

# Chapter 10: Audit and Auditors

## Introduction

Large business corporations are managed by the directors who represent the members who are the real owners of the company through board. In the absence of any check, the directors may mismanage the finances of the organization. Thus, members appoint auditor/auditors to look into the true and fair view of the financial affairs of the company. Large business corporations are managed by the directors, who act as fiduciaries (a person who prudently takes care of finances or other assets for another person) to the members (the real owners). This is the reason that the board of directors is responsible for the preparation of the financial statement and laying it out at the general meeting of members.

Despite assuming a fiduciary role, in the absence of proper checks and balances, the directors may indulge in mismanagement of the finances and other assets of the corporation. Hence, financial statements prepared and laid down by the board need to be audited by an independent auditor.

Thus, members appoint auditors to have an independent professional opinion on the financial affairs of the company, who examine such financial statements to frame opinions to report; whether they reflect a true and fair view of financial position and performance or not.

## Appointment' Of Auditors [Section 139]

**Appointment of Auditor [Sub-Section 1 Read with rule 3 and 4 of the companies (audit and auditors) rules, 2014]**

**Who can be appointed as Auditor and when?**

Every company shall appoint an individual or a firm ("firm" shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008) **as an auditor of the company at the first Annual General Meeting (AGM).**

**Tenor of appointment as Auditor**

The **auditor shall hold office from the conclusion of 1 AGM** (or the AGM in which he is appointed) till the conclusion of its 6<sup>th</sup> AGM (and thereafter till the conclusion of every sixth AGM).

**Example:** Rashail Tech Labs Private Limited was incorporated during the financial year 2019-20. First AGM of the company was held on 30.09.2020. The company appointed M/s. Rams & Associates, Chartered Accountant firm for the period of 5 Years as a subsequent statutory auditor.



### Manner and procedure of selection and appointment of auditors (Rule 3 of the Companies (Audit and Auditors) Rules, 2014]

The manner and procedure of selection of auditors by the members of the company at AGM has been prescribed under the **Rule 3 of the Companies (Audit and Auditors) Rules, 2014**: tabled and stated below.

Categories of Companies	Competent authority	Responsibility of the competent authority
A company Which is Required to Constitute an Audit Committee Under <b>section 177</b>	Audit Committee	The competent authority shall take into consideration the qualifications and experience of the individual or the firm proposed to be considered for appointment as auditor and such qualifications and experience are commensurate with the size and requirements of the company.
A Company which is not required to constitute an Audit Committee Under <b>section 177</b>	Board of Directors	It shall have regard to any order or pending proceeding relating to professional matters of conduct against the proposed auditor before the Institute of Chartered Accountants of India (ICAI) or any competent authority or any Court. It may call for such other information from the proposed auditor as it may deem fit.

**\*Where competent authority is the audit committee**, the committee shall recommend the name of an individual or a firm as auditor to the Board for consideration; the Board shall consider and recommend an individual or a firm as auditor to the members in the AGM for appointment.

If the Board agrees with the recommendation of the Audit Committee It shall further recommend the appointment of an individual or a firm as auditor to the members in the annual general meeting. If the Board disagrees with the recommendation of the Audit Committee - It shall refer back the recommendation to the committee for reconsideration citing reasons for such disagreement.

**Example:** Audit Committee recommended KPM & Associates, Chartered Accountants firm for appointment as statutory auditor to the board of Surya Solar Limited. However, the board of the company disagreed with the recommendation of the audit committee. In such conditions, the board shall refer back the recommendation to the committee for reconsideration citing reasons for such disagreement.

If the Audit Committee, after considering the reasons given by the Board, decides not to reconsider its original recommendation, the Board shall record reasons for its disagreement with the committee and send its own



recommendation for consideration of the members in the AGM; and if the Board agrees with the recommendations of the Audit Committee, it shall place the matter for consideration by members in the AGM.

### **Author's Note:**

#### **Companies that require to constitute an audit committee**

**Section 177(2)** of the Act, read with Companies (Meetings of Board and its Powers) Rules, 2014 provides Audit Committee shall be constituted by Board of directors in case of;

- i. Every listed public company and
- ii. Those public companies which having:
  - a. Paid up capital of ten crore rupees or more; or
  - b. Turnover of one hundred crore rupees or more; or
  - c. Aggregate, outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more.

