



*Synopsis –  
Auditors  
(Reporting  
Obligations)  
Regulations, 2018*

*A revolution in Audit  
Reports*



# ***Auditors (Reporting Obligations) Regulations***

The Securities and Exchange Commission of Pakistan (SECP) through SRO 558(I)/2018 dated April 26, 2018 has notified the Auditors (Reporting Obligations) Regulations, 2018 (here-in-after referred to as '2018 Regulations'). The draft for comments on these regulations was notified by the SECP through SRO 471(I)/2017 dated June 15, 2017.

The 2018 Regulations have not only replaced the Auditor's report formats prescribed through Rules 17A, 17B & 17C of the Companies (General Provisions and Forms) Rules, 1985 but also include the Auditor's report formats applicable to audit of financial statements of insurance companies, review of half yearly financial statements of listed companies and reporting on Code of Corporate Governance compliance by listed companies. Previously such formats for reporting by the auditors were provided under the Insurance Rules, 2002 and by the Institute of Chartered Accountants of Pakistan (ICAP), respectively.

This document summarises the salient features of the new Auditor's Reports and is aimed at facilitating an overview of the major changes that have taken place. For considering and understanding the precise effects of a particular change / clause on the entity's reporting requirements, reference should be made to the specific wording of the 2018 Regulations.

This document can also be accessed on our website <https://www.pwc.com.pk>.

May 9, 2018

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# 1. Introduction

In exercise of the powers conferred by the Companies Act, 2017, the SECP on April 26, 2018 has notified the 2018 Regulations, which are applicable for reporting periods ending on or after June 30, 2018.

We understand that in accordance with provisions of section 509 of the Companies Act, 2017, the forms 35A, 35B, 35C and 35D relating to the Audit / Review Reports prescribed under the Companies (General Provisions and Forms) Rules, 1985 issued under the repealed Companies Ordinance, 1984 shall continue to apply up to the effective date of the 2018 Regulations.

Accordingly, the companies that have financial year / half year ending prior to June 30, 2018 would receive audit / review report, as applicable, on the same format as was provided for December 31, 2017 year / period end. However, with the applicability of the Companies Act, 2017, including the fourth and fifth schedules thereto, for the preparation of financial statements for the periods ending after December 31, 2017 the only change would be replacing the references to the Companies Ordinance, 1984 with the Companies Act, 2017 and the nomenclature of primary statements of the financial statements since these have now been defined under the Companies Act, 2017.

## 1.1 Key changes

We understand that the following two key changes brought through the 2018 Regulations will have apparent impacts on the audit and its reporting are as follows:

- Inclusion of Key Audit Matters in the auditor's report on the financial statements of listed companies (elaborated in paragraph 4.2 below).
- Elimination of the concept of division of responsibilities in case of the audit of the consolidated financial statements. The group auditor will be responsible for the direction, supervision and performance of the group audit even though some subsidiaries may be audited by other auditor (elaborated in paragraph 5 below).

The above mentioned key changes along with other important matters are set out in paragraphs 2 to 6 below.

## 2. Annexures to the 2018 Regulations

The 2018 Regulations are structured in a manner that various forms of Auditor's Reports as annexures have been appended thereto. These annexures prescribe the following reports:

