

Provisions relating to Audit and Auditors –
Rotation of Audit, Ceiling on Audits etc.,
Mandatory Internal Audit, Reporting on Frauds
and Auditors responsibility, Auditor's focus areas
– compliances and responsibilities



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Historic Year for Company Law - 2013



★★★★2013★★★★ A Historic Year

- Change on Economic environment
- Limitations of Companies Act, 1956
- The “S” frauds – Satyam, Sahara and Saradha
- Self-Regulation over Regulatory Control
- Undue hurry to pass the legislation before elections

What the New Act Seeks to



- The Companies Act, 2013 seeks to
 - Corporate Governance
 - Corporate Social Responsibility
 - Audit Accountability and increased focus on professionals/auditors
 - Enhanced disclosure norms
 - Related party transactions – from control based norms to disclosure based norms
 - Prohibition of insider trading and forward deals
 - Fraud defined wider than Indian Contract Act
 - Class Action suits
 - Regulation of the Act under Central Government

Provisions relating to Audit and Auditors



- **The Broader Perspective**

- At par with global practices
- Flexibility in accounting
- Compliance focused
- Enhanced accountability on the part of companies.
- Audit accountability
- Vigil mechanism introduced
- Class Action suits
- Enhanced monitoring of quality and new regulatory structure (NFRA)
- Innovative concepts – Audit rotation, re-opening of past financial statements, auditing standards, experts, KMP.

New concepts



- **First-timers**
 - Financial year
 - Key Managerial Personnel (KMP)
(MD/CEO/WTG/CS/CFO/Others)
 - E-books
 - Re-opening / Recasting of Accounts
 - Voluntary revision of financial statements
 - Internal audit
 - Auditing Standards
 - Secretarial Standards
 - National Financial Reporting Authority

Definitions



- **‘Book and paper’ and ‘book or paper’ [section 2(12)]**
 - ‘Book and/or Paper’ include books of account, deeds, vouchers, writings, documents, minutes, registers maintained on paper or electronic form.
- **Books of account [Section 2(130)]**
 - Books of account includes records maintained in respect of:-
 - ✦ (i) all sums of money received and expended by a company and matters in relation to which the receipts and expenditure take place.
 - ✦ All sales and purchases of goods and services of the company
 - ✦ The assets and liabilities of the company; and
 - ✦ The items of cost as may be prescribed under section 148 in the case of a company which belongs to any class of companies specified under that section.

Definitions



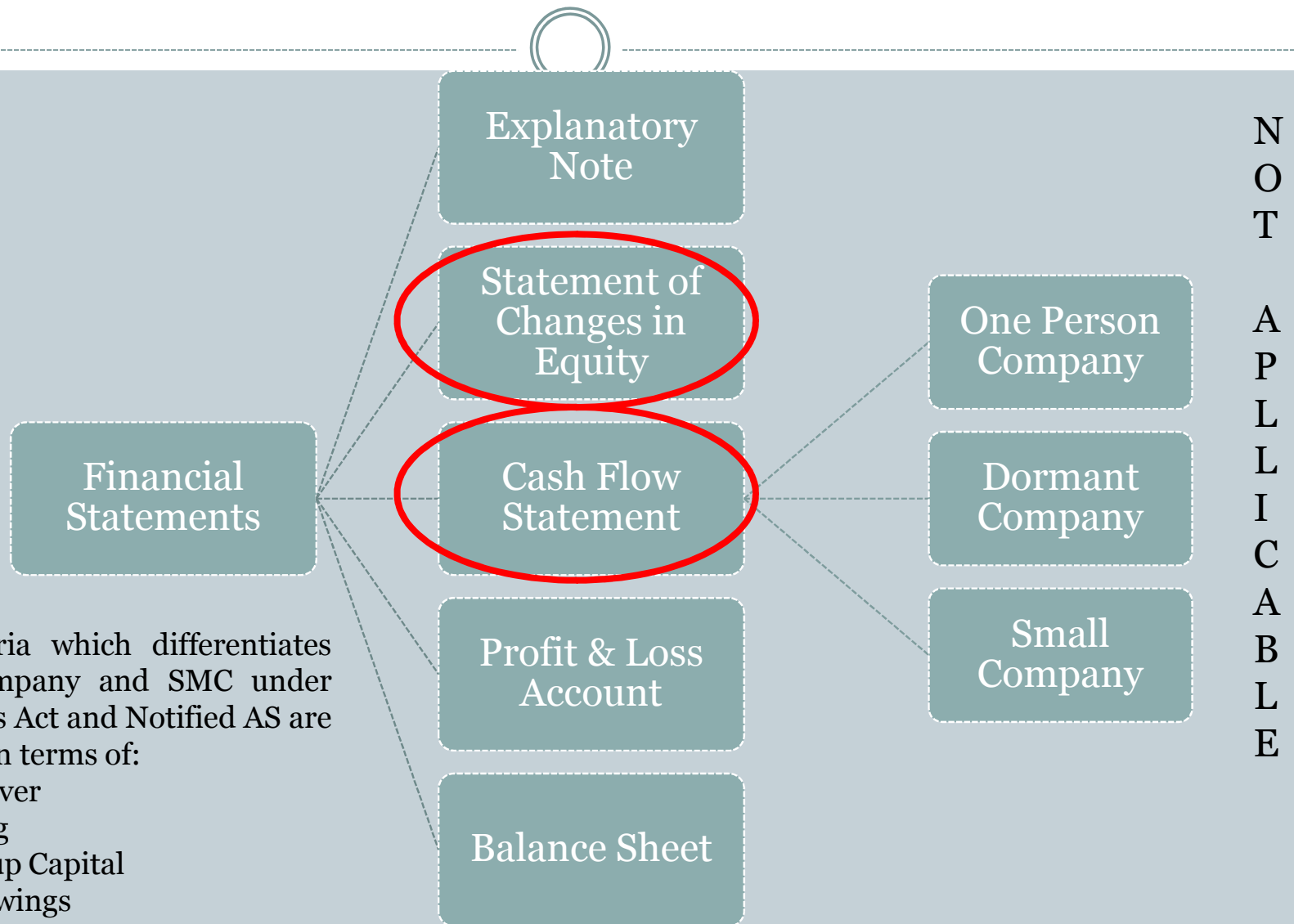
- **Associate Company [Section 2(6)]**
- 2(6) defines “Associate company”, in relation to another company, means a company in which that other company has a significant influence, but which is not a subsidiary company of the company having such influence and includes a joint venture company.
- *Explanation.*—For the purposes of this clause, “significant influence” means control of at least twenty per cent. of total share capital, or of business decisions under an agreement;

