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# **Seminar on Companies Act, 2013 – A Comparative Analysis & Issues**

21<sup>st</sup> June, 2014

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## ***Companies Act, 2013***

Audit & Auditors—Appointment,  
Auditor Rotation, Removal, Role and  
Responsibilities

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# ***Companies Act, 2013 (2013 Act): Overview***

Status as on June 2014

## **Sections notified**

1 section w.e.f 30.08.2013  
99 sections w.e.f 12.09.2013  
183 sections w.e.f 01.04.2014

187 yet to notified

## **Circulars Issued & Rules notified**

15 Circulars / Notifications issued with respect to clarifications of notified sections

20 rules are notified

## **Orders Issued**

Companies (Removal of Difficulties) Order, 2013  
Companies 1<sup>st</sup> (Removal of Difficulties) Order, 2014  
Companies 2<sup>nd</sup> (Removal of Difficulties) Order, 2014

# Overview

## Status as on June 2014

- Currently, Companies Act, 1956 (1956 Act) and 2013 Act to **co-exist**
- Harmonization with other laws / regulations required

<i>Companies Act, 2013: A Statistical Snapshot</i>	
Number of Schedules	7
Number of Chapters	29
<i>Number of times the phrase 'as may be prescribed' is used</i>	340+
Number of Clauses	470

## ***Overview***

### A delegated law: Powers vested with MCA

<b>Power to make rules (S.469)*</b>	Approval by both Houses of Parliament required <i>after</i> notification
<b>Power to amend schedules (S.467)*</b>	Approval by both Houses of Parliament required <i>after</i> notification
<b>Power to exempt class or classes of companies from provisions of this Act (S.462)*</b>	Complete / partial exemption to class / classes of companies Proposed notification to be approved by both Houses of Parliament
<b>Power to remove difficulties (S.470)*</b>	<ul style="list-style-type: none"><li>• Provisions necessary or expedient to remove difficulties</li><li>• 5 years from the commencement of section 1 of the 2013 Act</li></ul>

*\* Notified*

# ***Audit and Auditors***

## **Appointment**

- First appointment by Board
- If Board fails to appoint, appointment by EGM
- Once appointed, appointment valid for 5 years (subject to ratification at each AGM)
- Casual vacancy is to be filled by Board
- Vacancy due to resignation of auditor is to be filled by Shareholders

## ***Audit and Auditors***

### **Appointment**

- If at an AGM, no auditor is appointed, the existing auditor will continue
- Disqualification: extended to relatives also
- Maximum number of audits: Restricted to 20 companies (no exemption for private limited companies)
- Company to notify ROC within 15 days

# ***Audit and Auditors***

## **Appointment**

- Audit committee / Board to consider:
  - Qualification and experience of the auditor
  - Any order or pending proceeding relating to professional matters of conduct against the proposed auditor before the Institute of Chartered Accountants of India or any competent authority or any Court
- CAG to appoint auditor of Govt. Co. within 180 days of financial year



# ***Audit and Auditors***

## Rotation

- Mandated at 5 years for individual / 10 years for audit firm, for listed companies and other specified companies except OPC and small companies:
  - a) All unlisted public companies having paid up share capital of Rs. 10 crores or more.
  - b) All private companies having paid up share capital of Rs. 20 crores or more.
  - c) All Companies not covered by (a) and (b) above, but having borrowings from financial institutions, banks or public deposits of Rs. 50 crores or more.

## ***Audit and Auditors***

### **Rotation**

- Applicable retrospectively
- Cooling off period: 5 years; transition period: 3 years
- Existing auditors can continue to audit till March 31, 2017 accounts, if reappointed by the members
- Members of a company may rotate audit partner and staff / require joint audit

## ***Audit and Auditors***

### Rotation

- Firms with common partners in the outgoing audit firm will also be ineligible during the cooling off period.
- New auditor not to be from the same network / brand / trademark
- In case of joint auditors, rotation to be followed in a manner that both or all joint auditors do not complete their term in the same year

## Removal and Resignation

- Special Resolution and prior approval of Central Government required for removal
- Auditor must be given reasonable opportunity of being heard
- File statement in prescribed form within 30 days from date of resignation with the company and the ROC.