Annexure reference	Reports prescribed	Previously prescribed
Annexure-I	Report on financial statements of a company other than a banking company	Rule 17A of the Companies (General Provisions and Forms) Rules, 1985 i.e. Form 35A
Annexure-II	Report on financial statements of a banking company	Rule 17B of the Companies (General Provisions and Forms) Rules, 1985 i.e. Form 35B
Annexure-III	<ul style="list-style-type: none"> <li>• Report on the Audit of the financial statements of:               <ul style="list-style-type: none"> <li>- General Insurance Company</li> <li>- Life Insurance Company</li> </ul> </li> <li>• Audit report for Regulatory Returns of:               <ul style="list-style-type: none"> <li>- General Insurance Company</li> <li>- Life Insurance Company</li> </ul>               [These have been prescribed taking into account the requirements of International Standard on Auditing (ISA) 800 'Special considerations - Audits of financial statements prepared in accordance with special purpose frameworks']             </li> </ul>	<p>Reports to the members on the financial statements of:</p> <ul style="list-style-type: none"> <li>- Life Insurance Company</li> <li>- Non-Life Insurance Company</li> </ul> <p>[SECP's notification dated March 11, 2003]</p> <p>Audit reports for financial statements and regulatory returns have been prescribed separately as previously financial statements were also part of the regulatory returns as defined in the Insurance Ordinance, 2000.</p> <p>Previously, separate auditor's reports for certain statements forming part of the regulatory returns but not part of the published financial statements were being issued. However, formats for those were not prescribed earlier.</p>
Annexure-IV	Report on the consolidated financial statements	Rule 17C of the Companies (General Provisions and Forms) Rules, 1985 i.e. Form 35C
Annexure-V	Report on second quarterly (half yearly) financial statements	Circulars 6/2009 and 2010/07 issued by ICAP
Annexure-VI	Report on Statement of compliance with the Listed Companies (Code of Corporate Governance) Regulations, 2017	Circular 2/2014 issued by ICAP
Public Sector Companies (Corporate Governance Compliance) Guidelines, 2018	Report on statement of compliance with Public Sector Companies (Corporate Governance) Rules, 2013 for public sector companies	No change

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## ***3. Reporting obligations of auditors as per the Companies Act, 2017***

### ***3.1 Second quarter (half yearly) financial statements***

Section 237 of the Companies Act, 2017 states that the cumulative figures for the half year, presented in the half yearly financial statements shall be subjected to a limited scope review by the statutory auditors of the company in such manner and according to such terms and conditions as may be determined by ICAP and approved by the SECP.

### ***3.2 Annual stand-alone financial statements***

Section 249 of the Companies Act, 2017 states that a company's auditor shall conduct the audit and prepare the report in compliance with the requirements of the ISAs as adopted by ICAP. The auditor shall make out a report to the members of the company on the financial statements and books of account of the company and on every other document forming part of such financial statements including notes, statements or schedules appended thereto, which are to be laid before the company in general meeting. The report shall provide opinion on the following:

- Whether they have obtained all the information and explanations which to the best of their knowledge and belief were necessary for the purposes of the audit.
- Whether in their opinion and to the best of their information and according to the explanations given to them, the said financial statements give the information required by the Companies Act, 2017 in the manner so required and give a true and fair view.
- Whether in their opinion proper books of accounts as required by the Companies Act, 2017 have been kept by the company.
- Whether in their opinion the statement of financial position and profit and loss account and other comprehensive income or the income and expenditure account and the cash flows have been drawn up in conformity with the requirements of accounting and reporting standards as notified under the Companies Act, 2017 and are in agreement with the books of accounts and returns.
- Whether in their opinion investments made, expenditure incurred and guarantees extended, during the year, were for the purpose of the company's business.
- Whether in their opinion zakat deductible at source was deducted by the company and deposited in the Central Zakat Fund.

### ***3.3 Annual consolidated financial statements***

Section 228(3) states that every auditor of a holding company appointed under section 246 shall also report, in the specified form, on the consolidated financial statements and exercise all such rights and duties as are vested in him under sections 248 and 249, respectively.

These requirements of the Companies Act, 2017 serve as the foundation for the 2018 Regulations and the forms of Auditor's Reports prescribed therein. An overview of the contents of the Auditor's Reports is provided in paragraph 4 of this document below.

