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Preparing for Audit in India

Introduction

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Understanding different audit types is crucial for business credibility and financial health. Whether conducted internally or by a third party, audits assess company performance, enhance efficiency, and ensure compliance with relevant laws. In India, the audit landscape encompasses statutory, internal, and cost audits under the Companies Act, 2013, GST audits post-GST law implementation, and tax audits under Section 44AB of the Income-tax Act, 1961.

In this *India Briefing Magazine* issue, we provide readers with an overview of India's audit types and processes, outlining general requirements and materials to be prepared. We highlight the role of the auditor and significance of diverse audit reports for effective business management, error identification, and to meet tax and regulatory norms. We also discuss the GST audit process and transfer pricing reporting requirement. Lastly, we introduce some of the latest tech-driven audit innovations and detail a recent mandate from Indian authorities to enable 'audit trails' in business management software.

At Dezan Shira & Associates, we have a dedicated team of accounting and legal professionals in India with extensive experience in helping foreign enterprises ensure compliance. If you have any questions or require assistance with Annual Statutory Audit, GST Audit, Bookkeeping, Financial Reporting, or other compliance matters, please feel free to contact our offices in India or email us at **india@dezshira.com**.

With kind regards,

Rohit Kapur

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Preparing for Audit in India

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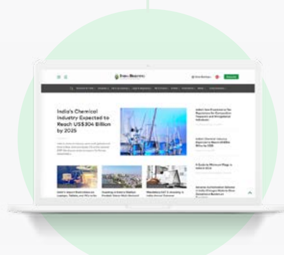

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An Introduction to Auditing in India

Audits are vital for ensuring transparent, accountable, and reliable financial information within organizations. Indian regulations mandate different types of audits and government scrutiny over financial reporting continues to be dialed up. Businesses are advised to align their reporting obligations with auditor demands to meet regulatory standards.

Melissa Cyrill
Author

Audits serve the crucial purpose of determining the accuracy and fairness of a company's financial statements. In accordance with the Companies Act, 2013, specific classes of companies are required to appoint auditors to conduct audits of their functions and activities. India's Company law prescribes four main types of audits for companies: statutory audit, internal audit, cost audit, and secretarial audit. Additionally, the Income Tax Act, 1961, under section 44AB, outlines the provisions for income tax audit, which assesses the accuracy of income tax returns filed by individuals or companies for a given assessment year.

We introduce the concept of each type of audit and explore the classes of companies obligated to conduct audits and appoint auditors in this chapter.

Types of audits

Statutory audit

The primary purpose of a statutory audit is to verify whether a company presents an accurate representation of its financial situation by examining crucial information, such as books of account, bank balance, and financial statements. All public and private limited companies are required to undergo a statutory audit. Irrespective of their business nature or turnover, these companies must have their annual accounts audited each financial year.

Limited liability partnership firms (LLPs) are subject to a statutory audit only if their turnover in any financial year exceeds INR 4 million (US$55,945) or their capital contribution exceeds INR 2.5 million (US$34,963). Upon registration of a company, it must appoint an auditor within 30 days during its first board meeting.

At each Annual General Meeting (AGM), the shareholders of the company appoint an auditor who holds the position from one AGM to the conclusion of the next AGM. The Companies (Amendment) Act, 2017 specifies that auditors can only be appointed for a maximum term of five consecutive AGMs. Their appointment does not need to be ratified in each AGM. However, for individual and partnership firms, auditors cannot be appointed for more than one or two terms, respectively.

Qualifications for statutory auditors

As per the law, only an independent chartered accountant firm, a chartered accountant, or a limited liability partnership firm with a majority of partners practicing in India are eligible to be appointed as an auditor for a company.

The Companies Act, 2013 specifically disqualifies the following individuals from becoming auditors:

- Corporate bodies, except for LLPs registered under the Limited Liability Partnership Act, 2008.
- Officers or employees of the company.
- Any partner of the company and any person whose relative is a director or is in the employment of the company as a director or key managerial personnel.
- Individuals who are indebted to the company for a sum exceeding INR 1,000 (US$14) or have guaranteed to the company on behalf of another person a sum exceeding INR 1,000 (US$14).
- Individuals who have held any securities in the company after one year from the date of commencement of the Companies (Amendment) Act, 2000.
- Individuals who have been convicted of an offense involving fraud, and a period of 10 years has not elapsed from the date of such conviction.

CARO 2020

In February 2020, the Ministry of Corporate Affairs (MCA) introduced a new format for statutory audits of companies through the Companies (Auditor's Report) Order, 2020 (CARO 2020). This order replaced the earlier Companies (Auditor's Report) Order, 2016. CARO 2020 requires auditors to report on various aspects of the company, including fixed assets, inventories, internal audit standards, internal controls, statutory dues, among others. It applies to all statutory audits commencing on or after April 1, 2020 (corresponding to the financial year 2019-20). However, companies previously excluded from CARO 2016, such as one-person companies, banking and insurance companies, small companies, etc., would continue to be excluded from CARO 2020.

Furthermore, the MCA announced additional amendments to Schedule III of the Companies Act, 2013, effective from April 1, 2021. The primary objective behind the amendments is to enhance compliance stringency and incorporate several additional disclosures in the Financial Statements.

Internal audit

Internal audit is mandated by Section 138 of the Companies Act, 2013, for certain categories of companies falling within the prescribed threshold. Its primary purpose is to assess the financial health and operational efficiency of a company. As an independent function of management, it continuously and critically evaluates the entity's operations, with a specific focus on identifying areas for improvement and strengthening governance mechanisms to add value.

