

REGULATORY COMPLIANCE

NFRA Circular on Auditor Communication with TCWG

Effective Communication Between Statutory Auditors and Those Charged with Governance

Circular Reference

NF-25013/3/2025-NFRA

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National Financial Reporting Authority

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OVERVIEW

About This Circular

1 To Whom It Applies

All Listed Companies

Companies listed on recognized stock exchanges in India

Companies under Rule 3 of NFRA Rules, 2018

Unlisted public companies & private companies meeting specified thresholds

Auditors of Above Companies

Statutory auditors appointed under Section 139 of Companies Act, 2013

⚠ Why This Matters

NFRA's investigations into professional misconduct by some Auditors revealed widespread non-compliance with SA 260 and SA 265. **Every non-compliance impacts the governance framework of public interest entities and may ultimately erode investors' confidence.**

Subject Matter

In the course of discharging NFRA's statutory functions, it has been noticed that there is a need to strengthen the communications between:



Statutory Auditors (Auditors)

Responsible for audit of financial statements



Those Charged with Governance (TCWG)

Including Audit Committees (ACs)

In line with the requirements of the **Companies Act, 2013 (CA 2013)**, the **Standards on Auditing (SAs)** prescribed under CA 2013, and other relevant Rules and Regulations.

Board of Directors & Independent Directors

Key provisions of Companies Act, 2013 establishing auditor-TCWG communication obligations



Section 134 of CA 2013

Board of Directors

Financial Statement Approval

Section 134 and related Rules require that the financial statements, including consolidated financial statements, be **approved by the Board of Directors**.

Directors' Responsibility Statement

According to sub-section 5 of Section 134, this statement shall disclose the Board's assertions regarding:

- Adherence to applicable accounting standards
- Judgements/estimates on reasonable basis
- Prevention and detection of fraud
- Implementation of internal financial controls
- Selection and application of accounting policies
- Maintenance of adequate records for safeguarding assets
- Preparation on going concern basis
- Compliance with applicable laws



Schedule IV to CA 2013

Independent Directors

Integrity Obligation

Code for Independent Directors ("the Code") prescribed under Companies Act, 2013 casts an obligation on them to **satisfy themselves of the integrity of financial information** and that financial controls and the systems of risk management are robust and defensible.

Key Duties

Clause III of the Code casts several duties on independent directors:

1. Appropriate induction and regular updation of skills, knowledge and familiarity with the company
2. Remaining well informed about the company and external environment
3. Paying sufficient attention and ensuring adequate deliberations before approving related party transactions
4. Reporting concerns about unethical behaviour, actual or suspected fraud or violation of Code of Conduct
5. Where concerns are not resolved, insist that concerns are recorded in Board meeting minutes

Audit Committees & Auditors

Critical roles and responsibilities under Companies Act, 2013



Section 177 of CA 2013

Audit Committees

★ Critical Responsibilities

One of the critical responsibilities is to **review and monitor the Auditor's independence and performance, and the effectiveness of the audit process.**

☰ Key Areas of Significance

- Related party transactions
- Valuation of assets
- Risk management systems
- Discussions with Auditors before audit commences
- Inter-corporate loans and investments
- Evaluation of internal financial controls
- Major accounting entries involving estimates
- Post-audit discussions to ascertain concerns



Section 143 of CA 2013

Auditors

📄 Reporting Obligation

Sub-section 2 of section 143 requires the Auditor to **make a report to members of the company** on the accounts examined and the financial statements, inter alia, after taking into account the provisions of CA 2013, the accounting and auditing standards, and whether the financial statements give a true and fair view.

Further, **subsection 9 of section 143 of CA 2013 casts a statutory obligation on the Auditor to comply with the auditing standards.**

SA 260 (Revised) & SA 265

Two primary SAs governing auditor-TCWG communication requirements



SA 260 (Revised)

Communication with TCWG

Definition of TCWG

Paragraph 10(a) defines TCWG as **those with responsibility for overseeing the strategic direction of the company and obligations relating to accountability**. Auditor must determine appropriate persons within governance structure at start of audit.

Two-Way Communication Process

Mandatory two-way communication process that **must be documented**. Communicate audit approach, specialized skills needed (e.g., Fair Value Measurements, ECL computations), and seek TCWG's suggestions.

Board Communication Assessment

If communicating with sub-group (e.g., Audit Committee), auditor must **assess need to also communicate with full Board of Directors**.



SA 265

Communicating Deficiencies in Internal Control

Control Deficiencies Communication

Auditor must communicate **deficiencies in internal controls identified during audit** to both TCWG and Management. Must be communicated in writing and on timely basis.

Significant Deficiencies

Auditor determines whether deficiencies are **significant, individually or in combination**. Communication must explain their potential effects and provide sufficient context.

Written Communication Mandatory

Significant deficiencies must be communicated in writing on timely basis. Cannot rely solely on oral communication or presentations.

Important: Many other SAs including SQC 1 have specific communication requirements with TCWG. Refer to Annexure I of the circular for complete list.