## 4. Overview of contents of the Auditor's Reports

In accordance with the changes that have been brought about in the ISAs by the International Auditing and Assurance Standards Board (IAASB), forms of the Auditor's Reports in Pakistan have also been revised. Based thereon the new audit report formats have the following two separate sections and separate headings for the subsections and additional paragraphs are required, if required:

- (i) Report on the audit of the financial statements; and
- (ii) Report on other legal and regulatory requirements

The section comprising report on the audit of financial statements provides the format of the opinion of the auditor, alongwith other contents of the audit report, in accordance with the accounting and reporting framework applicable in Pakistan on the relevant company, whereas, the section comprising report on other legal and regulatory requirements provides the auditor opinion with regard to the specific requirements prescribed under the Companies Act, 2017 applicable for auditor's reporting. The requirements have been summarised as follows:

### 4.1 New structure of the Audit Reports

<b>Report on the audit of the financial statements</b>	
Opinion	The audit opinion and identification of the financial statements that have been audited is now the first section of the report.
Basis for opinion	The basis for opinion follows the opinion section and, in addition to referring to compliance with the ISAs and referring to the auditor's responsibilities section, now includes the new assertion of the auditor's independence in accordance with the Code of Ethics adopted by ICAP. If the audit opinion is modified, the explanation thereof is to be presented here as well.
Material uncertainty regarding going concern (if applicable)	If there is a material uncertainty with respect to going concern of the entity, it has to be described in a separate section that identifies it as such.
Emphasis of matter (if any)	An emphasis of matter paragraph may be included, if the auditor concludes that it is relevant to fulfill his reporting responsibilities.
Key Audit Matters (KAMs)	A new section providing insight into the key matters addressed during the audit has been introduced. In case of audit of a non-listed company, the KAMs section in the report is not obligatory.  In case there is no KAM the following wording may be used for inclusion in the report:  <i>"We have determined that there are no key audit matters to communicate in our report."</i>
Information other than the financial statements and auditor's report thereon	A new section in the auditor's report will describe the auditor's responsibilities for 'other information' (e.g., the rest of the annual report, including the directors report) and the outcome of fulfilling those responsibilities.
Responsibilities of management and board of directors for the financial statements	The description of management's responsibilities has been expanded to explain its responsibilities with respect to going concern. It also now identifies board of directors as those charged with governance (TCWG).
Auditor's responsibilities for the audit of the financial statements	The description of the auditor's responsibilities under the ISAs is now much more comprehensive and also includes a description of the auditor's responsibilities with respect to going concern. The new format accordingly incorporates such description.

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## Report on Other Legal and Regulatory Requirements

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Matters relating to (i) maintenance of proper books of account; (ii) presentation of financial statements in accordance with the Companies Act, 2017; (iii) investments made, expenditure incurred and guarantees extended; and (iv) zakat.

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### Other requirements

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Other matter (if any)	The other matter paragraph will be included in accordance with the requirements of the ISAs as applicable in Pakistan.  Other matter is a paragraph included in the auditor's report that refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.
Name of the engagement partner	Name of the engagement partner signing the audit report is to be stated. Previously, ICAP through its Auditing Technical Release 19 'Identification of Audit Engagement Partner in the Auditor's Report on the Financial Statements (Revised 2012)' had directed that where the auditor's report on the financial statements or the interim financial information is signed in the firm's name, the name of the engagement partner should be identified.
Signature, place / location and date	Signature, place / location and date are to be included as was done previously.

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## 4.2 Key Audit Matters

The most significant change brought about through the new format is the inclusion of Key Audit Matters in the auditor's report on the financial statements of listed companies. The requirements in relation to Key Audit Matters are explained below:

### What are Key Audit Matters?

Key Audit Matters (KAMs) are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements in the current period. KAMs are selected from matters that the auditor has already communicated to / discussed with TCWG. There is a focus on those matters which are of most significance.