Definitions



- **Financial Statements [Section 2(40)]**
 - defines “financial statement” in relation to a company, includes—
 - (i) a balance sheet as at the end of the financial year;
 - (ii) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;
 - (iii) cash flow statement for the financial year;
 - (iv) a statement of changes in equity, if applicable; and
 - (v) any explanatory note annexed to, or forming part of, any document referred to in sub-clause (i) to sub-clause (iv):
 - Provided that the financial statement, with respect to One Person Company, small company and dormant company, may not include the cash flow statement;

Financial Statements [Section 2(40)]



The Criteria which differentiates Small Company and SMC under Companies Act and Notified AS are Different in terms of:

- a) Turnover
- b) Listing
- c) Paid-up Capital
- d) Borrowings

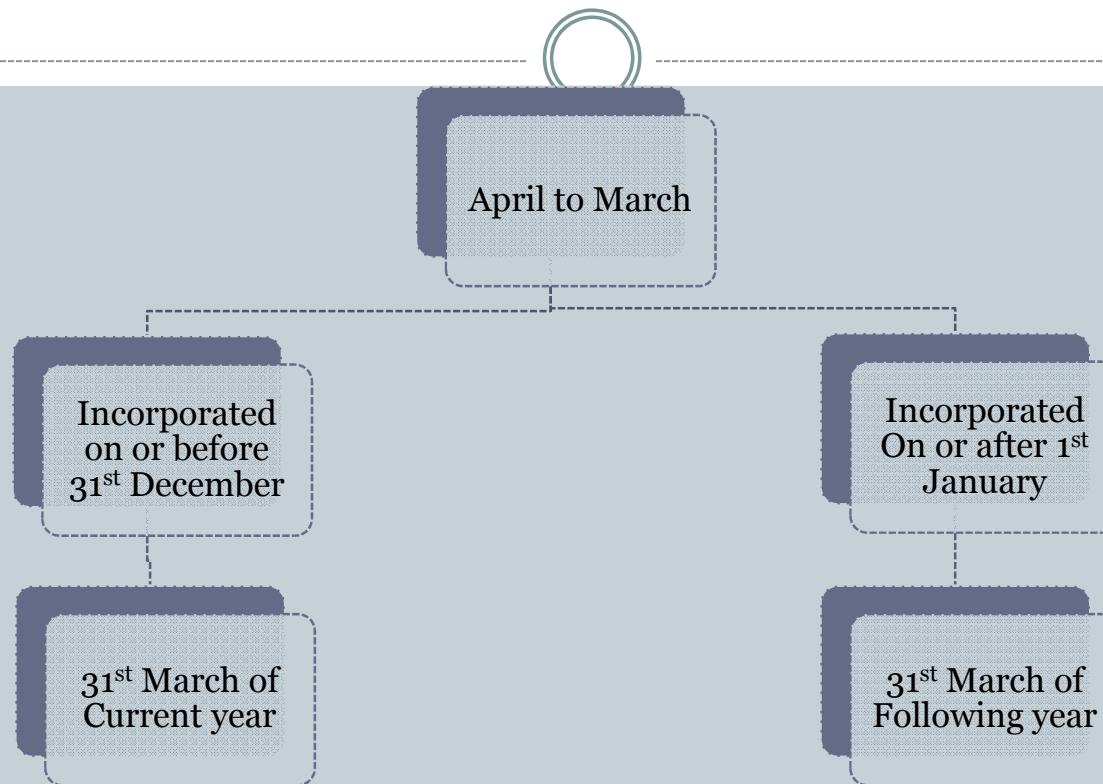
Definitions



○ Financial Year [Section 2(41)]

- 2(41) defines “financial year”, in relation to any company or body corporate, means **the period ending on the 31st day of March every year**, and where it has been incorporated on or after the 1st day of January of a year, the period ending on the 31st day of March of the following year, in respect whereof financial statement of the company or body corporate is made up:
- Provided that on an application made by a company or body corporate, which is a holding company or a subsidiary of a company incorporated outside India and is required to follow a different financial year for consolidation of its accounts outside India, the Tribunal may, if it is satisfied, allow any period as its financial year, whether or not that period is a year:
- Provided further that a company or body corporate, existing on the commencement of this Act, shall, within a period of two years from such commencement, align its financial year as per the provisions of this clause;

Financial Year



Adopt different Financial Year on application to the Tribunal. By companies having holding or subsidiary company outside India and require to prepare consolidation financial statements outside India. (No other reason for application) Not necessary to have 12 months for those companies

Existing companies get two years to toe the line.

Definitions



- Definition of *Financial year* changed – ‘April to March’
 - Lack of flexibility
 - Increased cost of compliance
- New company (after 1 January) : 31st March of the following year
- Transition Period : 2 years from commencement of the Act
- Exception/ exemption :
 - ❖ Holding/ subsidiary of a company incorporated outside India and required to follow different financial year for consolidation of financial statements outside India
 - ❖ Tribunal’s approval required

Definitions



- **Net Worth [Section 2(57)]**
 - defines “net worth” means the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation;
- **Turnover [Section 2(91)]**
- “turnover” means the aggregate value of the realisation of amount made from the sale, supply or distribution of goods or on account of services rendered, or both, by the company during a financial year;

Definitions



- **Small Company [Section 2(85)]**
 - “small company” means a company, other than a public company,—
 - (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than five crore rupees; and *[the word ‘or was replaced by the word ‘and’ vide Order No. S.O. 504(E) dated 13-2-2015 by the Ministry of Corporate Affairs]*
 - (ii) turnover of which as per its last profit and loss account does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than twenty crore rupees:
 - Provided that nothing in this clause shall apply to—
 - (A) a holding company or a subsidiary company;
 - (B) a company registered under section 8; or
 - (C) a company or body corporate governed by any special Act;

Definitions



- **Subsidiary company [Section 2(87)]**
- “subsidiary company” or “subsidiary”, in relation to any other company (that is to say the holding company), means a company in which the holding company—
- (i) controls the composition of the Board of Directors; or
- (ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:
- Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.
- *Explanation.*—For the purposes of this clause,—
- (a) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;
- (b) the composition of a company’s Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;
- (c) the expression “company” includes any body corporate;
- (d) “layer” in relation to a holding company means its subsidiary or subsidiaries;

How to Consolidate?



Particulars	Case I	Case II	Case III
Equity capital	100/100	30/100	0/100
Convertible Preference capital	100/200	200/200	200/200
Holding to Total Paid up capital	200/300	230/300	200/300
% holding in equity shares	100%	30%	0%
% holding in total paid up capital	67%	77%	67%
Subsidiary as per Companies Act?	Yes	Yes	Yes
Subsidiary as per AS 21?	Yes	No	No
Associate as per AS 23?	NA	Yes	No
Under Companies Act 2013	Subsidiary	Subsidiary	Subsidiary
Under AS	Subsidiary	Associate	No consolidation

Definitions



- **Sick Company [Section 253(1)]**

- “Where on a demand by the secured creditors of a company representing fifty per cent. or more of its outstanding amount of debt, the company has failed to pay the debt within a period of thirty days of the service of the notice of demand or to secure or compound it to the reasonable satisfaction of the creditors, any secured creditor may file an application to the Tribunal in the prescribed manner along with the relevant evidence for such default, non-repayment or failure to offer security or compound it, for a determination that the company be declared as a sick company.