The Institute of Chartered Accountants of India defines the role of internal audit as providing independent assurance that an organization's risk management, governance, and internal control processes operate effectively. Unlike external audits, internal auditors go beyond financial risks and statements and consider broader issues, including the organization's reputation, growth, environmental impact, and treatment of employees.

Applicability of internal audits

An internal audit must be conducted by either a chartered accountant or a cost accountant. However, not all companies are required to conduct internal audits. The Companies Act, 2013, and Rule 13 of the Companies (Accounts) Rules, 2014, mandate internal audits for the following classes of companies:

- Every listed company.
- Every unlisted public company with a paid-up capital exceeding INR 500 million (US$7 million) in the previous financial year.
- Every unlisted public company with a turnover greater than INR 2 billion (US$28 million) in the previous financial year.
- Every unlisted public company with outstanding loans and liabilities exceeding INR 1 billion (US$14 million) at any point during the previous financial year.
- Every unlisted public company with outstanding deposits exceeding INR 250 million (US$3.5 million) in the previous financial year.
- Every private company with a turnover of more than INR 2 billion (US$28 million) in the previous financial year.
- Every private company that has had outstanding loans and liabilities exceeding INR 1 billion (US$14 million) at any point.

Complying with the internal audit requirements ensures that these companies maintain a robust evaluation of their operations and corporate governance practices.

Secretarial audit

Secretarial audit is a crucial requirement for certain businesses in India to ensure compliance with key company legislation and corporate governance rules. Failure to conduct the secretarial audit and submit the secretarial compliance report may lead to non-compliance.

Who requires a secretarial audit?

As per Section 204(1) of the Companies Act, 2013, every listed company and the following class of companies are required to submit a Secretarial Audit Report signed by a Company Secretary in Practice along with the Board Report as per Section 134(3), Companies Act, 2013:

- Public companies with a paid-up share capital of INR 500 million (US$7.03 million) and above.
- Public companies with a turnover of INR 2.5 billion (US$35.02 million) or more.
- Every company with outstanding loans or borrowings from banks or public financial institutions of INR 1 billion (US$14.08 million) or more per provisions of Section 204 of the Companies Act. This requirement considers the paid-up share capital, turnover, or outstanding loans or borrowings as of the last date of the latest audited financial statement. Per the amendment to Rule 9(1), this does not cover loans from directors, body corporates, related parties, or deposits received under Chapter V of the Companies Act, 2013.

The secretarial audit is conducted by a practicing company secretary (PCS), who prepares the audit report.

It is worth noting that companies not covered under Section 204 of the Companies Act, 2013, have the option to obtain a secretarial audit report voluntarily. This voluntary audit provides independent assurance of the company's compliance status.

Cost audit

Cost audit involves the verification of a company's cost accounts and serves as a check on its compliance with cost accounting standards. Cost accounting helps understand the total cost of production by analyzing variable and fixed costs. Through a cost audit, companies can closely examine their production costs and find effective ways to reduce expenses related to labor, materials, and overheads.

Who should maintain cost records?

Companies are required to maintain cost records under the following circumstances:

- If the company is engaged in the production of goods or providing services as prescribed by the law.
- If the company's overall turnover from all its products and/or services amounts to INR 350 million (US$4.9 million) or more during the immediately preceding financial year.

Mandatory cost records audit

Companies in India must get their cost records audited in the following cases:

- The overall annual turnover from all the company's products and services during the immediately preceding financial year is either INR 500 million or INR 1 billion (US$7 million or US$14 million), depending on whether the company operates in a regulated or unregulated sector.
- The aggregate turnover of the products and services for which cost records are required to be maintained amounts to either INR 250 million or INR 350 million (US$3.5 million or US$4.9 million), depending on the company's sector regulation.

Classification of industrial activity

The Companies Act classifies company industrial activity into two categories: regulated and unregulated sectors. Regulated sectors include industries such as petroleum products, drugs and pharmaceuticals, fertilizers, and sugar, among others. Unregulated sectors encompass industries like arms and ammunitions, cement, tea and coffee, milk products, turbo jets, and propellers, among others.

Exemption from cost audit

Certain companies are exempt from the cost audit requirement, including:

- Companies covered under Rule 3 of the Companies (Cost Records and Audit) Rules, 2014.
- Companies with revenue from exports in foreign exchange exceeding 75 percent of their total revenue.
- Companies operating in special economic zones (SEZ).

Tax audit

Tax audit serves several essential objectives to ensure the proper functioning of businesses. Firstly, it aims to ensure the accurate and well-maintained books of accounts, which are verified and certified by a tax auditor. Secondly, the tax auditor meticulously examines the books of accounts and highlights any observations or discrepancies found during the audit process. Thirdly, the tax audit report includes prescribed information, such as tax depreciation, and compliance with various provisions of income tax law. These objectives collectively enable tax authorities to verify the accuracy of income tax returns filed by taxpayers, making the calculation and verification of total income and deductions smoother and more efficient. Conducting a tax audit is a crucial step for businesses to maintain compliance and accuracy in their financial reporting, ensuring transparency and adherence to tax laws and regulations.

