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Auditors Watchlist

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As auditors gear-up to audit the financial statements, it is critical that they continue to evaluate the implications of the recent development in the financial reporting and auditor reporting requirements. This article aims to provide an overview of the significant matters that should be considered by the auditor while auditing the financial statements for the year-ended March 31, 2022.

1. *Unwinding effect of COVID 19*

Determination of future cash flows

The onset of the pandemic might have prompted auditors of certain entities to include an Emphasis of Matter ('EOM') paragraph in the audit report highlighting the uncertainties faced by the management in determination of future cash flow projections and that the actual results of the entity may differ from such estimates depending on future developments.

Where the key financial parameters e.g. revenue from operations, profit after tax have reached the pre-COVID levels or the auditor concludes that the impact already recognised in the financial statements is not expected to materially different, the auditor might conclude that the EOM paragraph included in the auditor report of previous is no longer be relevant and should be discontinued.

Reversal of impairment loss

There may be triggers for reversal of impairment losses previously recognised. The auditor should refer to the relevant accounting framework in this regard e.g. Ind AS 36 requires entities to assess whether there is any indication that an impairment loss may no longer exist or may have decreased. If there is any such indication, the entity has to recalculate the recoverable amount of the asset.

Adequacy of disclosures - customised and transparent

The auditor should assess that the affected entities have provided information that is relevant to the users and adequately reflects the current and the expected impact (to the extent possible). Given the fragility of the recovery, auditor should assess the need to expand the level of detail of the information beyond the minimum disclosures so as to enable a user's understanding of the impact of particular transactions.

2. *Accounting developments*

Accounting framework for companies preparing financial statements as per Accounting Standards

Effective 1 April 2021, companies preparing financial statements as per Accounting Standards should prepare financial statement as per Companies (Accounting Standards) Rules, 2021. This Rule has also enhanced the monetary thresholds prescribed for determination of a Small and Medium sized Company:

A company:	**Pre-revised (INR)**	**Revised (INR)**
Whose turnover excluding other income) does not exceed	*50 crores	*250 crores
Which does not have borrowings (including public deposits) in excess of	** 10 crores	**50 crores

** In the immediately preceding accounting year*
***At any time during the immediately preceding accounting year*

Small and Medium sized Company enjoy certain exemptions/ relaxations from the accounting requirements e.g Segment Reporting (AS 17) is not mandatory. Where a company decides to avail these exemptions/ relaxations in the current year, the auditor should assess that such company complies with the above Rules. Further, pursuant to the substitution of the erstwhile requirements, the auditor should update the reference of the applicable Rules in the audit report e.g. in the management responsibility section of the audit report.

Key amendments to Ind AS

The COVID -19 pandemic had prompted lessors to grant rent concessions to lessees e.g a reduction in lease payments for a period of time. Ind AS 116 included an optional practical expedient - accordingly, a lessee may elect not to assess whether a COVID-19 related rent concession from lessor is lease modification if the prescribed conditions are met e.g. the reduction in lease payments affect only payments originally due on or before 30 June 2021. Ind AS 116 was amended to extend the due date of lease payments by one more year i.e. 30 June 2022.

3. Developments in financial statements disclosures and auditors reporting obligations

MCA has prescribed numerous disclosures in the financial statements by amending Schedule III to the Companies Act, 2013. The amendments have been brought to bring more transparency in financial reporting framework such as details of funding transactions, title deeds of immovable properties, including undisclosed income, details of benami property, ratios etc. These new/ revised disclosures would require the management to present information of prior year - auditor should assess the appropriateness of the information of the previous year.

Further, corresponding reporting requirements have also been prescribed for most of the above disclosures. Most of these reporting obligations have been prescribed under Companies (Auditor's Report) Order, 2020 except for reporting on funding transactions – which has been prescribed under the Companies (Audit and Auditors) Rules, 2014.

4. Russia Ukraine conflict

Impairment of financial and non-financial assets

While assessing the impairment of financial instruments including trade receivables, loans and advances, the auditors should assess whether the effect of invasion has led to a significant increase in credit risk and whether these events have affected the measurement of expected credit losses/ loss allowance as per the applicable accounting framework. Auditors should carefully assess that the-models used by the entities have been updated considering the invasion/ sanctions.

Auditors should also assess whether there are any indications that an asset in the scope of Ind AS 36/ AS 28 (e.g., tangible, intangible assets) may be impaired. In making this assessment or write-down of assets, the auditor should carefully consider entity's decisions to abandon, dispose or suspend operations in Ukraine, Russia or Belarus.

Insurance recoveries

Careful consideration of these policies will be required by the auditor to determine whether losses directly or indirectly attributable to the war in Ukraine are covered by insurance. The ability to claim these proceeds will depend on the specific terms of the insurance contract and interpretation of the applicable law. An entity should recognise a compensation for business interruption as a receivable when it has an unconditional right to receive the compensation.

Non availability of financial information from component auditor

Decision to abandon operations in the affected areas might restrict access of Group management to the financial information of the component. Similarly, the component auditor might not be able to perform and/or complete sufficient appropriate audit procedures. If the Group management has used the financial information of a different period while preparing the consolidated financial statements, the auditor should assess that the maximum time gap between the reporting dates of the component and the holding company donot exceed the limits prescribed under the applicable accounting framework e.g. under Ind AS 110, difference between the reporting dates should not be more than 3 months.

The principal auditor may employ alternative means or methods to obtain sufficient appropriate audit evidence e.g. outcome of any prior visits, screen sharing software or other electronic means used discuss the work with the component auditor. If principal auditor is unable to obtain adequate information or reporting from the component auditors, the principal auditor should express a qualified opinion or disclaimer of opinion because there is a limitation on the scope of audit of the consolidated financial statements.

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