Books of Accounts



- For every financial year, every company shall prepare and keep, including that of its branches:
 - Books of account
 - Other relevant books and papers
 - Financial statement
- In case of branches, proper summarised returns, say quarterly, sent by the branches shall be maintained by the registered office.
- It shall be on accrual basis and in according to double entry system of accounting
- Kept at the registered office. If any other place, ROC to be notified within 7 days of the decision to keep at such other place

Books of Accounts



- Books of accounts and other relevant books can be maintained in electronic mode (as defined by the Information Technology Act, 2000)
- Precautions such as display in legible form, not capable of being altered, in the format in which they were originally generated, proper system of storage, retrieval, back-up, display and printout as the Board/Audit Committee may deem fit.
- The company shall intimate to ROC on annual basis while filing the financial statements following information:
 - Name and internet protocol address of the service provider
 - Location of the service provider
 - Where the records are maintained on cloud, such address as provided by the service provider
 -

Books of Accounts



- Rule 9.1 - 9.2
- Proper system for storage, retrieval, display or printout of the electronic records shall be ensured
- Electronic record shall remain complete , unaltered and in a legible form
- Electronic mode –as defined in Section 2(1)(t) of Information Technology Act, 2000-data, record , image stored in electronic form/micro film/micro fiche

Books of Accounts



- Inspection of books /financial information by directors(themselves and not through their attorneys). In case of subsidiary, inspection may be by a person authorised by the Board by its resolution. Officers and employees to co-operate. Provide financial information within 15 days of the request.
- Books etc., shall be maintained and kept in good order for a period of immediately preceding eight financial years. However where investigation is ordered, the books to be maintained for such longer period.
- MD/WTD-Finance/CFO or any other person so authorised who contravenes the provisions – penalty ranging from Rs. 50,000 to Rs. 500,000 and imprisonment upto one year or both.

Financial Statements



- Financial statements shall give a true and fair view of the state of affairs of the company and in accordance with the applicable Accounting Standards.
 - Not applicable in case of a banking company, insurance company or a company engaged in supply/generation of electricity or such other class of companies to which the form of financial statement has been specified under the statute governing such class of companies.
- Financial statements shall be laid at every annual general meeting. In case of subsidiaries, consolidated financial statement and a statement containing salient features of the financial statement of its subsidiary(ies) [Form No. AOC 1] shall also be laid at the AGM.
- In case of non-compliance of Accounting Standards, to disclose the fact of such non-compliance, the deviation, the reasons for such deviation and the impact thereof.

Financial Statements



- Balance Sheet and Statement of Profit & Loss Account in the prescribed format – Schedule III.
- Financial statement of the company including consolidated financial statements, if applicable, should be approved by the Board of Directors, before such statements are signed.
- Financial statement should be signed on behalf of the board by at least the Chairperson of company, duly authorised by board, or two directors of whom one should be the managing director/ Chief executive officer, Chief financial officer and company secretary, if any, in the company

Financial Statements



- One person company's financial statements shall be signed by only one director. Such sign is required for submission of financial statements to the auditor for his report
- Auditors report is required to be attached to every financial statement
- Board report shall be attached to the statements laid before the company in general meeting
- Signed copy of financial statements (including cash flow statement) shall be issued / circulated / published alongwith copy of –
 - ❖ notes to accounts forming part of financial statements
 - ❖ auditor's report thereon
 - ❖ board's report

Financial Statements



- Rule 9.10
- Board report to contain a separate section wherein a report on the performance and financial position of each of the subsidiaries, associates and joint venture companies included in the consolidated financial statement is presented.

Depreciation



- Schedule II (Section 123)
- Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.
- Depreciable Amount = $[\text{Cost} - \text{Residual Value}]$
- Useful Life of asset is
 - the period over which an asset is expected to be available for use by an entity; or
 - the number of production or similar units expected to be obtained from the asset by the entity.
- Depreciation includes amortisation.
- It contains only useful lives of tangible assets and does not prescribe depreciation rates.

Depreciation



- The depreciation shall be calculated on a *pro rata basis*
 - In the case of additions, from the date of such addition or,
 - In case such asset has been sold, discarded, demolished or destroyed up to the date thereof.
- Component approach mandatory.
 - Where cost of a part of the asset is significant to total cost of the asset and useful life of that part is different from the useful life of the remaining asset, useful life of that significant part shall be determined separately.

Depreciation



- **Transitional Provisions:**
- From the date this Schedule comes into effect, the carrying amount of the asset as on that date—
 - (a) shall be depreciated over the remaining useful life of the asset as per this Schedule;
 - (b) after retaining the residual value, shall be recognised in the opening balance of retained earnings where the remaining useful life of an asset is NIL.
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- “*Continuous process plant*” means a plant which is required and designed to operate for 24 hours a day.
- Factory Buildings does not include offices, godowns, staff quarters.

Depreciation



- Extra Shift Depreciation working simplified by the 2013 act-
 - Will apply to P&M items subject to general rate i.e., useful life of 15 years
 - **For Double shift:** 50% more depreciation for that period for which asset used.
 - **For Triple shift:** 100% more depreciation for that period for which asset used.
 - **Not applicable to** Items marked NESD in the schedule.

Depreciation



- Illustration

Nature of asset	Act, 2013		Act 1956	Increase	% change
	Useful Life	Deemed rate	Rate		
General P & M	15 yrs	6.35%	4.75%	1.58%	33.33
General F & F	10	9.50%	6.33%	3.17%	50.08
Office Equipments	5	19%	4.75%	14.25%	300
Desktop/Laptop etc.,	3	31.67%	16.21%	15.46%	95.35
Electrical Installation Equipments	10	9.50%	4.75%	4.75%	100

Financial Statements



- The Central Government may on its own or on an application made to it, exempt by notification, a class or classes of companies, from complying with the provisions relating to the financial statements on the grounds of public interest, whether unconditionally or subject to such conditions as it may deem fit.
- Contravention :- MD/WTD-Finance/CFO or any other person so authorised who contravenes the provisions – penalty ranging from Rs. 50,000 to Rs. 500,000 and imprisonment upto one year or both.

Financial Statements



- Member's right to copies of audited financial statements.
- Abridged financial statements in Form AOC 3 may be attached to Directors' Report, Notice etc.,
- To file the financial statements in XBRL form [alongwith Form No. AOC 4] to be filed with ROC within thirty days of AGM. Accounts of subsidiaries also to be filed. Procedure fo filing in case of unadopted accounts or where AGM is not held, is specified.
- All listed company and prescribed public companies may send notice and financial statements by electronic mode. Otherwise as specified in Section 20 of the Act.
- OPC to file the financial statements within 180 days of the financial year end.