Overview of Financial Reporting Requirements for Different Entities in India				
Type of audit	**Scope of audit**	**Standards to comply**	**Who conducts the audit?**	**Who is the report submitted to?**
Statutory audit	Audit of the financial records and statements of the company	Auditing standards recommended by Institute of Chartered Accountants of India (ICAI)	• A chartered accountant (CA) (Excluding the statutory auditor of the company); or • A cost accountant; or • A professional decided by the Board.	Members
Internal audit	Audit of the functions and activities of the company	NA	• A CA (excluding the statutory auditor of the company); or • A cost accountant; or • A professional decided by the Board.	Board of Directors
Secretarial audit	• Reporting on the compliance of five laws as mentioned in Form MR-3 • Reporting on the compliance of secretarial standards issued by the Institue of Company Secretaries of India • Monitoring and ensuring compliance with general laws, such as labor laws, competition laws, and environmental laws • Examining and reporting on the specific observations or qualification, reservations or adverse remarks in respect of the board structures/ system and processes relating to the audit period	Auditing Standards recommended by the Institute of Company Secretaries of India (ICSI)	A practicing company secretary (CS)	Members
Cost audit	Audit of the cost records of the company	Cost auditing standards issued by the Institute of Cost and Works Accountants of India	A practicing cost accountant	Board of Directors

Who needs a tax audit?

A taxpayer is obligated to undergo a tax audit if their business's sales, turnover, or gross receipts exceed INR 10 million during the financial year. Additionally, there may be certain other circumstances where a taxpayer is required to get their accounts audited. The different scenarios have been categorized in the tables provided below.

Penalty for non-compliance

In case of non-compliance with the tax audit provisions or failure to conduct a tax audit, a penalty of 0.5 percent of total sales, not exceeding INR 150,000, will be imposed on the company or individual.

Tax audit report

The tax audit must be carried out by a practicing licensed chartered accountant. The auditor is required to submit the tax audit report in one of the following formats:

- Form 3CA: When a company is already mandated to get its accounts audited under the Companies Act, 2013; or
- Form 3CB: When a company or an individual gets their accounts audited under Section 44AB of the Income-tax Act, 1961.

Transfer pricing report

All taxpayers, without exception, are required to obtain an independent accountant's report for international transactions between associated enterprises or specified domestic transactions. This report must be provided by the deadline for filing the tax return.

Deadline for transfer pricing audit

For individuals engaged in international transactions or specified domestic transactions under section 92E of the Income-tax Act, 1961, the report from an accountant must be furnished by October 31, 2023, for FY 2022-23. In the case of assesses subject to transfer pricing regulations, the due date to submit the Return of Income for Assessment Year 2023-24 is November 30, 2023. Form 3CEB must be filed.

Recent amendments

The Finance Act 2020 initially raised the tax audit threshold from INR 10 million to INR 50 million for the assessment year 2020-21 (FY 2019-20). To be eligible, cash receipts and payments were to be within 5 percent of gross receipts/turnover for the enterprise.

The Finance Act 2021 later increased this threshold to INR 100 million from April 1, 2021, with the same 5 percent cash transaction cap.

These changes ease tax audit burdens for small to medium-sized businesses meeting the specified conditions related to cash receipts and payments.

The auditor's report

Audit reports provide the auditor's opinion based on their review and analysis of a firm's financial statements. These reports serve as valuable tools for investors to assess the financial performance and position of the company for potential investment opportunities. Likewise, company directors and shareholders rely on them to gauge the management's integrity and the transparency of financial statements.

To ensure the credibility of an auditor's report, investors must confirm that the report comes from an independent audit firm. Different types of audit opinions carry varying levels of assurance and convey distinct messages to users. Auditors may issue one of four opinions: unqualified, qualified, adverse, or disclaimer of opinion. These opinions

Category of person	Threshold for tax audit in India
Business	For businesses not opting for the presumptive taxation scheme, the tax audit is mandatory under the following conditions: • Total sales, turnover, or gross receipts exceed INR 10 million in the financial year. • If cash transactions are up to 5% of total gross receipts and payments, the threshold limit for tax audit is increased to INR 100 million, effective from the financial year 2020-21.
	• For businesses eligible for presumptive taxation under Section 44AE, 44BB, or 44BBB, the requirement for tax audit arises if they claim profits or gains lower than the prescribed limit under the presumptive taxation scheme.
	• For businesses eligible for presumptive taxation under Section 44AD, a tax audit is required if they declare taxable income below the limits prescribed under the presumptive tax scheme and their income exceeds the basic threshold limit.
	• For businesses that are not eligible to claim presumptive taxation under Section 44AD due to opting out during any one financial year within the lock-in period of 5 consecutive years from when the presumptive tax scheme was opted, a tax audit is required if their income exceeds the maximum amount not chargeable to tax in the subsequent 5 consecutive tax years from the financial year when the presumptive taxation was not opted for.
	• For businesses that are declaring profits as per the presumptive taxation scheme under Section 44AD, a tax audit is required if their income exceeds the maximum amount not chargeable to tax in the subsequent 5 consecutive tax years from the financial year when the presumptive taxation was not opted for.
	• For businesses declaring profits as per the presumptive taxation scheme under Section 44AD, a tax audit will not be applicable if the total sales, turnover, or gross receipts do not exceed INR 20 million in the financial year. In such cases, businesses meeting this sales threshold are exempt from the requirement of undergoing a tax audit, ensuring ease of compliance for smaller enterprises.
Profession	• For individuals engaged in a profession, a tax audit is required if their total gross receipts exceed INR 5 million in the financial year. When their professional earnings surpass this specified threshold, they must undergo a tax audit to ensure accurate reporting of income and compliance with tax regulations.
	• For individuals engaged in a profession eligible for presumptive taxation under Section 44ADA, a tax audit is required if they claim profits or gains lower than the prescribed limit under the presumptive taxation scheme or if their income exceeds the maximum amount not chargeable to income tax. The tax audit becomes essential in such cases to verify the accuracy of income reporting and ensure compliance with tax laws and regulations.
Business loss	• If a business incurs a loss and does not opt for the presumptive taxation scheme, a tax audit is required if the total sales, turnover, or gross receipts exceed INR 10 million. In such situations, the business must undergo a tax audit to ensure proper financial reporting and compliance with tax regulations, even in the event of a loss.
	• If a taxpayer's total income exceeds the basic threshold limit but they have incurred a loss from carrying on a business (not opting for the presumptive taxation scheme), a tax audit under 44AB is required if the sales, turnover, or gross receipts from the business exceed INR 10 million.
	• If a business is opting for the presumptive taxation scheme under section 44AD and has a business loss but its income falls below the basic threshold limit, a tax audit is not applicable. In such cases, the business is not required to undergo a tax audit, as its income is below the specified threshold, providing relief from the audit requirement despite the business loss.
	• If a business is carrying on the presumptive taxation scheme under section 44AD and incurs a business loss, but its income exceeds the basic threshold limit, it is required to declare taxable income below the limits prescribed under the presumptive tax scheme. In such situations, the business must ensure that its reported taxable income falls within the prescribed limits of the presumptive tax scheme, even when facing a business loss and having income exceeding the basic threshold limit. This is essential to comply with tax regulations and accurately report the income for tax purposes.