# Removal and Resignation

- For Govt Co, statement also to be filed with the CAG
- Tribunal suo motu or on application by Central Govt or by any person, direct company to change auditor, if auditor found involved in fraud. Central Government can appoint auditor.

## Qualifications of an auditor

- Only a Chartered Accountant can be appointed as an auditor
- In case of a firm, majority of partners should be Chartered Accountants
- In case of a firm, only Chartered Accountants can sign on behalf of the firm

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## ***Audit and Auditors***

### Disqualifications of an auditor

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Body corporate other than LLP

An officer / employee of the company

Person who is a partner, or who is in the employment , of an officer /employee of the company

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A person or firm who has business relationship (directly / indirectly) with the company, or its subsidiary or its holding or associate company, or subsidiary or associate company of the holding company.

Exceptions: Professional services permitted to be rendered by an auditor

Commercial transactions in the ordinary course of business at arms' length e.g. hotels, airlines, hospitals, telecommunications etc.

# ***Audit and Auditors***

## **Disqualifications of an auditor**

A person who, or his relative or partner is holding securities or interest in,  
(Except a relative of a partner who is holding security or interest of [face value < Rs.1 lakh])

A person, who or his relative or partner are indebted to  
[> Rs.5 lakh]

A person, who or his relative or partner has given guarantee / provided security in connection with indebtedness of any third party to [>Rs.1lakh]

**Company/its  
subsidiary /  
its holding  
or associate  
or  
subsidiary of  
such holding  
company**



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## ***Audit and Auditors***

### Disqualifications of an auditor

- A person whose relative is a director or is a key managerial personnel
- A person in full time employment elsewhere / person or partner who is holding audit of more than 20 companies
- Person convicted for fraud & 10 years have not elapsed
- Any person whose subsidiary or associate or other entity is engaged in consulting & specialised services

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## ***Audit and Auditors***

### Prohibited Services

- Specifically prohibited services, provided to either the Company / holding company / subsidiary company, whether directly or indirectly:
  - Accounting and book keeping services
  - Internal audit
  - Design and implementation of any financial information system
  - Actuarial services

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## ***Audit and Auditors***

### Prohibited Services

- Investment advisory services
- Investment banking services
- Rendering of outsourced financial services
- Management services and
- Any other kind of services as may be prescribed
- Any other service rendered by the statutory auditor, would have to be approved by the board of directors or audit committee.

## ***Auditor: Regulator and Role***

### **Multiple Regulators**

- ICAI
- Tribunal – has power to change / debar auditor / audit firm
- New regulator – NFRA (replaces NACAAS) with substantial power - not just standard setter – but also enforcer and monitoring agency and regulator

## ***Auditor: Regulator and Role***

### **Auditor as Whistle Blower**

- Auditor to report to the Central Government: if any reason to believe “offence involving fraud is being committed or has been committed against the company by its officers or employees”
- Audit Committee / Board required to respond to Auditor
- Auditor is protected if reporting is done in good faith

# ***Audit and Auditors***

## Auditors responsibility and liability

### Additional matters to be reported in the Auditors Report

- Adequate *internal financial controls system* and operating effectiveness of such controls \*\*
- observations or comments on ‘financial transactions’ or matters having *adverse effect* on the functioning of the company
- any qualification, reservation or adverse remark relating to maintenance of accounts

\*\* Directors required to comment only in case of listed companies, but auditors required to comment in all cases!