Financial Statements



- Revision/Re-opening of accounts by an order of the Court/Tribunal:
 - on an application made by the Central Government, the Income Tax Authorities, SEBI, any other statutory regulatory body or authority or any person concerned that the relevant earlier accounts were prepared in a fraudulent manner or the affairs of the company were mismanaged during the relevant earlier period, casting doubt on the reliability of the financial statement
 - The revised/re-cast accounts shall be final

Financial Statements



- **Revision of accounts by an order of the Tribunal:**
 - On an application made by the company, where it appears that the financial statements and the Board's report do not comply with the applicable provisions of Companies Act 2013 and that revised financial statement or report be prepared for the three preceding financial years
 - Representations of Central Government and the Income tax authorities to be taken into account before passing such order
 - Revised financial statements/report shall not be prepared or filed more than once.
 - Detailed reasons for revision to be disclosed in Board's Report.
 - The revision to be confined to comply with the applicable provisions of law.

Financial Statements



- Functions of present auditor towards revised financial statements:
 - ❖ Carry out audit procedures on revised financial statements
 - ❖ Issue revised audit report
 - ❖ Revised report to contain reasons for revision in bold
 - ❖ Revised financial statements to be signed in manner specified in Section 134 of the Act.

Financial Statements



- Preparation of consolidated financial statements by holding company of its and its subsidiaries / associates / joint ventures is compulsory
- Subsidiary includes associate company and joint venture
- Consolidated financial statements should comply with accounting standards
- Wherever applicable, consolidated financial statements are to be laid before the Annual General Meeting, in addition to its own financial statements
- Company is also required to attach the accounts of its foreign subsidiary which does not have place of business in India

Consolidated Financial Statement (CFS)



Earlier :

- * Clause 32 of the Listing Agreement mandates Listed Companies to prepare CFS
- * Neither AS 21 nor Companies Act 1956 requires other company to prepare CFS



Companies Act 2013 :

- * Mandatory for all Companies to prepare CFS in respect of the Subsidiary, Associate, JV Co.
- * CFS will have to be done in addition to SFS
- * CFS should be prepared in same form and manner as Standalone Financial Statement (SFS) of holding company.



Impact :

- * All companies including private companies need to prepare CFS. They need to gear up their financial reporting process for the same.
- * CFS should comply with notified AS
- * Reopen and revision of accounts mandatory to CFS also

Financial Statements



- **Consolidated financial statements now mandatory for all classes of companies**
 - Increase the cost of compliance
 - Duplication of information*: requirement to give *summary statement for all subsidiaries / associates / joint ventures continues*

[General Circular No. 39/2014 dated 14th October, 2014 states that in the CFS, the company would need to give all disclosures relevant for CFS only.]*

Financial Statements



- Consolidated financial statements shall be prepared in the same form and manner as that of its own. Consolidated financial statements shall be subject to same provisions as applicable to financial statements, so far as they relate to preparation, adoption and audit of financial statements
- A separate statement in prescribed form containing salient features of financial statement of its subsidiary or subsidiaries required to be attached along with its own financial statement
- Central Government empowered to prescribe for consolidation of accounts of companies
- Central Government empowered to exempt any company or class of companies from compliance of requirements of Section 129 in public interest

Content of Directors' Report



- Extract of Annual Return
- Number of meetings held
- Directors' Responsibility Statement
 - Application of Accounting Standard and explanation for material departure, if any.
 - Statement of Accounting Policies, judgements and estimates being reasonable and prudent to give true and fair view.
 - Maintenance of Accounting records in accordance with the provisions of the Act, safe-guarding of assets and prevention and detection of fraud.
 - Declaration of going concern

Content of Directors' Report



- Directors' Responsibility Statement (contd.)
 - Policy, adequacy and effective operation of Internal financial controls (for listed companies)
 - Setting up proper system, which is adequate and operating effectively, to ensure compliance with laws.
- Declaration by Independent Directors that they meet the criteria of independence.
- Directors' appointment and remuneration policy – for listed companies
- Explanation/comment on every qualification, reservation or adverse remark or disclaimer made by the Statutory Auditor and the Company Secretary

Content of Directors' Report



- Particulars of loans, guarantees and investments
- Particulars of contracts/arrangements made with related parties
- State of company's affairs
- Transfer to Reserves
- Dividend recommendation
- Material changes/commitments made after the date of Balance Sheet.
- Conservation of Energy, Technology and absorption.

Content of Directors' Report



- Actual foreign exchange earnings and outgo.
- Development and implementation of risk management policy
- Identification of elements of risk which may threaten the existence of the company.
- CSR policy
- Formal annual evaluation of performance of the Board and its committees – for listed companies and public companies with paid up capital > Rs. 25 crores

Content of Directors' Report



- Performance and financial position of each subsidiary, associate and joint venture including addition / deletion of such entities
- Change in the nature of business
- Details of directors and key managerial personnel – their appointments/resignations, if any.
- Details of deposits
- Significant and material orders passed by the regulators/ courts/ Tribunals/ impacting the going concern status.