determine whether the financial statements adhere to Generally Accepted Accounting Principles (GAAP) and whether they fairly represent the entity's financial accounts.

Unqualified opinion

The unqualified opinion is considered the most favorable audit outcome for a company. It is expressed by an independent auditor when the financial records and statements of the company present a true and fair view and adhere to the accounting principles generally accepted in India.

In essence, an unqualified opinion confirms the following key points:

- Consistent application of GAAP norms in preparing financial statements.
- Compliance of financial statements with relevant statutory requirements and regulations.
- Adequate disclosure of all material matters necessary for the proper presentation of financial information (subject to statutory requirements).
- Proper verification and determination of any changes in accounting principles or application methods, as reflected in the company's financial statements.

Qualified opinion

On the other hand, a qualified opinion is issued when the auditor is not entirely confident in the fair representation of the financial statements and identifies areas of non-compliance with GAAP.

An auditor may issue a qualified opinion under the following circumstances:

- Misstatement or misclassification of accounting entries, such as an expense incorrectly placed below the gross profit line, resulting in misleading gross profit figures.
- Limitations on audit scope, which means the auditors may not have had access to specific financial data.
- Doubts about the accuracy of specific financial data, such as a significant number of unverifiable inventories in the opening balance of the entity.

Adverse opinion

An adverse opinion is rendered when the financial statements do not fairly represent the entity's financial positions, results, and cash flows. The adverse opinion may be issued if:

- There are limitations on the scope of the auditor's work, meaning that certain areas of the company's financial records were not thoroughly examined.
- Certain required disclosures are missing from the financial statements, or there is disagreement with management regarding the acceptability of the accounting policies selected and their method of application.

AUDIT AND FINANCIAL REVIEW

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Sample Format: Independent Auditor's Report

Addressee: Members of XXX COMPANY LIMITED

Introductory Paragraph:

We have audited the accompanying standalone financial statements of XXX COMPANY LIMITED ("the Company"), which comprise the Balance Sheet as at 31st March, 20XX, the Statement of Profit and Loss, the Cash Flow Statement for the year then ended, and a summary of the significant accounting policies and other explanatory information.

Management's Responsibility:

It is the responsibility of the management to prepare its financial statements in compliance with the financial reporting framework. They need to establish appropriate systems to minimize errors, detect and mitigate fraud. Efficient internal controls are to be implemented and governed by management to establish quality control throughout its operations and increase accuracy in all departments.

Auditor's Responsibility:

The auditor is responsible for conducting the audit in accordance with established Standards on Auditing and expressing a true opinion on the financial statements. To ensure that the financial statements are free of any misrepresentations, the auditor collects reasonable evidence to support an opinion. It is the responsibility of the auditor to plan and perform the audit with professional integrity.

Auditor's Opinion:

In our opinion and to the best of our information and according to the explanations given to us, the aforesaid standalone financial statements give the information required by the Act in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India, of the state of affairs of the Company as at 31st March, 20XX, and its profit/loss and its cash flows for the year ended on that date.

Other Reporting Responsibilities (Optional):

[Include any other reporting responsibilities here if applicable.]
Signature of the Auditor:
[Name of the Auditor]
[Name of the Audit Firm]
[ICAI Registration Number of the Audit Firm]
Date of the Auditor's Report:
[Date of the report's finalization]
Place of Signature:
[City where the report is signed]

- The entity has not prepared its financial statements in accordance with the provisions of the applicable accounting framework.

When an auditor issues an adverse opinion, the audit report includes a clear description of all the substantive reasons for the adverse opinion. Auditors may point out specific accounting errors or departures from GAAP in their report. An adverse opinion can have severe consequences for the reporting entity. It may result in the company being unable to issue financial statements to external parties like creditors, lenders, and investors. Additionally, if the audit uncovers any illegal activities, corporate officers may be held personally accountable.