NFRA OBSERVATIONS

Common Non-Compliances Observed by NFRA

Specific violations identified during investigations into professional misconduct

a Incorrect TCWG Identification

Incorrectly identified only Audit Committee or even Management Executives / Executive Directors as TCWG.

b Incomplete Communication

Communication process was incomplete and inadequately documented.

c No Two-Way Process

Failed to establish and document form, timing, and two-way nature of communication.

d Limited AC Presentations

Communications limited to presentation shortly before approval of financial statements, without adequate supporting documentation.

e Management = TCWG Error

Meetings and discussions with management were erroneously construed as communication with TCWG.

f Failure to Communicate

Unusual transactions: Supplier advances, circuitous dealings with promoter entities

g Non-Compliance Not Communicated

Instances of non-compliance with laws and regulations, were not communicated.

h RPT Issues Not Communicated

No communication of deficiencies in the entity's related party transaction policy and issues in related party transactions,

i IC Weaknesses Not Communicated

The Auditors failed to communicate identified weaknesses or the absence of internal controls to TCWG, including serious deficiencies

! **Critical Note:** Every non-compliance with these provisions is not just a procedural violation but impacts governance framework and may erode investor confidence.

Key Requirements & Implementation Framework

A comprehensive guide to auditor-TCWG communication framework covering six critical areas for effective implementation

01

Determining TCWG

Correct identification of Those Charged With Governance

02

Two-Way Communication

Establishing robust, documented communication processes

03

Audit Planning Matters

Pre-audit meeting agenda and strategy

04

During Audit Findings

Periodic communication of significant matters

05

SA 265 - IC Deficiencies

Mandatory written communication requirements

06

Independence & Ethics

Auditor independence declaration and compliance

Determining TCWG & Establishing Two-Way Communication

01 Appropriate Determination of TCWG

Who Constitutes TCWG?

Per SA 260 (Revised) Para 10(a): **Those with responsibility for overseeing strategic direction and obligations relating to accountability of the company.**

- 1. Board of Directors:** Primary TCWG under Companies Act 2013. Responsible for overall governance oversight.
- 2. Audit Committee:** Sub-group of Board. May be treated as TCWG but requires assessment of Board communication need.
- 3. Other Sub-groups:** Risk committee, governance committee based on entity's governance structure.

Documentation Requirements

Auditor shall **determine and document TCWG at the start of the audit** (SA 260 Para 11). This includes evaluation of entity's governance structure, assessment of Board communication need, identification of appropriate person(s), and written record in audit work papers.

When to Communicate with Full Board?

If Audit Committee is treated as TCWG, auditor must assess whether communication with full Board is also required for significant matters beyond AC's authority, matters affecting overall governance, or strategic decisions requiring Board oversight.

02 Establishing Robust Two-Way Communication

Joint Responsibility

It is a **joint or collective mandatory obligation** of the Company's Governing Body (Board of Directors, Audit Committee, Management, and Auditors) to establish a robust, effective two-way communication.

Communication Framework Elements

- Objective and Purpose of Two-way Communication
- Name and details of Nodal Persons from Board and Audit Engagement Team
- Expectations of Auditors from Board regarding two-way communication
- Summary of prescriptions of key SAs requiring communication
- Policy and Process of updating or escalating matters to TCWG
- Policy and process of documenting views/instructions/actions of TCWG
- Frequency of meetings and expected Agenda matters
- All significant communications shall be in writing and formally acknowledged

Recommended Pre-Audit Discussions

It is recommended (though not mandatory) that the Auditor and TCWG discuss at the start of the financial year: (i) The planned scope and timing of the audit (SA 260 Revised, Paragraph 15); and (ii) The expectations of two-way communication, including typically expected agenda items.

REQUIREMENTS

Appropriate Documentation & Timely Communication

Appropriate Documentation

a Written Communication Requirement

Communication shall be in writing & shall form part of Audit Working Papers & Agenda items of meetings of Board / Audit committee. In case of oral communication, it shall be documented in writing and shall include the date, time and details of the persons involved in the communication.

b Unambiguous and Specific

Written communication shall be unambiguous and specific in respect of issues or matters for the consideration of both parties.

c Views and Suggestions

Communication shall also contain the views/suggestions of TCWG on the subject matter raised by the Auditors and vice versa.

d Sufficient Duration

Duration of discussion between the Auditors and TCWG must be sufficient for a meaningful outcome.

Timely Communication with TCWG/ACs

Regular Two-Way Communication

Regular two-way communication between the Auditors and TCWG/its sub-groups/nodal persons throughout the audit period is key to achieving the objectives of SA 260 (Revised) and SA 265.

Mandatory Meeting Frequency

Auditors and TCWG should meet in person or virtually at least twice a year:

1 Before Commencement of Audit

Discuss audit strategy, scope, materiality, key risks

2 Before Approval of Financial Statements

Discuss significant findings, concerns, conclusions

Situations Warranting Additional Discussions

There may be situations warranting discussion:

- i. Where Auditors experience difficulty obtaining sufficient appropriate audit evidence,
- ii. Where Auditors have reason to believe a potential fraud,
- iii. Where they have observed significant weaknesses in internal controls

In such situations, Auditors shall request a meeting with TCWG in writing, and TCWG shall either accede to the request or, in writing, communicate the reasons for declining it.