Audit & Auditors

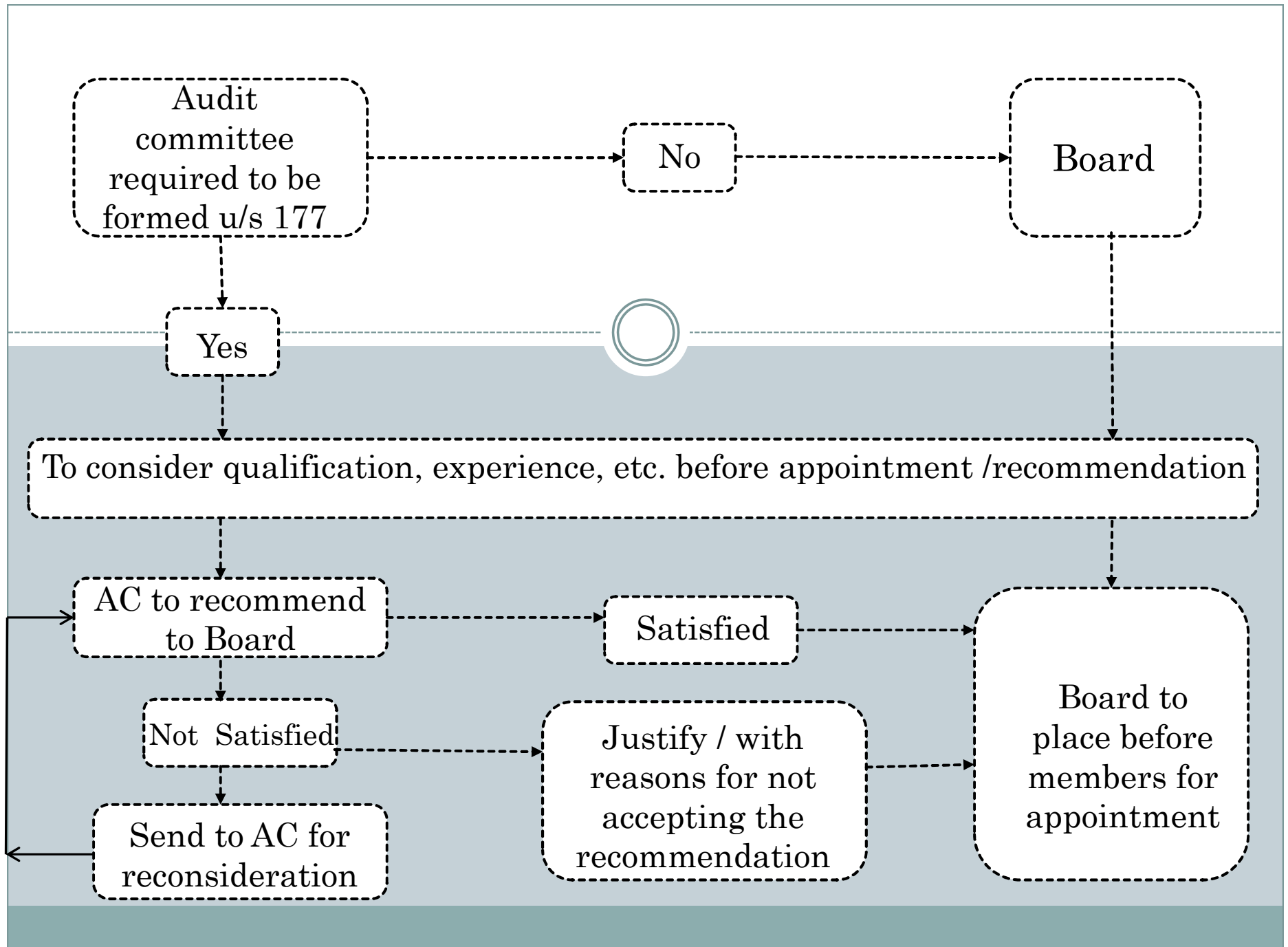


- Section 138: Internal Audit
- Section 139: Appointment of auditors
- Section 140: Removal, resignation of auditor and giving of special notice
- Section 141: Eligibility, Qualifications and Disqualifications of auditors
- Section 142: Remuneration of Auditors
- Section 143 : Powers & Duties of auditors
- Section 144 : Auditor not to render certain services
- Section 145 : Auditors to sign audit reports etc.
- Section 146 : Auditors to attend General Meeting
- Section 147 : Punishment for contravention

Audit & Auditors



- Appointment of First Auditors
 - For Government Companies –
 - ✦ CAG* to appoint first auditors within 60 days of its incorporation.
 - ✦ If not so appointed, Board to appoint within 30 days thereafter.
 - ✦ If not so appointed, Members to appoint within 60 days thereafter.
 - For Companies other than Government Companies –
 - ✦ Board to appoint within 30 days of its incorporation.
 - ✦ If not so appointed, Members to appoint at an EGM within 90 days thereafter.
- Appointment valid till the 1st AGM
- *Subsequent auditors to be appointed by CAG within 180 days of the end of the financial year.



Appointment or Reappointment Of Auditor

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graph TD; A[Appointment or Reappointment Of Auditor] -.-> B[Individual as an Auditor]; A -.-> C[Audit Firm]; B -.-> D[Not more than 5 Consecutive years]; C -.-> E[Not more than 10 Consecutive years];
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Individual as an Auditor

Not more than
5 Consecutive
years

Audit Firm

Not more than
10 Consecutive
years

Audit & Auditors



- Auditors – Individual practising Chartered accountant or a firm of chartered accountants can be appointed as auditors.
- LLPs can be appointed as auditors, In case of multi-disciplinary partnership firms, the financial statements to be signed by CA. Guidelines yet to be issued by ICAI.
- Term of Appointment – Individual ≤ 5 years*
- - Firm ≤ 10 years*
- * ratification at each AGM
- Proposed auditor to submit certificate of eligibility u/s Section 141 of the Act. File notice of appointment within 15 days thereof with ROC by the company [Form No. ADT 1]
- Cooling period of 5 years after above term
- File the fact of appointment in Form No. ADT 1



Illustration



Number of Consecutive years for which an audit firm has been functioning as an auditor in the same company as on today	Maximum number of consecutive years for which the firm may still be appointed in the same company (including transitional period)	Aggregate period for which the firm can be appointed auditor
10 years or more	3 years	13 years or more
9 years	3 years	12 years
8 years	3 years	11 years
7 years	3 years	10 years
6 years	4 years	10 years
5 years	5 years	10 years
4 years	6 years	10 years
3 years	7 years	10 years
2 years	8 years	10 years
1 year	9 years	10 years

Audit & Auditors



- Retiring auditor re-appointed unless:
 - He is disqualified for appointment as auditor
 - Has expressed his unwillingness to act as auditor
 - Special resolution passed to
 - ✦ Appoint another person as auditor
 - ✦ Refuse to appoint him/her/them as auditor
- Where no new auditor is appointed, the existing auditor to continue.
- Joint auditors can be appointed, provided their term does not complete in the same year.

Audit & Auditors



- Rotation of auditors
- Applicability
 - All listed companies
 - Unlisted public companies with paid-up capital > Rs. 10 crores
 - Private companies with paid-up capital > Rs. 20 crores
 - All companies with outstanding loans/deposits > Rs. 50 crores
- Transition period three years. Provisions to apply retrospectively. Individuals/ Firms who are auditors for the last five/ten (as the case may be) consecutive years as on the date of appointment in September, 2014 can be re-appointed for a maximum period 3 years.
- Not applicable to OPC and small companies.