Disclaimer of opinion

In cases where an auditor is unable to express an opinion on the financial statements, they may issue a disclaimer of opinion. This can occur when auditors doubt the reliability of the financial data, have limited scope, or cannot audit impartially. A disclaimer of opinion is issued when auditors lack sufficient support for their conclusions and refrain from providing an opinion in such instances.

Standards of Auditing – SA 701: Communicating key audit matters in the independent auditor's report

SA 701 aims to provide users of financial statements with additional information to better understand critical matters deemed important by the auditor during the audit of financial statements for the relevant period. By exercising professional judgment, the auditor highlights key audit matters, enhancing the communication value of the auditor's report and promoting transparency about the audit process.

Limitations of communicating key audit matters

It is essential to note that the communication of key audit matters in the auditor's report does not serve as a replacement for the following disclosures:

- The disclosures made in the financial statements themselves.
- An auditor's modified opinion, as required under SA 705 (Revised), when specific circumstances of the audit necessitate such expression.
- Reporting under SA 570 (Revised) when significant uncertainties exist regarding conditions or events that may cast substantial doubt on the entity's ability to continue as a going concern, i.e., its ability to operate indefinitely.

Determining key audit matters

The auditor considers the following factors to determine key audit matters in the audit of financial statements for the relevant period:

DOING BUSINESS IN INDIA

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Find spotlight and explainer articles, news, updates, factsheets, useful tools, and webinars featuring on-the-ground advisors.

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a. Areas assessed with a higher risk of material misstatement or substantial risks identified as per SA 315.
b. Significant judgments made by the auditor concerning areas in the financial statements where noteworthy management judgment was exercised, including accounting estimates associated with high uncertainty.
c. The impact of substantial transactions or events that occurred during the relevant period on the audit.

Absence of key audit matters

If there are no key audit matters that require communication based on the circumstances and facts of the audit and the entity, the auditor must explicitly state this fact separately in the "Key Audit Matters" section of the audit report.

More Entities Brought Under India's Anti-Money Laundering Regime

- Chartered accountants, company secretaries, cost work accountants
- Directors, secretaries of companies, partners of firms
- Intermediaries in casinos and cryptocurrency or virtual digital assets
- Trustees of express trusts, nominee shareholders
- People arranging addresses, trustees for businesses
- Individuals helping in formation of a company

Applicability of anti-money laundering legislation

Financial transactions by chartered accountants, company secretaries, and cost and works accountants on behalf of clients now come under the Prevention of Money Laundering Act (PMLA), 2002. The Ministry of Finance has expanded the scope of PMLA (as of May 2023) to cover activities like property transactions, fund management, and business entity deals.

The Finance Ministry also outlined the definition of 'relevant person' under this law. It includes individuals who have obtained a certificate of practice under the Chartered Accountants Act, 1949, and are practicing either individually or through a firm.

Similarly, individuals with a certificate of practice under the Company Secretaries Act, 1980, and the Cost and Works Accountants Act, practicing individually or through a firm, will also be governed by this new law.

With the inclusion of CAs, CSs, and CMAs, they now become reporting entities for certain transactions. As reporting entities, these professionals are required to conduct KYC (Know Your Customer) for all clients engaged in the specified transactions and maintain records accordingly.

While penalties are limited under Section 13 of the Act, the Enforcement Directorate can pursue legal action if there's a deliberate involvement in money laundering. Professional bodies like The Institute of Chartered Accountants of India are expected to conduct awareness programs to ensure compliance and clarify the professionals' roles in these transactions.

Preparing for the GST Audit

The GST audit ensures businesses are in full compliance with GST regulations—their GST payments are timely and accurate, and their transaction records are precise. Additionally, the GST audit highlights areas where operational improvements can be made, ultimately helping businesses enhance their profitability and efficiency.

Melissa Cyrill
Author

Under India's Goods and Services Tax (GST) system, taxpayers are responsible for self-assessing their tax liability and making tax payments without intervention from tax authorities. To ensure compliance, the law incorporates a robust audit mechanism.

The GST audit primarily focuses on verifying the accuracy of information provided, taxes paid, refund claims, and input tax credit availed by individual taxpayers.

Recent changes to GST audit norms

Effective from the Finance Act of 2021, there have been significant changes to the GST audit requirements:

Threshold limit: Any registered taxable person with an annual aggregate turnover exceeding INR 50 million during a financial year is now obligated to get their accounts audited. Previously, this limit was set at INR 20 million.

1. **Removal of compulsory auditor requirement:** Taxpayers with a turnover exceeding INR 20 million are no longer required to undergo a compulsory GST audit conducted by a Chartered Accountant or a Cost and Management Accountant.
2. **Self-certification of Form GSTR 9C:** Starting from FY 2020-21 onwards, taxpayers with a turnover exceeding INR 50 million are now required to self-certify and submit Form GSTR 9C.

These changes aim to streamline the GST audit process and make it more efficient for taxpayers while still ensuring compliance with the GST regulations.

Calculation of annual turnover for companies with multiple locations

For companies operating in multiple locations, having subsidiaries or branches across the country, the computation of annual turnover must be done on an all-India PAN basis.

Turnover	GSTR 9: Annual return to be filed yearly by taxpayers registered under GST	GSTR 9C: Certified copy of the audited annual accounts and a reconciliation statement
Up to INR 20 million	Optional	Not applicable
IRN 20 million - INR 50 million	Mandatory	Optional
Above INR 50 million	Mandatory	Mandatory (can be filed on the GST portal through seft-certification, no professional required)

According to the GST Law, each entity of a company located in more than one state or union territory is considered distinct.