## ***Audit and Auditors***

### Auditors responsibility and liability

#### Additional matters to be reported in the Auditors Report

- Whether the company has disclosed the effect, if any, of *pending litigations* on its financial position in its financial statements
- Whether the company has made provision for *foreseeable losses*, if any, on long term contracts including derivative contracts
- Whether there has been *delay in depositing* money into the Investor Education and Protection Fund by the company

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## ***Audit and Auditors***

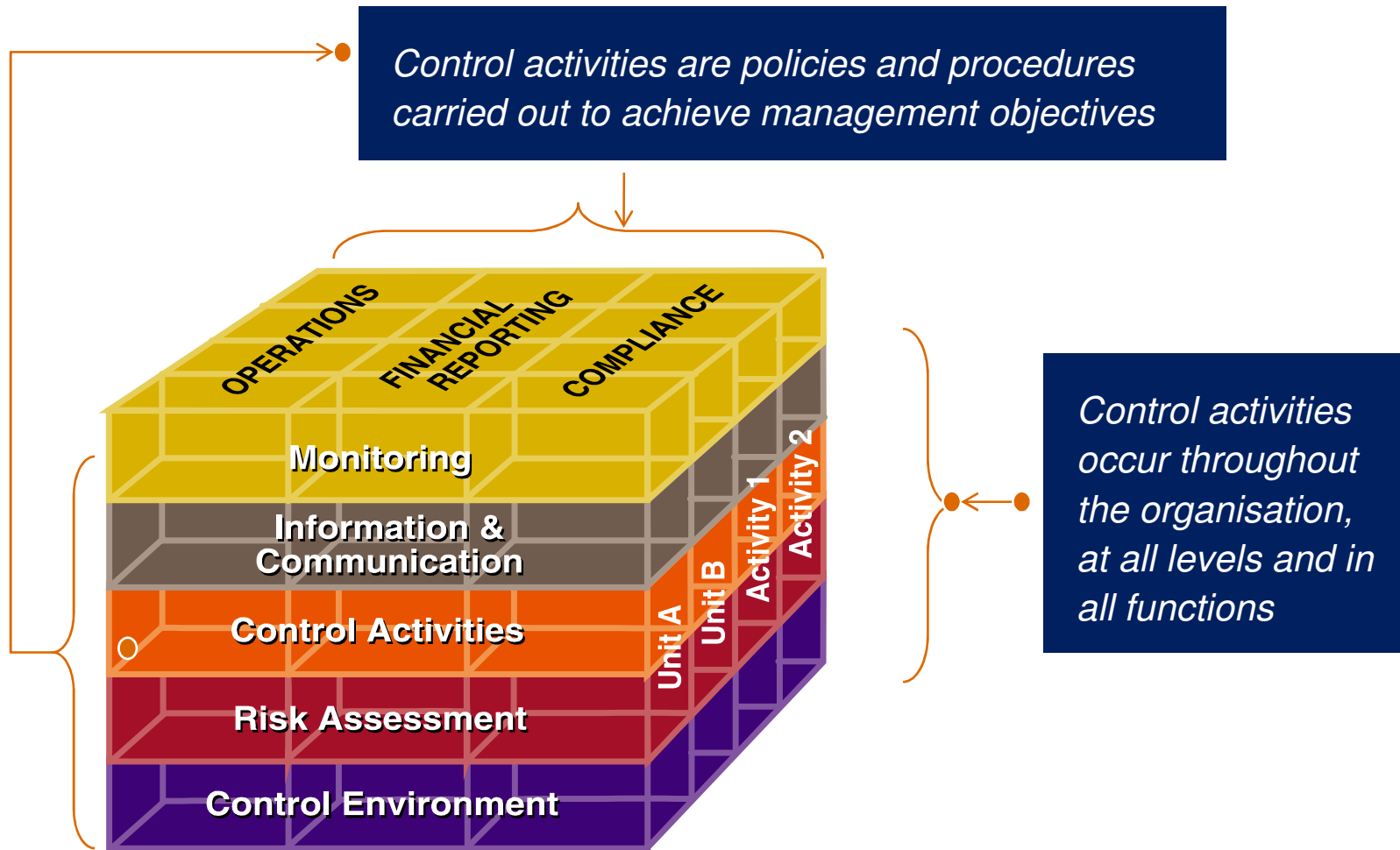
### Internal Financial Control System

**Internal financial controls** means the policies and procedures adopted by the company for ensuring the orderly and efficient conduct of its business, including adherence to company's policies, the safeguarding of its assets, the prevention and detection of frauds and errors, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information.