Audit & Auditors



- Members in AGM may decide to rotate audit signing partner/team
- Incoming auditor not eligible for appointment, if:
 - It has common partner in the outgoing audit firm
 - It is associated with outgoing auditor under same network, trade mark or brand.
- Branch Auditors
 - By the auditor of the company or by any CA (in case of a foreign branch, a person duly qualified to act as auditor), appointed by the company.
 - Branch auditor to submit report to the statutory auditor
 - All powers and responsibilities, similar to that of statutory auditor. Duty to report fraud under Section 143(12) extended to branch auditors

Audit & Auditors



- **Qualifications**
 - Should be a chartered accountant or a firm/LLP, whereof majority of the partners are chartered accountants practising in India. In case of LLP, only chartered accountants eligible to act and sign as auditor(s).
- **Disqualifications:**
 - A body corporate other than a LLP
 - An officer or an employee of a company
 - A person who or his partner/relative
 - ✦ Holds securities or interest in the company/subsidiary/holding or its associate.[Limit of holding security of the company, by an auditor or his partner or his relative – Section 141(d)(i)]

Audit & Auditors



- Disqualifications (Contd.):
 - A person who or his partner/relative (Contd.)
 - ✦ Is indebted or has given guarantee for indebtedness of third person, to the company/subsidiary/holding or its associate. [Limit of indebtedness or guarantee to the company, by an auditor or his partner or his relative – fixed at Rs. 100,000. Section 141(d)(ii) and (iii)]
 - A person or the firm has business relationship with the company/subsidiary/holding or its/their associate.
 - ✦ Business relationship defined as any transaction entered into for commercial purpose except:
 - Commercial transactions which are in the nature of professional services permitted under the Act and Rules.
 - Commercial transactions which are in the ordinary course of business at arm's length price.

Audit & Auditors



- Disqualifications (Contd.):
 - A person whose relative is a director or is in the employment of the company as a director or Key Mgmt. Personnel.
 - A person or the firm, as the case may be, has audits of more than twenty companies on the date of such appointment.
 - A person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed since such conviction.
 - Any person, whose subsidiary or associate or any other form of entity is engaged in specified consulting and specialised services

Audit & Auditors



- **Remuneration**
 - First Auditors – By the Board/Shareholders
 - Subsequent Auditors – Shareholders
 - Remuneration to include out-of-pocket expenses incurred in connection with the audit and any facility extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company.
- **Powers**
 - Shall have access at all times to the books of accounts and vouchers
 - Shall be entitled to require such information and explanation as he may consider necessary for the performance of his duties.

Audit & Auditors



- Report u/s 143(1) [corresponding to Section 227(1A)]
 - Secured Loans and advances have been properly secured and whether the terms are prejudicial to the interest of the company.
 - Transactions represented by mere book entries are prejudicial to the interest of the company.
 - In case of non-investment and non-banking company, whether the securities have been sold at a price below its purchase price
 - Whether loans and advances made are shown as deposits
 - Whether personal expenses have been debited to revenue a/c.
 - Whether cash has been actually received in case of allotment for cash or where the cash is not so received, whether position is correctly shown in the balance sheet and is not misleading

Audit & Auditors



- Report u/s 143(2) [corresponding to Section 227(2)]
 - Report on the accounts examined by him and every financial statement laid before the general body meeting
 - Shall take into account the provisions under the Act, accounting and auditing standards and matters required to be reported on under the Act or on the order of NFRA
 - To the best of his information and knowledge, the said accounts and the financial statements give a true and fair view of:
 - ✦ The state of affairs of the company as at the end of the financial year
 - ✦ Profit or loss during the financial year
 - ✦ Cash flow for the year
 - Any other matter as may prescribed.

Audit & Auditors



- Report u/s 143(3) [corresponding to Section 227(3)]
 - Sought and obtained all necessary information and explanations. If not, details thereof.
 - Proper books have been kept as required by law.
 - Report on the accounts of the branch(es) received and the manner in which he has dealt with the same.
 - Whether Balance sheet and statement of profit and loss is in agreement with the books of accounts and return
 - Whether the financial statements comply with the accounting standards
 - Observations/comments of transactions/matters having adverse effect on the functioning of the company
 - Whether any director is disqualified.
 - Any qualification, reservation or adverse remark relating to maintenance of accounts
 - The company has adequate internal financial control system and its operating effectiveness.

Audit & Auditors



- Additional reporting requirement as per Rules:
 - Whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement.
 - Whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts.
 - Whether there has been a delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

Audit & Auditors



- Where any matter to be reported by the auditor is answered in the negative, or with a qualification, state the reasons therefor.
- Every auditor shall comply with the auditing standards prescribed by the Central Government as recommended by the ICAI and after consultation with NFRA. In case such standards are not notified by CG, standards issued by ICAI shall be complied with.
- CG in consultation with NFRA, may direct the auditor to report on such matters as may be specified in that Order (corresponding to CARO)

Audit & Auditors



- Audits of Government Companies
 - CAG to appoint and direct the manner in which audit to be conducted and reported upon.
 - CAG can conduct supplementary audit within 60 days from the receipt of the audit report. Alternatively comment thereupon.
 - CAG comments to be circulated among the members
 - CAG can conduct test audit of any Government company.

Audit & Auditors



- **Duty to report Fraud**

- In the course of his duties, if the auditor has reasons to believe that an offence involving fraud is being or has been committed against the company by its officers/employees, he shall immediately report within the prescribed time.
- The auditor shall not have contravened any provisions relating to his duties, merely because he has reported the fraud in good faith.
- The above provisions are applicable to the cost accountants as well as company secretaries mutatis mutandis to the cost audit/secretarial audit conducted by them.
- Penalty ranging from Rs. 1 lakh to Rs. 25 lakh

Audit & Auditors



- Prohibition of certain services to be rendered by an auditor, whether directly or indirectly, to the company, or its holding/subsidiary company:
 - Accounting and book-keeping services
 - Internal Audit
 - Design and implementation of any financial information system
 - Actuarial services
 - Investment advisory services
 - Investment banking services
 - Rendering of outsourced financial services
 - Management services
 - Other services as may be prescribed.

Audit & Auditors



- Directly or indirectly means:
 - Either himself, or through his relative, or any person connected or associated with him or through any other entity, whatsoever, in which he has significant influence or control or whose name or trade mark or brand is used by such individual.
 - Either the firm itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity in which the firm or any partner of the firm has significant influence or control or whose name or trade mark or brand is used by such firm

Audit & Auditors



- The Auditor's report and other documents
 - Shall be signed by the auditor
 - Shall be kept open for inspection
 - The qualifications, observations or comments which have any adverse effect shall be read at the general meeting.
- All notices of and other communications relating to general meeting shall be forwarded to the auditor
- The auditor, shall, himself or through his authorised representative who shall also be qualified to be a auditor, any general meeting shall have the right to be heard on matters concerning him

Audit & Auditors



- Penalties on auditor for non-compliance [Section 147]
 - Non-compliance of Sections 139, 143, 144 or 145 – fine ranging from Rs.25,000 to Rs.100,000. [section 147(2)]
 - Where the contravention has been done knowingly or willingly with the intention to deceive – punishable with imprisonment upto one year and fine ranging from Rs.100,000 to Rs.25,00,000. Besides the auditor shall be liable to refund the remuneration received by him and pay for damages to the company, statutory bodies or authorities or any other person for loss arising out of incorrect or misleading statements in his report [section 147(3)]
 - Where it is proved that the auditor has acted in a fraudulent manner or abetted or colluded in any fraud, the partner as well as the firm shall be liable, jointly and severally. [section 147(5)], Criminal liability to devolve on concerned partner only.