Hence, if the company is registered in multiple states or union territories, and the total aggregate turnover from all these locations exceeds INR 50 million, then the entity must undergo state-wise accounts audit as per the GST law.

The aggregate turnover includes the value of all exempt supplies and exports under the same PAN, considering the entire country. In cases where companies have multiple GSTIN (Goods and Services Tax Identification Number) state-wise registrations under the same PAN, traders and dealers must internally derive their turnover for each GSTIN and declare the corresponding amount in the Form GSTR-9C.

Additionally, companies with multiple registrations within the same state must maintain separate accounts. The GST law mandates companies to file a reconciliation statement separately for each GSTIN registration within the state. This ensures compliance and accurate reporting for each location within the state.

Filing GST audit

To complete the GST audit filing process, taxpayers are required to submit the following documents electronically:

- Annual return: File the annual return using Form GSTR-9 by December 31 of the subsequent financial year.
- Audited annual accounts: Provide a copy of the audited annual accounts.
- Reconciliation statement: Submit a certified reconciliation statement in Form GSTR-9C, reconciling the declared supplies with the audited annual financial statement.
- Other prescribed particulars: Include any other particulars as prescribed by the GST law.

For the reconciliation statement, it is advisable for GST registered entities to maintain a copy of their accounts as proof to demonstrate the correctness of various aspects, including production of goods, stock of goods, input tax credit availed, and output tax payable and paid.

General GST audit

The general GST audit pertains to an overall assessment of a business's transactions. It is conducted by the commissioner or any other authorized officer in accordance with the GST law. The audit period, frequency, and methodology are prescribed under the GST law.

The audit can take place at the registered person's place of business or at the office of the commissioner or authorized officer. The timeframe for conducting the audit is typically three months. The registered taxpayer receives an advance notice at least 15 days prior to the audit's commencement, and the audit must be completed within three months from that date. In special cases, the authorized officer can extend the audit completion period by up to six months.

During the GST audit, the authorized officer may require the registered person to:

- Provide facilities: Offer necessary facilities to verify books of accounts and other required documents.
- Furnish information: Provide the required information and offer assistance to ensure timely completion of the audit.

Special GST audit

A special GST audit is conducted at the behest of a GST Officer and carried out by a Chartered Accountant (CA) or Cost and Management Accountant (CMA). Such an audit is ordered when the GST Officer suspects that the taxpayer has incorrectly declared taxable values or inappropriately utilized input tax credit. The disparities that may trigger a special audit include incomplete audits, discrepancies in liability to evade tax, and incorrect revenue declarations.

The GST Officer initiates a special audit by issuing Form GST ADT-03, and the taxpayer must get their accounts audited either before or after the commencement of any scrutiny, enquiry, or investigation. The appointed CA or Cost and Management Accountant (CMA) performs the audit, and the taxpayer is expected to cooperate with the auditor throughout the audit process.

Upon completion of the special audit, the CA or CMA submits the audit findings in Form ADT-04. The special audit must be concluded within 90 days. However, in exceptional cases, the Commissioner may grant an extension of another 90 days based on an application made by the CA or CMA.

At the end of the special audit under GST, the taxpayer is given an opportunity to be heard concerning any material gathered during the special audit that may be used in any proceedings against them. This provision ensures that the taxpayer's viewpoint is considered before any action is taken based on the audit findings.

MANAGE COMPANY TAX AND COMPLIANCE ACROSS MULTIPLE JURISDICTIONS

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Preparing Your Business for the GST Audit and Annual Return Filing Checklist

The GST audit and annual return filing are essential compliance activities for businesses in India. Proper preparation can help streamline the process and ensure accurate reporting. Here are some steps to prepare for the GST audit and annual return filing:

- **Organize financial records:** Gather and organize all financial records, including sales and purchase invoices, expense documents, input tax credit details, and other relevant documents. Maintaining proper records will facilitate a smooth audit process and simplify annual return filing.

- **Reconcile books of accounts:** Ensure that the books of accounts reconcile with the financial statements and GST returns filed during the year. Identify any discrepancies and rectify them before the audit.

- **Verify input tax credit:** Verify the accuracy of input tax credit claimed during the year. Ensure that all eligible input tax credit is properly accounted for and supported by valid documents.

- **Review compliance with GST laws:** Conduct a thorough review of your business's compliance with GST laws and regulations. Identify any potential non-compliance issues and take corrective actions to avoid penalties.

- **Perform internal audits:** Conduct internal audits periodically to assess the accuracy of GST filings and identify areas that need improvement. Address any discrepancies or errors discovered during the internal audit.

- **Engage professional help:** It is advisable to engage the services of a qualified Chartered Accountant or a GST consultant to guide you through the audit process and ensure compliance with GST regulations.

- **Stay updated with GST changes:** Keep yourself updated with any changes in GST laws, rules, or procedures to ensure that your business adapts to the latest compliance requirements.

- **Review GST annual return:** Thoroughly review the details provided in the GST annual return before filing. Verify all figures and ensure that all relevant information is accurately captured.

- **Submit documentation timely:** Ensure that all required documents and information are submitted to the auditor or tax authorities promptly to avoid any delays in the audit process.

- **Seek clarifications:** If you have any doubts or queries related to the GST audit or annual return filing, seek clarifications from a qualified professional or contact the relevant tax authorities.

