

Companies (Auditor's Report) Order, 2016

The Ministry of Corporate Affairs (MCA) has by notification dated 29th March, 2016 issued 'The Companies (Auditor's Report) Order, 2016' (hereinafter referred to as 'CARO 2016') under section 143(11) of the Companies Act 2013 replacing 'The Companies (Auditor's Report) Order, 2015'.

APPLICABILITY OF CARO 2016

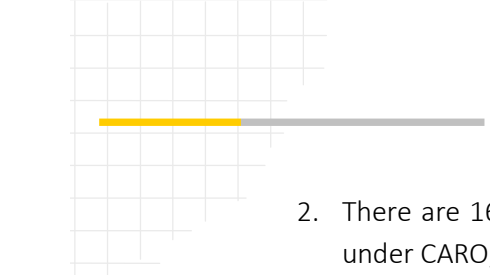
1. It is applicable to all companies including foreign companies for the financial year commencing from 1st April 2015 and onwards except following companies:
 - a. Banking company,
 - b. Insurance company,
 - c. Non-profit making company under section 8 of the Act,
 - d. One person company,
 - e. Small company,
 - f. Private limited company
 - i. not being a subsidiary or holding company of a public company
 - ii. having paid up capital and reserves not more than Rs. 1 crore as on the balance sheet date,
 - iii. total borrowings from bank / financial institution not exceeding Rs. 1 crore at any point of time during the financial year and
 - iv. total revenue as disclosed in Schedule III to the Companies Act 2013 (including revenue from discontinuing operations) not exceeding Rs. 10 crore during the financial year.

Further, CARO 2016 will not apply to Consolidated Financial Statements (CFS).

Our Comments:

Increasing the threshold limits for applicability to private companies is a positive development. However private company which are subsidiary or holding company of a public company would now be covered under CARO, 2016 thereby expanding applicability for such private companies.

CARO was earlier applicable to standalone as well as CFS however now reporting requirement are only to the extent of standalone financials. This is a welcome step considering that only relevant matters will be reported to the members of the company and would save significant time in compilation of CARO applicable to entities which were consolidated. The CARO, 2016 would apply to financial year commencing from 1st April 2015 and onwards i.e. CARO, 2015 would be applicable for financial year ending December 2015 and December 2016.

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2. There are 16 clauses for reporting under CARO, 2016 as against existing 12 clauses under CARO, 2015 (3 clauses have been deleted & 7 clauses are added).
 3. Summary of key changes in CARO, 2016

NEW REPORTING REQUIREMENTS /MODIFICATIONS IN EXISTING CLAUSES

1. Fixed assets

The auditors would now be required to report on whether the title deeds of the immovable properties are held in the name of the company. Details of the property which are not held in the name of the company would have to be mentioned in the audit report.

2. Loans granted under Section 189

- The requirements of reporting on terms and conditions of the loans granted and whether they are prejudicial to the interest of the company or not has been reintroduced. The auditors are also specifically required to comment on whether there is a repayment schedule or not apart from comment on regularity of receipts.
- The reporting is now only for all amounts overdue for more than 90 days. Earlier this reporting was required for all overdue amounts in excess of Rs. 1 lac.

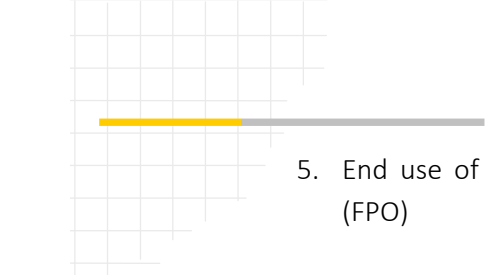
3. Loans, investments etc. – compliance of Section 185 and 186 of Companies Act 2013

New clause has been added on reporting on compliance with provisions of Section 185 and 186 of Companies Act 2013 in respect of loans, investments, guarantees and security.

There are diverse views and legal opinions being obtained by companies on the applicability of the section 185 and 186 and hence reporting on this clause would be a challenging task.