Audit & Auditors



- Casual Vacancy
 - In case of government companies:
 - ✦ to be filled by CAG within 30 days .
 - ✦ If not , The Board shall fill the vacancy within 30 days thereafter.
 - In case of other companies
 - ✦ In case of vacancy caused due to reasons other than resignation by the auditor: To be filled by the Board within 30 days
 - ✦ In case of vacancy caused by resignation of the auditor: To be filled by the Board and thereafter confirmed by the members at an EGM convened within 3 months

Audit & Auditors



- Removal of Auditors by the company
 - Application to be made to Central Government within 30 days in Form No. ADT 2.
 - EGM to be held for removal within 60 days of the approval from CG. Removal valid on passing of the special resolution at the EGM
- Removal by Tribunal
 - Either suo muto or on an application by the CG, direct the company to change the auditor or CG can appoint a new auditor, if the existing auditor had acted in a fraudulent manner. Application to be disposed of within 15 days.
 - Removed auditor not eligible for re-appointment for 5 years

Audit & Auditors



- **Branch auditors**
 - Duties and Powers same as company's statutory auditors as specified in Section 143 (1) to (4)
 - Duty to report fraud under Section 143(12) extended to branch auditors
 - Branch audit or to report to company's auditor
- **Procedure for reporting of fraud to Central Government**
 - Forward report to Board/Audit Committee seeking their reply/observations within 45 days.
 - Send the report alongwith the reply received from the Board/Audit Committee to the Central Government within 15 days thereof.
 - In case no reply is received from the Board/Audit Committee, send his report alongwith a note containing the details of his report to the Board/Audit Committee, to the Central Government.
 - Report should be sent in Form No. ADT 4.

Audit & Auditors



- Cost Audit
- Power of Central Govt. to prescribe maintenance of cost records by certain class of companies.
- Power of Central Govt. to require the cost records to be audited by a cost accountant not being a statutory auditor.
- Cost Audit shall be in accordance with cost auditing standards issued by ICWAI.
- Submission of cost audit report
- Power of Central Govt. to call for additional information.
- Penalty for non-compliance as per Section 147

Internal Auditor



- Following companies to appoint internal auditor :
 - Listed companies
 - Public company having
 - paid up capital of 10 crores or more
 - Turnover of Rs 200 crores or more
 - Outstanding loans & borrowings of 25 crores or more or
 - Accepted Deposits are 25 crores or more
 - Private company whose :
 - Turnover of Rs 200 crores or more
 - Outstanding loans & borrowings of 25 crores or more
- in previous financial year
- He may be an employee /external professional
- Formulation of scope, functioning, periodicity and methodology

Summary Of Types of Audit



	Statutory	Internal	Secretarial	Cost
Relevant sections	139-147	138	204	147
Applicability	All companies	Listed and public Cos having capital > 10 crores or loans > 25 crores	Listed Cos and Public Cos with capital > 100 crores	To be notified
Who can conduct	CA / CA firm /LLP	Employee or external [CA / Cost Actt.]	CS in Practice	Cost Actt. in practice
Scope of Audit	Financial Statements	Functions and activities	Secretarial and related records	Cost records
Standards applicable	NFRA notified	ICAI (optional)	ICSI Standards	ICWAI
Frequency	Annual	Board to decide	Annual	Annual
Report to be given to	Members	Board	Members	Board

Impact on Auditors



Regulatory Authorities



- National Financial Reporting Authority/Appellate Authority [Section 132]
- Serious Fraud Investigation Office [Section 211]
- National Company Law Tribunal/Appellate Tribunal – Chapter XXVII [Sections 407 to 434]
- Special Courts/ Mediation and Conciliation Panels – Chapter XXVIII [Sections 435 to 446]
- -----
- Class Action Suits [Section 37 and Section 245]

National Financial Reporting Authority



- NFRA constituted u/s 132 of the Act, to provide for matters relating to accounting and auditing standards . A quasi judicial body.
- Functions
 - To recommend the Accounting and Auditing Standards
 - To monitor and enforce the compliance of the above standards
 - To oversee the quality of service of the profession associated thereto and to suggest measures required for improvement in the quality of professionals
 - To perform such other prescribed functions

National Financial Reporting Authority



- Structure of NFRA
 - Accounting Standards Committee
 - Auditing Standards Committee
 - Enforcement Committee

National Financial Reporting Authority



- Who can complain

Central Government	Authorised by an officer not below the rank of Jt. Secy and signed by an officer not below the rank of Under Secretary
RBI or SEBI any other Regulator	-- same as above --
Bank	Complaint shall be accompanied by a resolution authorising the officer
Company or firm	-- same as above --
Any other person	

- Every complaint to be acknowledged by ordinary post
- Complaint should accompany requisite fees.

Serious Fraud Investigation Office



- Failure of non-banking financial institutions, vanishing companies and stock market scam prompted the establishment of SFIO by CG
- Set up in 2003 under the Companies Act, 1956
- SFIO has experts from the fields of – Finance, Company Law, Capital Markets, Law, Information Technology, Forensic Auditing, Taxation and Investigation (generally from IAS,IPS and IRS cadre.
- Headed by Director – SFIO
- Existing SFIO will function till the new SFIO under Companies Act, 2013 is constituted

Serious Fraud Investigation Office



- Limitations of SFIO under the old Act:
 - Powers largely restricted to examination of documents
 - No powers of arrest
 - Search and Seizure powers subject to permission
 - Operates in a matrix of investigating bodies with overlapping authority
 - Inadequate/shortage of manpower
- Recommendations of Vepa Kamesan Committee
 - Suggested statutory recognition
 - Use of technology and skilled manpower
- New SFIO under the new Act without the limitations

Serious Fraud Investigation Office



- Responsibilities

- Detecting and prosecuting or recommending for prosecution white-collar crimes/ corporate frauds.
- Investigations characterised by
 - ✦ Complexity and having inter-departmental and multi-disciplinary ramifications
 - ✦ Substantial involvement of public interest – either in terms of size of monetary misappropriation or persons affected.
 - ✦ Investigations leading to or contributing towards a clear improvement in systems
 - ✦ Serious Fraud cases referred to be the Department of Corporate Affairs.