In making this determination, the auditor shall take into account the following:

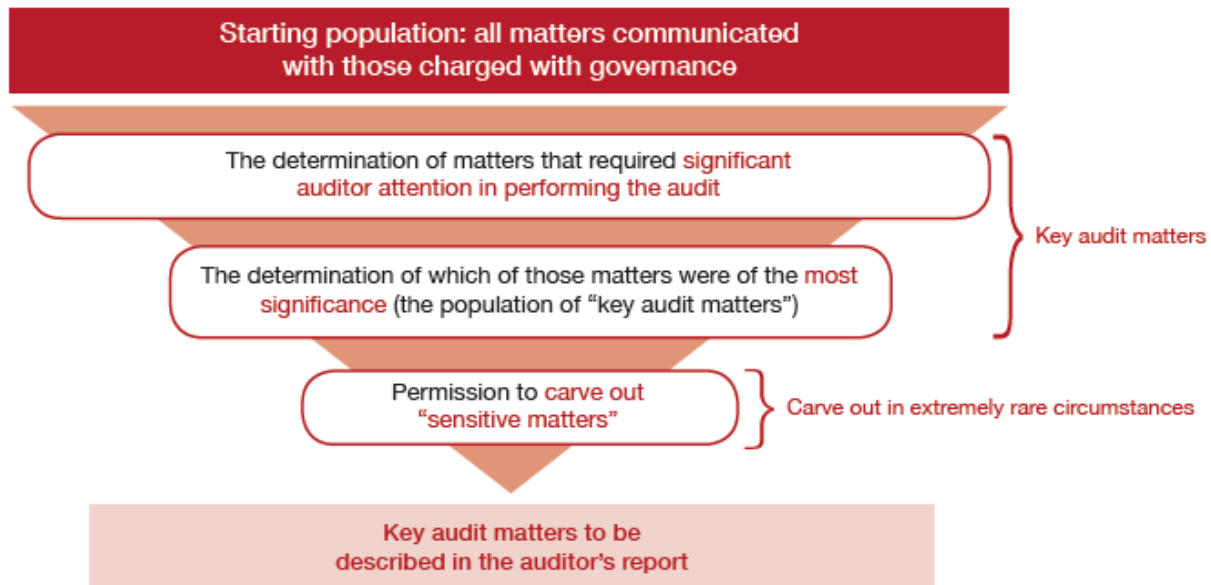
- (i) Areas of higher assessed risk of material misstatement, or significant risks identified in accordance with ISAs.
- (ii) Significant auditor judgments relating to areas in the financial statements that involved significant management judgment, including accounting estimates that have been identified as having high estimation uncertainty.
- (iii) The effect on the audit of significant events or transactions that occurred during the period.

### How will auditors select KAMs?

ISA 701 states that professional judgement will be needed to determine which, and how many, KAMs are to be included in the audit report. This will be an important as well as challenging judgement. KAMs will be drawn from matters discussed with TCWG. ISA 701 does not prescribe an exclusive list for KAMs, as that would be contrary to the notion of such matters being those of most significance in the audit.

KAMs are selected from those matters involving significant auditor attention during the course of the audit. This recognises that an audit is risk-based and areas of significant auditor attention often relate to complex matters and where significant management judgement is involved in the financial statements.

A demonstration of the selection process of KAMs is as follows:



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### ***4.3 Section for information other than the financial statements and auditor's report thereon***

The auditor's report shall include a separate section stating the following:

- A statement that management is responsible for the other information. Other information refers to financial or non-financial information (other than financial statements and the auditor's report thereon) included in an entity's annual report.
- Identification of:
  - Other information, if any, obtained by the auditor prior to the date of the auditor's report; and
  - For an audit of financial statements of a listed entity, other information, if any, expected to be obtained after the date of the auditor's report.
- A statement that the auditor's opinion does not cover the other information and, accordingly, the auditor does not express (or will not express) an audit opinion or any form of assurance conclusion thereon.
- A description of the auditor's responsibilities relating to reading, considering and reporting on other information as required under ISA.
- When other information has been obtained prior to the date of the auditor's report, either:
  - A statement that the auditor has nothing to report; or
  - If the auditor has concluded that there is an uncorrected material misstatement of the other information, a statement that describes the uncorrected material misstatement of the other information.