# ***Audit and Auditors***

## **Internal Financial Control System**



# Audit and Auditors

## Internal Financial Control System

Examples of Entity-Level Controls														
<u>Internal Control Components</u>	Assignment of Authority and Responsibility	Enterprise Risk Management	Audit Committee	Internal Audit	Whistleblower	Code of Conduct	IT Environment & Organisation	Self Assessment	Shared Services	Disclosure Committee	Oversight by the Board, and Senior Management	Policies and Procedures Manual	Period End Reporting	Business Performance Reviews
Control Environment	X		X		X	X	X				X	X		
Risk Assessment	X	X	X	X	X			X		X	X			
Information & Communication	X	X	X	X	X	X	X		X	X	X	X	X	
Monitoring of Controls			X	X	X			X		X	X	X		
Control Activities									X				X	X

## ***Other Significant Provisions - Fraud***

Fraud' in relation to affairs of a company or any body corporate, includes any act, omission, concealment of any fact, 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, shareholders, creditors, any other person, whether or not there is any wrongful gain or wrongful loss

## *Other Significant Provisions*

### Penal Consequences

**Fine** for not reporting fraud will range from **Rs 1 lac to Rs 25 lacs.**

Contravention of **Sections 139, 143, 144 or 145** punishable with fine from **Rs 25 thousand to Rs 5 lacs.**

*Imprisonment* upto 1 year and fine if willful contravention done to deceive the company, shareholders, creditors or tax authorities

Fine upto **Rs 25 lacs** for wilful contravention of statutory provisions

# ***Audit and Auditors***

## Auditors responsibility and liability

### Penalties

- Refund the remuneration to the company
- Pay for damages to the company, statutory bodies or authorities or to any other persons for loss arising out of incorrect or misleading statements of particulars made in his audit report
- In case of criminal liability of any audit firm, the liability other than fine, shall devolve only on the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud.

# ***Audit and Auditors***

## Auditors responsibility and liability

### Penalties

- NFRA can debar a member / firm from 6 months to 10 years, impose penalties not less than Rs 1 lac / Rs.10 lacs extending to 5/10 times the fees received in case of a member / firm
- Tribunal also has powers to *debar* a firm from being appointed as an auditor for any company for 5 years
- Auditor can also be prosecuted for *fraud* u/s 447 and subjected to *class action suits*\*

\* Yet to be notified

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# ***Audit and Auditors***

## **Internal Audit**

- Mandated for:
  - every listed company
  - every unlisted public company having paid up share capital > Rs 50 cr/turnover >Rs.200 cr/outstanding loans or borrowings from banks or public financial institutions > Rs.100cr/outstanding deposits >Rs.25cr.
  - every private company which having turnover >Rs.200cr/ outstanding loans or borrowings from banks or public financial institutions > Rs. 100 cr.
- Internal Audit can be done by:
  - Chartered accountant, cost accountant or such other professional.
  - Per Rules: Individual or firm of internal auditors

# ***Audit and Auditors***

## **Secretarial Audit and Cost Audit**

	<b>Secretarial Audit</b>	<b>Cost Audit</b>
Applicable to	All listed companies & every public company with paid-up share capital > Rs. 50 cr/turnover > 250cr	Companies engaged in production of specified goods / providing specified services
Who can be appointed as the auditor	Company Secretary in Practice	Cost Accountant in Practice
Board Response	Explain in full any qualification or observation or other remarks in Board's report	Company to furnish report of auditor along with full information and explanation on every reservation or qualification to CG
<i>Liabilities</i>	<i>Provisions of NFRA which apply to statutory auditor to apply in both cases</i>	



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***Questions?***

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***Thank You***