Serious Fraud Investigation Office



- CG may by order assign investigation into the affairs of a company –
 - On receipt of a report of the Registrar or Inspector u/s 208
 - On intimation of the special resolution passed by the members
 - In the public interest
 - On request from any department of Central Government or State Government
- Exclusivity of investigation
- Powers of Investigation Officer = Powers of Inspector u/s 217

Serious Fraud Investigation Office



- The company, its officers and employees, whether present or past shall provide all information, explanations, documents and assistance.
- Notwithstanding anything contained in Criminal Procedure Code, the offences which attract the punishment for fraud provided in Section 447 of the Act, shall be cognisable and no person accused of any offence under those sections shall be released on bail or on his own bond except in certain circumstances.
- Investigation Report filed with the Special Court for framing charges shall be deemed to be a report filed by a police officer u/s 173 of the Cr.P.C.

Serious Fraud Investigation Office



- Where SFIO is investigating any offence, any other investigating agency, State Government, police authority or income tax authorities having information or documents in respect of such offence shall provide all such information or documents available with it to the SFIO.
- Similarly, SFIO shall share any information or documents with it, with any other investigating agency, State Government, police authority or income tax authorities

Fraud



- Fraud defined
- Fraud, in relation to affairs of a company or any body corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person or any other person with the connivance in any manner with intent to deceive to gain undue advantage from or to injure the interests of the company, or its shareholders or its creditors or any other person whether or not there is wrongful gain or wrongful loss.

Fraud



- Wrongful gain means the gain by unlawful means of property to which the person gaining is not legally entitled.
- Wrongful loss means the loss by unlawful means of property to which the person gaining is legally entitled
- Definition much wider than the definition contained in Indian Contract Act.

Fraud



- Section 447 states: Without prejudice to any liability including repayment of any debt under this Act or any other law for the time being in force, any person who is found to be guilty of fraud, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud:
- Provided that where the fraud in question involves public interest, the term of imprisonment shall not be less than three years.

Class Action Suits



- Concept is very common in developed nations such as USA, UK and Singapore. Recommended by J.J. Irani Committee Report in 2005.
- Statutory recognition given by the new Act.
- It is also known as Representative action
- It means a lawsuit (civil action) where
 - a person sues a group of people; or
 - a group of people sues another group of people; or
 - a group of persons sues a person
 - The group is so large that it becomes impracticable to bring them all before the court.
- The group has common rights and grievances.

Class Action Suits



- The origin can be traced to Satyam scam
 - Mr. Ramalingam Raju confessing to misstatements in accounts of the company.
 - 300,000 shareholders of Satyam Computer Services Ltd., sued the company and claimed damages worth Rs. 5,000 crores.
 - No law in India enabling such class action suits. Suits were filed before various courts/bodies such as National Consumer Disputes Redressal Cell to the Supreme Court, which rejected their claims
 - US investors who owned American Depository Receipts were able to claim US\$125 million (Rs. 700 crores approx.) from the company by mounting a class action suit under US laws.

Class Action Suits under the new Act



- Section 37 states : A suit may be filed or any other action may be taken under section 34 or section 35 or section 36 by any person, group of persons or any association of persons affected by any misleading statement or the inclusion or omission of any matter in the prospectus.
- Section 245(1) states : Such number of member or members, depositor or depositors or any class of them, as the case may be, may, if they are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members or depositors, file an application before the Tribunal on behalf of the members or depositors.

Class Action Suits under the new Act



- Section 244 read with Section 241 states:
- Specified number of members of a company shall have the right to apply to the Tribunal if :
 - (a) the affairs of the company have been or are being conducted in a manner prejudicial to public interest or in a manner prejudicial or oppressive to him or any other member or members or in a manner prejudicial to the interests of the company; or
 - (b) the material change, not being a change brought about by, or in the interests of, any creditors, including debenture holders or any class of shareholders of the company, has taken place in the management or control of the company, whether by an alteration in the Board of Directors, or manager, or in the ownership of the company's shares, or if it has no share capital, in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests or its members or any class of members,

Reliefs under Class Action Suits



- (a) to restrain the company from committing an act which is *ultra vires* the articles or memorandum of the company;
- (b) to restrain the company from committing breach of any provision of the company's memorandum or articles;
- (c) to declare a resolution altering the memorandum or articles of the company as void if the resolution was passed by suppression of material facts or obtained by mis-statement to the members or depositors;
- (d) to restrain the company and its directors from acting on such resolution;
- (e) to restrain the company from doing an act which is contrary to the provisions of this Act or any other law for the time being in force;

Reliefs under Class Action Suits (Contd.)



- (f) to restrain the company from taking action contrary to any resolution passed by the members;
- (g) to claim damages or compensation or demand any other suitable action from or against—
 - (i) the company or its directors for any fraudulent, unlawful or wrongful act or omission or conduct or any likely act or omission or conduct on its or their part;
 - (ii) the auditor including audit firm of the company for any improper or misleading statement of particulars made in his audit report or for any fraudulent, unlawful or wrongful act or conduct; or
 - (iii) any expert or advisor or consultant or any other person for any incorrect or misleading statement made to the company or for any fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on his part;
- (h) to seek any other remedy as the Tribunal may deem fit.

Class Action Suits



- Who can file:
 - In case of company having share capital:
 - ✦ Any 100 or more members
 - ✦ At least 10% of the number of members
 - ✦ members , singly or jointly holding, more than 10% of the issued capital, provided all calls thereon are paid.
 - In case of company not having share capital
 - ✦ Members equal to or exceeding $1/5^{\text{th}}$ of the total number of its members
 - In case of depositors
 - ✦ Any 100 or more depositors
 - ✦ At least 10% of the number of depositors
 - ✦ Depositors, singly or jointly holding, more than 10% of the outstanding deposits of the company.

Class Action Suits



- Who can be sued:
 - The Company
 - Its directors
 - The Auditor(s) of the company
 - any expert or advisor or consultant or any other person for any incorrect or misleading statement made to the company or for any fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on his part;

Class Action Suits



- Consequences on non-compliance of the order passed by the Tribunal:
 - A company shall be punishable with a fine which shall not be less than Rs. 500,000 but may extend upto Rs. 25,00,000.
 - Any officer of the company who is in default can be punished with
 - ✦ With imprisonment for a term upto 3 years and
 - ✦ Imposition of fine of not less than Rs. 25,000 which may extend upto Rs. 100,000.
- Any order passed by the Tribunal shall be binding on the company and all its members, depositors and auditor including audit firm or expert or consultant or advisor or any other person associated with the company.

Auditor's focus areas – compliances and responsibilities



- Changes in provisions are not only in letter but compliance in spirit of law is desired.
 - Disqualifications
 - Prohibited services
- More responsibilities are cast on Key Managerial Personnel, auditors and other professionals
 - Reporting requirements
 - Class Action suits
- Penalties have been increased manifold

*Thank
You..*



Why worry and have wrinkles

When you can smile and have Dimples..... 😊

Provisions relating to
Audit and Auditors – Rotation of Audit, Ceiling on Audits etc.,
Mandatory Internal Audit, Reporting on Frauds and Auditors responsibility,
Auditor's focus areas – compliances and responsibilities



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