Technology-Enabled Changes in the Audit Compliance Landscape

Traditionally, audits have relied on manual assessments, consuming time and resources. Emerging technologies promise to revolutionize audits by overcoming limitations and enhancing efficiency. Indian audit regulations have also been amended to require audit trails to be enabled in business management software.

Melissa Cyrill
Author

As we look ahead to the next five to 10 years, the audit space is undergoing significant changes, driven by three key factors. First, the evolving business landscape and changing client expectations are reshaping how companies operate. The increasing complexity of organizational structures and the rise of intangible assets, such as digital transactions, require auditors to adapt their methodologies to match these new realities.

Secondly, auditors themselves are redefining their roles to deliver more value and meaningful insights beyond traditional transactional reviews. They aim to provide comprehensive and relevant reports that go beyond mere financial data.

However, one of the most significant drivers of change lies in the third aspect—the evolving regulatory landscape. The Institute of Chartered Accountants in India (ICAI) and the National Financial Reporting Authority (NFRA) are actively focused on enhancing the quality of financial reporting and ensuring auditors deliver high-quality audit reports.

To achieve robust audit processes, regulators have been updating existing guidelines and introducing new standards. Compliance with auditing standards is crucial for building trust among users of financial statements and fostering a robust economy. This includes the introduction of the concept of the audit trail, which is now mandatory for certain types of organizations in India.

What is an audit trail?

An audit trail serves as a date and time-stamped record documenting the history and details of various events, transactions, and activities. Whether related to a transaction, work event, product development step, control execution, or financial ledger entry, virtually any work activity or process can be captured in an audit trail, be it automated or manual. These trails take diverse forms in different fields, tailored to capture the unique focus areas of each domain. However, their core purpose remains consistent – to track a sequence of events and actions in chronological order. In today's rapidly evolving IT and risk environment, organizations often rely on real-time or near real-time access to audit trails as part of their day-to-day operations.

Most information technology systems also maintain comprehensive audit trails for user activity, and some systems are designed to consolidate inputs from various sources, creating extensive audit trail data.

The utility of audit trails is diverse, as they provide time-stamped records with varying levels of detail. While some may capture simple errors and basic details, others can be quite complex, requiring technical expertise to interpret.

Audit trails are an invaluable tool utilized for a range of purposes within organizations, including supporting audits, access controls, financial statements, investigations, security, and other functions.

Purpose for business organizations

The purpose of an audit trail is multifaceted. It serves as a comprehensive and complete record, enabling businesses to track irregularities and identify process breakdowns when they occur. By maintaining an airtight audit trail, companies can effectively detect internal fraud by monitoring user actions related to the company's data and information. Additionally, audit trail records are instrumental in identifying and addressing external data breach issues, which are becoming increasingly prevalent due to the rising threat of malware and ransomware crimes.

From a compliance perspective, audit trails are a requirement for many organizations. Publicly-traded companies (listed entities), in particular, must have active audit trails to comply with SEBI Listing Agreement 2014 (Clause 49), which necessitates an annual audit by independent external auditors. An audit trail captures crucial details about transactions and processes, providing essential information for future reviews and root cause analysis.

The uses of audit trails are diverse, with audits being one of the most common applications. Whether for financial, IT, HR, or operational audits, an audit log provides crucial evidence for inspection and validation of management's assertions. Audit trails are also employed to monitor access to sensitive data, investigate IT incidents, understand API transactions, track data deletions, and combat cybersecurity threats.

While audit trails offer substantial benefits, their maintenance can be costly and challenging, especially for key systems involved in audits for listed companies, where organizations are required to retain at least a year's worth of audit logs. Taking a risk-based approach can help organizations prioritize which audit trails are most critical for their operations and compliance requirements.

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Key sectors that rely on audit trails include financial and accounting, manufacturing and product design, healthcare and medical information, clinical research data, IT tracking and data, e-commerce sales records, among many others.

The benefits of maintaining an audit trail are manifold. Accurate financial records supported by an audit trail build trust with investors and lenders, positioning the business for potential investments or loans. Increased efficiency, meeting compliance requirements, disaster recovery, and overall business integrity are among the other advantages.

Compulsory 'audit trail' and 'edit log' for all companies (including Section 8 companies) in India

The Ministry of Corporate Affairs had introduced the concept of audit trail through a notification dated March 24, 2021, to come into effect from FY 2023-24.

Applicability

Starting April 1, 2023, it is now mandatory for all companies in India, regardless of their size, including not-for-profit companies licensed under Section 8 of the Companies Act 2023 (or Section 25 of the Indian Companies Act 1956), to incorporate a built-in mechanism in their software that records an audit trail for every transaction.

Thus, all companies under the Companies Act, including one-person-companies (OPC), small, dormant, and foreign companies, are required to maintain the audit trail in India.

Additionally, an edit log must be created for each modification made in electronically maintained books of account, capturing the date of such changes. It is crucial to ensure that the audit trail always remains enabled and cannot be disabled.

Business Management Software for SMEs

TallyPrime is an example of a comprehensive business management software designed for small and medium-sized (SME) businesses. With TallyPrime, the SME firm can efficiently handle various aspects of their business, including accounting, inventory management, banking, taxation, payroll, and more. By streamlining these processes, TallyPrime simplifies complexities, allowing the enterprise to focused on business growth and development.