## 4.4 Other changes

Details of changes other than those described above are as follows:

Report form	Revised / new reporting requirements	Previous reporting requirements
Report on financial statements of a company other than a banking company  (Annexure-I)	Opinion as to whether investments made, expenditure incurred and guarantees extended during the year were for the purpose of the Company's business.  <b>Note:</b> The new requirement has added opinion for the guarantees extended and removed reference to the objects of the company.	Opinion as to whether: <ul style="list-style-type: none"> <li>the expenditure incurred during the year was for the purpose of the company's business; and</li> <li>the business conducted, investments made and the expenditure incurred during the year were in accordance with the objects of the company.</li> </ul>
Report on financial statements of a banking company  (Annexure-II)	Opinion as to whether investments made, expenditure incurred and guarantees extended during the year were in accordance with the objects and powers of the Bank / branches and the transactions of the Bank / branches which have come to the auditor's notice have been within the powers of the Bank / branches.  <b>Note:</b> The new requirement has added opinion for the guarantees extended and opinion on expenditure with reference to purpose of the Bank's / branches' business has been removed.	Opinion as to whether: <ul style="list-style-type: none"> <li>the expenditure incurred during the year was for the purpose of the Bank's / branches' business; and</li> <li>the business conducted, investments made and the expenditure incurred during the year were in accordance with the objects of the Bank / branches and the transactions of the Bank /branches which have come to the auditor's notice have been within the powers of the Bank / branches.</li> </ul>
Report to the members on the financial statements of insurer registered under the Insurance Ordinance, 2000  (Annexure-III)	Opinion as to whether investments made, expenditure incurred and guarantees extended during the year were for the purpose of the company's business.	Not included in the prescribed report.
Report on the consolidated financial statements  (Annexure-IV)	The report has been significantly revised. In addition to the structural changes described in paragraphs 4, paragraph 5 provides detail of other changes.	
Report on second quarterly (half yearly) financial statements  (Annexure-V)	No significant change.	
Report on Statement of compliance with the Listed Companies (Code of Corporate Governance) Regulations, 2017  (Annexure-VI)	No significant change.	

## ***5. Auditor’s report on the consolidated financial statements***

Rule 17C of the Companies (General Provisions and Forms) Rules, 1985 (i.e. Form 35C) allowed the auditor of the consolidated financial statements when rendering opinion thereon, to base the opinion solely on the reports of subsidiaries’ auditors in so far as it related to the amounts of those subsidiaries included in the consolidated financial statements (i.e. concept of division of responsibility).

For ready references, extracts from Form 35C are as follows:

*“.....We have also expressed separate opinions on the financial statements of xxx and its subsidiary companies except for xxx and xxx which were audited by other firm(s) of auditors whose report(s) has/have been furnished to us and our opinion, in so far as it relates to the amounts included for such company(ies), is based solely on the report(s) of such other auditors.....”*

With the issuance of the 2018 Regulations, the aforementioned concept of the division of responsibilities has been eliminated, thus making the group auditor responsible for the audit opinion on the consolidated financial statements, without making reference in the audit report to any other auditor involved in the audit of subsidiaries. The opinion paragraph of the audit report on the consolidated financial statements shall state as follows:

*“In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at xxx, and (of) its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with the accounting and reporting standards as applicable in Pakistan.”*

The section on Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements interalia includes and emphasizes this matter as follows:

*“Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.”*

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## **6. Others**

### **6.1 Penalty**

The 2018 Regulations state that in case of contravention of any requirement, penalty be determined in accordance with section 512(2) of the Companies Act, 2017.

Section 512(2) of the Companies Act, 2017 states that a contravention of any regulation shall be punishable with a penalty which may extend to Rs. 5 million and, where the contravention is a continuing one, with a further penalty which may extend to Rs. 100,000 for every day after the first during which such contravention continues.

### **6.2 Repeal**

Rules 17A, 17B and 17C of the Companies (General Provisions and Forms) Rules, 1985 (i.e. Forms 35A to 35D) have been repealed through the 2018 Regulations.

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