REQUIREMENTS 03 & 04

Agenda Matters: Audit Planning & During Audit

03 Audit Planning Matters

Required under SA 260 (Revised) as reiterated in NFRA Circular

Audit Strategy & Plan

Overview of planned scope and timing of the audit, including overall audit approach & methodology.

Materiality Levels

Determination and application of materiality thresholds, including performance materiality

Risk of Material Misstatement (ROMM)

Significant risks identified, including fraud risks and areas with higher risk of material misstatement.

Fraud Risk Assessment

Risks of material misstatement due to fraud, including management override of controls and revenue recognition risks.

Areas Involving Significant Management Judgment

- | | |
|---|---|
| <ul style="list-style-type: none">• Valuation: Fair value measurements, business combinations, complex financial instruments• Going Concern: Assessment of entity's ability to continue as going concern | <ul style="list-style-type: none">• Impairment: Goodwill, intangible assets, PPE impairment assessments• ECL: Expected Credit Loss calculations under Ind AS 109 |
|---|---|

Internal Control Environment & Use of Experts

Assessment of internal financial controls over financial reporting and engagement of auditor's experts or management's experts for specialized areas.

04 During Audit - Status & Significant Findings

Matters to be discussed periodically throughout the audit engagement

Significant Audit Difficulties

- Delays in obtaining information or documentation from management
- Restrictions on access to people, information, or premises

Significant Unusual Transactions

Transactions outside normal course of business: Supplier advances with unusual terms, borrowing and lending arrangements with atypical structures, circuitous dealings with promoter or group entities.

Related Party Transactions (RPTs)

Deficiencies in RPT policy and implementation: Inadequate RPT policy framework, promoter/group transactions not at arm's length, non-disclosure or incomplete disclosure of RPTs.

Non-Compliance with Laws & Regulations

Instances of non-compliance with applicable laws identified during audit

Internal Financial Control Deficiencies

Significant weaknesses or absence of internal controls over financial reporting identified during audit procedures.

Differences of Opinion & Suspected Fraud

Disagreements on accounting treatments, estimates, disclosures, or scope of audit work.
Any suspected or identified fraud, including management override of controls, must be communicated immediately to TCWG.

REQUIREMENTS 05 & 06

SA 265 - Internal Control Deficiencies & Independence Requirements

05 SA 265 - Internal Control Deficiencies

Written communication is mandatory for significant deficiencies

What is a Significant Deficiency?

A deficiency or combination of deficiencies in internal control that **in the auditor's professional judgment, requires the attention of those charged with governance.**

Factors to Consider

- Susceptibility to loss or fraud
- Subjectivity and complexity of estimates
- Volume of activity in affected accounts

Written Communication Requirements

Significant deficiencies must be communicated in writing and include:

- Description of the deficiencies
- Sufficient context for understanding
- Explanation of potential effects
- Clarification that audit not for ICOFR opinion

Auditor's Responsibilities - Three-Step Process

- 1 Identify** Determine if deficiencies in internal control have been identified during audit
- 2 Evaluate** Assess whether deficiencies constitute significant deficiencies
- 3 Communicate** Communicate in writing on timely basis to TCWG and management

06 Independence & Ethics Requirements

Mandatory communication as per NFRA Circular

Auditor Independence Declaration

Confirmation of compliance with independence requirements of Code of Ethics, disclosure of all relationships that may affect independence, written representation from auditor regarding independence.

Non-Audit Services

Services provided by auditor that may impair independence: Complete list of non-audit services provided during the period, fees for audit and non-audit services separately disclosed, assessment of whether services impair independence, AC approval for permitted non-audit services.

Network Firm Relationships

Relationships with network firms that may create threats to independence: Disclosure of network firm relationships, services provided by network firms to entity, independence of auditors of domestic and foreign components, related party relationships with network firms.

Safeguards Against Threats

Measures implemented to mitigate identified threats to independence: All significant threats to independence identified, safeguards implemented to eliminate or reduce threats, rotation of audit partner (if applicable), cooling-off periods for former audit firm personnel.

Key Takeaways & Action Items



Correct TCWG Identification

Determine and document TCWG at the start of audit. **Board is primary TCWG;** assess Board communication need when AC is treated as TCWG.



Robust Two-Way Communication

Meet at least twice annually – before audit commencement and before financial statement approval. All communication must be documented.



Written Communication

Significant matters, internal control deficiencies, and independence issues must be communicated in writing. Oral communications must be documented.



Timely Escalation

Communicate significant findings, unusual transactions, suspected fraud, and non-compliance promptly. **Do not wait until final reporting.**

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Effective auditor-TCWG communication is not merely procedural—it strengthens governance oversight, enhances audit quality, and protects public interest.

Action Checklist

- ✓ Establish documented communication frameworks
- ✓ Meet at least twice annually
- ✓ Ensure all significant matters are communicated in writing
- ✓ Maintain proper documentation as part of audit work papers

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