

Newsflash

A trail of financial transaction – Audit trail

April 2023



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Introduction

The Ministry of Company Affairs (MCA) vide its notification dated March 24, 2021 introduced the Companies (Accounts) Amendment Rules, 2021 with the proviso to rule 3(1) of the Companies (Accounts) Rules, 2014, which required every Company to maintain an audit trail feature in the accounting software used by them originally with an effective date of April 01, 2021.

The applicability of maintenance of Audit Trail by Companies was deferred twice and this requirement has now been made applicable from April 1, 2023.

On similar lines to make the audit trail functionality maintenance auditable, MCA introduced modifications to Rule 11 of the Companies (Audit and Auditors) Rules, 2014 which post deferment of one year is applicable from financial year April 1, 2022.

This change has brought in a new reporting clause in Auditor's report in form of Rule 11(g) which requires auditors to report on the use of accounting software by the Company for maintaining its books of accounts which has a feature of recording audit trail.

Amendments

Below is the quick summary of the amendments mentioned above that requires Companies now to maintain an audit trail and that requires auditors to report on such audit trails maintained:

Rule 11(g) of the Companies (Audit & Auditors) Rules, 2014	Rule 3(1) Companies (Accounts) Rules, 2014
<i>"used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated throughout the year for all transactions recorded in the software and the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention"</i>	<i>Provided that for the financial year commencing on or after the 1st day of April 2023, every company which uses accounting software for maintaining its books of account, shall use only such accounting software which has a feature of recording audit trail of each and every transaction, creating an edit log of each change made in the books of account along with the date when such changes were made and ensuring that the audit trail cannot be disabled."</i>

What is Audit Trial?

Audit Trail (or Edit Log) is a visible trail of evidence enabling one to trace information contained in statements or reports back to the original input source. Audit trails are a chronological record of the changes that have been made to the data. Any change to data including creating new data, updating or deleting data that must be recorded. Records maintained as audit trail may include the following information:

- **when** changes were made i.e., date and time (timestamp)
- **who** made the change i.e., User Id
- **what** data was changed i.e., data/transaction reference; success/failure.

Company's Obligation

The new statutory requirement necessitates a Company to ensure that the accounting software used by them has a functionality of creating an audit trail for books of account maintained and that such functionality is operating effectively throughout the year and that the Company should be in a position to provide sufficient audit evidences to its auditors to check the edit log and provide rationalisation towards the changes. Such edit log report has to be retained for a period of 8 years.

Further Books of accounts have been defined as 'Any software that maintains records or transactions that fall under the definition of Books of Account as per the section 2(13) of the Act will be considered as accounting software for purpose of Rule 11(g).'

To illustrate, if sales are recorded in a standalone software and only consolidated entries are recorded monthly into the accounting software, the sales software should also have the audit trail feature since sales invoices would be covered under the ambit of Books of Account.

Auditor Obligation

The new statutory requirement puts an obligation on the auditor to report that, whether the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated throughout the year for all transactions recorded in the software and the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention.

Nangia's Take

Even though the amendment via Rule 11(g) of the Companies (Audit & Auditors) Rules, 2014 is applicable w.e.f. 1/4/2022 the legal requirement pursuant to Rule 3(1) Companies (Accounts) Rules, 2014 has only come into force w.e.f. 1/4/23.

The objective of MCA for mandating the requirement of an audit trail feature in accounting software is to mitigate the chances of fraudulent transactions and manipulation in the books of accounts of the company and to bring in more transparency to the recording of the transactions.

With the help of an audit trail, an auditor can trace every step of the financial data of a particular transaction right from the general ledger and therefore audit trail provides better accountability and compliance; protection against fraud, and above all, the right information to the stakeholders.



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