The paid-up share capital or turnover or outstanding loans, or borrowings or debentures or deposits, as the case may be, as existing on the date of last audited financial statements shall be taken into account for the purposes of this rule.

It is also worth noting that where a company ceases to fulfil any of three conditions laid down above for three consecutive years, it shall not be required to comply with the provisions pertaining to the audit committee until such time as it meets any of such conditions.

#### **Consent of auditors (proposed/selected auditor) for appointment, certificate from such auditor and notice to Registrar [Sub-section 1 read with rule 4 of the Companies (Audit and Auditors) Rules, 2014]**

##### **Written consent**

Before the appointment is made, the **written consent of the auditor** to such appointment shall be obtained.

##### **Certificate**

A certificate shall be also obtained from the auditor stating that,

- a. The individual or the firm (as the case may be to be, appointed as auditor) is **eligible for appointment and is not disqualified** for appointment under the Act, the Chartered Accountants Act, 1949 and the rules or regulations made thereunder,
- b. The proposed appointment is as per the term provided under the Act;
- c. The proposed appointment is within the limits laid down by or under the authority of the Act;



d. The list of proceedings against the auditor or audit firm or any partner of the audit firm pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.

**Author's Note:** The certificate shall also indicate whether the auditor satisfies the criteria provided in **section 141** [i.e., eligibility, qualification and disqualification of Auditor which will be discussed later] of this Act

### Notice to Registrar

The company shall inform the concerned auditor of his or its appointment, and **also file a notice in the Form ADT-1** of such appointment with the **Registrar within 15 days** of the meeting in which the auditor is appointed.

### Students are advised to take note:

#### **Intimation to NFRA under the National Financial Reporting Authority Rules, 2018 (here-in-after referred as to NFRA Rules)**

As per Rule 3 (2) of NFRA Rules, every existing body corporate other than a company governed by NFRA rules, shall inform the National Financial Reporting Authority (NFRA) **within 30 days of the commencement of the NFRA rules**, in **Form NFRA-1**, the particulars of the auditor as on the date of commencement of the NFRA rules.

According to Rule 3(3) of NFRA Rules, every body corporate, other than a company as defined in clause (20) of **section 2** of the Act, formed in India and governed under NFRA Rules shall, within 15 days of appointment of an auditor under **sub-section (1) of section 139**, inform the NFRA in **Form NFRA-1**, the particulars of the auditor appointed by such body corporate, provided that a body corporate governed under clause (e) of sub-rule (1) of NFRA Rules shall provide details of appointment of its auditor in **Form NFRA-1**.

### **TERM OF AUDITOR [Sub-Section 2 Read with Rule 5 of Companies (Audit & Auditors) rules, 2014]**

#### **Maximum terms and length thereof in case of individual and firm**

**Section 139(2)** provides that:

- i. Listed companies and
- ii. All companies (excluding one person companies & small companies), which are
  - a. Unlisted public companies and having paid up share capital of rupees ten crore or more;
  - b. Private limited companies and having paid up share capital of rupees fifty crore or more;



c. Having public borrowings from financial institutions, banks or public deposits of rupees fifty crore or more.

#### Shall not appoint or re-appoint

- i. An **individual** as auditor for **more than one term of five consecutive years**;
- ii. An **audit firm** as auditor for **more than two terms of five consecutive years**.

#### Students are advice to take note;

Nothing contained in **sub-section 2**, shall prejudice the right of the

- a. Company to remove an auditor or
- b. Auditor to resign from such office of the company.

**Example:** XYZ Ltd. which is a listed company appoints individual Mr. Raghav as an auditor in its AGM dated 29th September, 2022. Mr. Raghav will hold office of Auditor from the conclusion of this meeting up to conclusion of sixth AGM i.e., AGM to be held in the year 2027. Now as per **sub-section (2)**, Mr. Raghav shall not be re-appointed as Auditor in XYZ Ltd at 6th AGM (ie. 2027).

**Example:** XYZ Ltd. which is a listed company appoints M/s Raghav & Associates as an audit firm in its AGM dated 29th September, 2016. M/s Raghav & Associates will hold office from the conclusion of this meeting up to conclusion of the sixth AGM to be held in the year 2021. Now as per **sub-section (2)**, M/s Raghav & Associates can be appointed or re-appointed as auditor for one more term of five years i.e., up to year 2026. It shall not be re-appointed as Audit firm in XYZ Ltd at 11th AGM (i.e., 2026).