The 'Audit trail' and 'Edit log' feature is available in Tally Prime but not in Tally ERP9. If you are using Tally Prime, please make sure to enable this feature. For users of Tally ERP9, you may reach out to your Tally service provider to inquire about the possibility of obtaining new or additional software to access these features.

However, this requirement is not yet mandatory for public charitable trusts or societies registered under the Act of 1860. Similarly, limited liability partnership (LLP) firms are also currently exempt from this obligation.

Using a third-party service provider

To ensure compliance, it is essential to check with your software service (SaaS) provider and verify whether the mentioned features are available in the software you are using. Additionally, if you rely on third-party service providers for any services offered to your company, have a discussion with them to determine the applicability of the Audit Trail functionality in their software.

Furthermore, engage in discussions with your auditors regarding these requirements or any other specific needs that will aid in achieving due compliance with this new mandate. Collaborating with all relevant stakeholders will help ensure a seamless implementation of the Audit Trail concept and adherence to the regulatory guidelines.

Penalty for non-compliance

If a company fails to meet the specified requirements, the managing director, the whole-time director in charge of finance, the Chief Financial Officer, or any other person charged by the management defined as per the provisions will be liable for punishment. The punishment entails a penalty ranging from INR 50,000 to maximum INR 500,000.

Furthermore, auditors are obligated to disclose the non-compliance in their auditors' report, making it transparent and accountable.

Summary

To achieve robust audit processes, regulators have been updating existing guidelines and introducing new standards.

In this dynamic environment, businesses and auditors alike must embrace these changes to stay ahead and foster a transparent and resilient economy.

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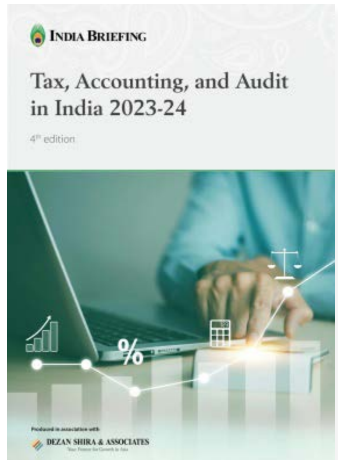
Tax, Accounting, and Audit in India 2023-24



"Tax, Accounting, and Audit in India 2023-24" serves as a comprehensive guide and will equip businesses and foreign investors with the necessary knowledge and insights to effectively navigate India's tax landscape.

The guide covers a wide range of topics, including the rules triggering an entity's tax liability in India, reporting obligations and their timeframe, and the scope of tax regulations.

Created in June 2023, this guide incorporates the most up-to-date information available at the time. to multinationals investing in emerging Asia.

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Emerging Technologies Driving Audit Innovation

Artificial intelligence

AI-based systems and machine learning capabilities are set to revolutionize audit processes, bringing greater efficiency and precision. Here are some ways these technologies will transform audits:

- Obsolete Statistical Sampling: AI and machine learning systems can scan and review entire sets of documents, eliminating the need for statistical sampling.
- Automated Verification of Evidence: Machine learning capabilities can aggregate data from various monitoring systems, serving as evidence of task performance. It can also log observations and issues based on anomalies in the data.
- Proactive Control Verification: AI-based systems can use automated measurement to predict expected outcomes and verify actual values against predictions. This proactive approach to control verification reduces the need for manual intervention.
- Expanded Use of Data Points as Evidence: Machine learning and AI systems can extract large amounts of data from diverse sources like text, images, and voice recordings. Auditors are no longer limited to the evidence provided by auditees.
- Continuous Auditing Becomes Reality: AI-based continuous control monitoring systems can examine complete sets of records and identify control violations. The system can prioritize risks based on incoming data and turn it into actionable information.
- Self-Improving Algorithms: Algorithms in deep learning allow continuous control monitoring systems to reconfigure themselves based on previous results, optimizing control design with minimal human intervention.

Blockchain

- A transformative technology across various industries, blockchains are designed to resist data modification, functioning as open, distributed ledgers for efficient and verifiable transaction recording. Auditors can use publicly available blockchain ledgers to verify transactions, reducing the need for bank statements or third-party confirmations, and increasing audit cost efficiencies.
- Yet while blockchain technology is inherently secure, it relies on human coding for integration and interfacing, presenting risks. To comply with International Standards on Auditing (ISAs), auditors must comprehend the IT-related risks to an entity's financial statements and how the entity addresses them with IT controls. With the increasing adoption of blockchain, auditors would need to elevate their assurance services to meet the demands of agile business environments and upcoming digital transformations.

Automation

- Enhanced automation has played a crucial role in developing Software as a Service (SaaS) solutions, leading to improved audit efficiency. The effectiveness of audit documentation solutions hinges on several key factors, including cost-effectiveness, reliability of output, user-friendliness, real-time updates, and seamless change management.
- An example is the solution provided by Wolters Kluwer that streamlines the audit documentation process and also facilitates real-time documentation, aligning perfectly with the ISQCI requirements. With Wolters Kluwer's solution, organizations can enjoy the benefits of efficient and up-to-date audit documentation while meeting the necessary compliance standards.

Drone technology

- Drones have found diverse applications in the field of auditing, particularly in conducting remote inventory observations for extensive setups. Additionally, the integration of inventory observations with drones and mobile applications has further optimized the process.
- What previously took 15-20 days to complete can now be accomplished in just half a day, thanks to these technological advancements. This not only saves valuable time but also reduces costs, providing significant benefits to audit firms and auditors alike.

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