CA. Vaibhav Jain

Please Visit - <https://www.cavaibhavjain.com/>



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THANK YOU

I am deeply grateful for your trust in me 🙏 and would appreciate your continued support as I strive to contribute further. *I am always here for any assistance or clarification you may need—whether personal or professional.*

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Feel free to reach out anytime, as I'm available **24/7** to support you! 🤝

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