4. Default in repayment of loans and borrowings

In addition to existing reporting requirements, lender wise detail needs to be provided in case of default to banks, financial institution and government. Also the earlier clause did not cover reporting on loans from government.



5. End use of money raised from Initial Public Offer (IPO) & Follow-on Public Offer (FPO)

This reporting requirement is reintroduced. However, the reporting is now extended to cover debt instruments. However, similar disclosure was already required to be given under SEBI Regulation.

6. Fraud Reporting

Reporting is now restricted to the fraud on the company by its officers / employees against the earlier requirement of any fraud on the company. This is also in line with the requirement u/s 143(12) of Companies Act 2013 wherein reporting is required for fraud by the company and fraud on the company by officers/ employees.

7. Managerial Remuneration

New reporting requirement regarding compliance with section 197 and schedule V of Companies Act 2013 with respect to managerial remuneration paid /payable. In case the amount paid is in excess, the auditors would be required to report the amount involved and steps taken for securing refund. This section is not applicable to private companies hence reporting is not required in this case.

8. Nidhi company

The reporting required for Nidhi Companies has been reintroduced with certain modifications and certain additional reporting requirements.

9. Related party transactions

Auditors are now specifically required to comment on compliance with section 177 and section 188 of the Companies Act 2013 with respect to related party transactions and also confirm whether disclosure in accordance with accounting standards (AS) have been made or not. The above requirement is required even though prior approval would have been taken by the company from board /members for related party transactions. The definition of 'related party' is different under AS and Companies Act 2013 which has to be considered when reporting under this clause. Validating the arm's length price continues to be of challenge.

10. End use of fund raised by preferential allotment / private placement of securities

This reporting requirement is reintroduced. However the reporting is now extended to cover fully or partly convertible debentures. Monitoring and reporting on end use of funds raised would require considerable time / efforts. Additionally, reporting is also required on compliance with section 42 of the Companies Act 2013 which also requires the company to maintain separate bank accounts for application money.

11. Non cash transactions

New clause has been added on reporting of non-cash transactions with directors or persons connected with him and compliance with section 192 of Companies Act 2013.

As per section 192, non-cash transactions require prior approval of members of the company otherwise these are considered as void. Also if there are non-compliances under section 192 it would have been covered in the main audit report under modification.

12. Registration under RBI - NBFC

The auditors are now required to comment on whether the company is required to be registered under section 45-IA of the Reserve Bank of India (RBI) Act, 1934 and if so, whether the registration has been obtained. Currently, RBI requires a Non-Banking Financial Company (NBFC) to submit a certificate from their statutory auditors every year in regard to above matter.

REPORTING NO LONGER REQUIRED

1. Inventories

Reporting on procedure of physical verification are reasonable and adequate & maintenance of records.

2. Internal Control

Reporting on adequacy of internal control commensurate with the size of the company and nature of business for purchase of inventory and fixed assets and for sale of goods and services. This would now be part of the report on Internal Financial Controls (IFC).



3. Statutory dues

Reporting on amounts required to be transferred to investor education and protection fund. In CARO, 2015 reporting was in regard to IEPF under the provisions of the Companies Act, 1956. The reporting in the main audit report would continue.

4. Net worth

Reporting on accumulated losses in excess of 50% of the net worth and cash losses.

5. Guarantees for loans

Reporting on any guarantee for loans taken by others from bank or financial institution and whether its terms and conditions are prejudicial to the interest of the company.

Our comments – CARO, 2016 focuses significantly on the related party transactions, loans taken from banks, financial institutions, government and debenture holders as also end use of funds raised by the company from public which in our view is a positive development from the perspective of transparency and governance. However this would definitely increase the responsibility on the auditors of the company.

The revised guidance note is expected from the ICAI on CARO, 2016 which would provide guidance on new reporting requirements mainly on matters related to loans and advances, related party transactions, title deeds of the Company etc.

[Link](#) of notification issued by the MCA. In case of any clarification, you may reach us at info@nashah.com

Disclaimer:

This document has been prepared as a service to the clients. We recommend you to seek professional advice before taking any action on the specific issues.