

No. 358 CA-IV/ 5 -2006

भारत के नियंत्रक-महालेखापरीक्षक का कार्यालय

10, बहादुरशाह जफर मार्ग,

नई दिल्ली - 110 002

OFFICE OF THE
COMPTROLLER & AUDITOR GENERAL
OF INDIA

10, BAHADUR SHAH ZAFAR MARG,

New Delhi - 110 002

दिनांक / DATE 20.6.07

To,

1. All Pr. Directors of Commercial Audit & Ex-officio
Member, Audit Board,

2. Director General of Audit (P&T).

Subject: Circular for guidance of MsAB/DGA (P&T) in exercising their judgment in determining the significance/materiality for CAG's comments.

Sir/Madam,

The matter regarding defining criteria to ensure that only significant/material comments are proposed u/s 619(4) of the Companies Act, 1956 has been examined in this office. It has been observed that materiality depends on the size and nature of an item, judged in the particular circumstances of its misstatement and determining the significance/materiality of the comment is wholly a matter of the auditor's own professional judgment. However, in order to assist MsAB/DGA (P&T) in exercising their judgment, certain instructions, as contained in the enclosed Circular, are forwarded for their guidance. ♦

Yours faithfully,

Sd/-

(A.K. Awasthi)

Director General (Commercial)

Encls.: as above

Copy along with a copy of circular forwarded for information to ADAL(C& SCS)

Sd/-

Director General (Commercial)

Copy along with a copy of circular forwarded for information and necessary action to all Sr.AOs/AOs/AAOs, CA-III Section, Sr. AO (Cordn). Guard file.

Admn. Officer/CA-IV (Tech)

Strictly for departmental use
Circular

The issue of defining the criteria for ensuring that only significant/material comments are proposed u/s 619(4) of the Companies Act, 1956 has been under deliberation for some time now. Attention is drawn to the Auditing and Assurance Standard 13 of ICAI, which states that **materiality depends on the size and nature of an item, judged in the particular circumstances of its misstatement.** While determining the significance/materiality of the comment is wholly a matter of the auditor's own professional judgment, the following guidance is intended only to assist Members Audit Board/Principal Directors of Commercial Audit/Director-General (P&T) in exercising their judgment.

The guidance has been divided in two parts-- **CAG's comments on Financial Statements** and, **CAG's comments on Statutory Auditor's report.**

CAG's comments on Financial Statements:

1. **Compliance with legal and regulatory requirements:** If the legal or regulatory requirements applicable to the preparation and presentation of the financial statements have not been followed or complied with, the fact should, with reasons, if any, be commented upon. Such legal/regulatory are prescribed as under:

(a) Requirements regarding form and contents of the financial statements as prescribed under the regulating Act like Section 211 of the Companies Act 1956 read with Schedule VI and Section 11(1)(a) of the Insurance Act, 1938 read with Schedule B to IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulation, 2000.

(b) Compliance with prescribed Accounting Standards, as applicable.

2 **Disclosure of Accounting Policy:** Inadequate or improper disclosure of an accounting policy when it is likely that a user of the financial statements would be misled by the description, should be commented upon.

3 **Impact of comment:** If the impact of an audit comment or the aggregate impact of a number of comments-

- (a) converts profit into loss or vice versa in a financial statement;
- (b) reverses a trend in the accounts generally or in a particular figure;
- (c) increases losses above the limits for disclosure;

- (d) increases the amount in an expenditure head above the threshold that requires an explanation in the account; and
- (e) creates or eliminates the margin of solvency in a balance sheet (post balance sheet events should also be considered).

4 **Repeated comments:** In case certain comments are being repeated in the Statutory Auditor's Report or are not being proposed for issue as CAG's comments due to low materiality (value) or on which Management has offered an assurance but the same has not been complied with, such comments may be proposed after a cycle of two years.

5 **Money value of the comments:**

(a) **Individual comments**

- (i) Individual observations on Profit / Loss Account involving money value equal to or exceeding 2 percent of the net profit/loss; and
- (ii) Individual observations on Balance Sheet involving money value equal to or exceeding 2 percent of the value of net assets/liability (line item)¹ to which it pertains should be considered material/significant.

(b) **Aggregated Comments**

- (a) All quantified observations on the Profit/Loss Account should be aggregated, irrespective of individual values. If the value exceeds 3 percent of the net profit/loss, all observations together should be considered material/significant.
- (b) All quantified observations on a particular asset/liability head should be aggregated, irrespective of individual values. If the value equals or exceeds 3 percent of the net value of asset/liability, all observations should be considered material/significant. The base figure should be the line items in the balance sheet referred to in Footnote 1.

¹ Assets – Fixed assets, CWIP, Investments, Current Assets, Loans and Advances, Deferred Tax Assets and Deferred Revenue.

Liabilities – Share Capital, Reserves and Surplus, Secured Loans, Unsecured Loans, Deferred Tax Liabilities, Current Liabilities and Provision.

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CAG's comments on Statutory Auditor's report:

6 Comments on Statutory Auditors' Report should be taken in the following cases:

- (a) Non-compliance with Auditing and Assurance Standards of ICAI.
- (b) Non-compliance with reporting requirements of Companies Act, 1956 including any notifications prescribing reporting requirements under the Companies Act..
- (c) Wrong quantification involving significant variations.
- (d) Non-quantification of major qualifications where it can be demonstrated as quantifiable in supplementary audit and meets the criteria of materiality/significance by value as listed above.

7 The 'true and fair' opinion is given by the Statutory Auditors. The opinion of the Statutory Auditors may be viewed in the context of the comments in totality in the following cases:

- (a) If as an impact of the observations, profit is converted into loss and vice-versa, irrespective of the monetary value.
- (b) If the aggregate value of the CAG's observations and the value of the statutory auditors quantified qualifications on Profit and Loss account equals or exceeds 20 percent of the net profit/loss, the statutory auditors opinion should be reviewed to consider the sustainability of a 'true and fair' view, if such a view has been expressed by the Statutory Auditor.
- (c) If the aggregate value of the CAG's observations and the quantified value of the statutory auditors qualifications on the Balance Sheet equals or exceeds 10 percent of the total assets/liabilities, the Statutory Auditors opinion should be reviewed to consider the sustainability of a 'true and fair' view, if such a view has been expressed by the Statutory Auditor

It is reiterated that the monetary values and percentages mentioned in these guidelines should not be viewed in isolation of the particular circumstances of the financial statements/ Statutory Auditor's Report.

Sd/-
Director General (Commercial)

(File No. CA-IV/5-2006)

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