#### **Cooling Period (to ensure reinstatement of independence)**

An individual auditor who has completed his term (**ie. one term of five consecutive years**) shall **not be eligible for re-appointment as auditor** in the same company for five years from the completion of his term;

An audit firm which has completed its terms (**ie. two terms of five consecutive years**) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of second term.

#### Summary

Auditor	Appointed/Reappointed for	Not eligible for re-appointment
Individual	One term of five consecutive years (1 AGM to 6 AGM)	For five years from the completion of his term (till 11 AGM)
Firm	Two terms of five consecutive years (1 AGM to 11th AGM)	For five years from the completion of its second term (till 16" AGM)

**Example:** XYZ Ltd. which is a listed company appoints individual Mr. Raghav as an auditor in its AGM dated 29th September, 2016. Mr. Raghav will hold office of



Auditor from the conclusion of this meeting up to conclusion of sixth AGM i.e., AGM to be held in the year 2021. Now as per **sub-section (2)**, Mr. Raghav shall not be re-appointed as Auditor in XYZ Ltd. for further term of five years i.e., he cannot be appointed as Auditor in XYZ Ltd. up to year 2026.

**Example:** XYZ Ltd. which is a listed company appoints M/s Raghav & Associates as an audit firm in its AGM dated 29th September, 2016. M/s Raghav & Associates will hold office from the conclusion of this meeting up to conclusion of the sixth AGM to be held in the year 2021. Now as per **sub-section (2)**, M/s Raghav & Associates can be appointed or re-appointed as auditor for one more term of five years i.e., up to year 2026. It shall not be re-appointed as Audit firm in XYZ Ltd. for a further term of five years from 2026 to year 2031.

**Author's Note:** On the date of appointment, an audit firm shall not have any partner or partners who are/were also the partner/s to the other audit firm, whose tenure has expired in a company immediately preceding the financial year. It means, the audit firm with common partners shall not be appointed as succeeding auditor of the same company after two terms of five consecutive years.

**Example:** M/s Krishna & Associates is an audit firm having 2 partners namely Mr. Krishna and Mr. Shyam. Mr. Shyam is also a partner of another audit firm named M/s Kukreja & Associates. M/s Krishna & Associates was appointed as the auditors in the company Golden Smith Ltd. for two consecutive periods of 5 years i.e., from year 2016 to year 2026. Now, if Golden Smith Ltd. wants to appoint M/s Kukreja & Associates as its audit firm, it cannot do so because Mr. Shyam is the common partner between both the Audit firms. This prohibition is only for 5 years i.e., up to year 2031. After a cooling period of 5 years, Golden Smith Ltd. may appoint M/s Kukreja & Associates or M/s. Krishna & Associates as its auditors.

## Transitional period

Every company, existing on or before the commencement of this Act which is required to comply with the provisions as mentioned in above mentioned points (a) to (d) (i.e., provisions of this **subsection**), shall comply with those provisions within a period which shall not be later than the date of the first AGM of the company held, within the period specified under **sub-section (1)** of **section 96**, after three years from the date of commencement of this Act.

## ROTATION OF AUDITOR [Sub-Section 3 and 4 Read with Rule 6 of Companies (Audit & Auditors) Rules, 2014]

### Power to Members [Sub-Section 3]



Members of a company may resolve to provide that:

- a. In the audit firm appointed by them, the auditing partner and his team shall be rotated at such intervals as may be resolved by members; or
- b. The audit shall be conducted by more than one auditor.

### **Manner of Rotation of Auditors by the Companies on Expiry of Their Term [Sub-Section 4 Read with Rule 6 (2) and (3)]**

The Central Government may, by rules, prescribe the manner in which the companies shall **rotate their auditors**. The manner of rotation of auditors by the companies on expiry of their term as provided under **Rule 6 of the Companies (Audit and Auditors) Rules, 2014, as stated below:**

- a. Where a company is required to constitute an Audit Committee
  - i. Such Audit Committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent
  - ii. The Board shall consider the recommendation of such a committee, and make its recommendation for appointment of the next auditor by the members in the annual general meeting.
- b. In other cases, the Board shall itself consider the matter of rotation of auditors and make its recommendation for appointment of the next auditor by the members in the annual general meeting.

**Author's Note:** Most provisions of Rule 6 are either complementary, or in confirmation / conformance to Rule 3.

In case where Audit committee is not required to be constituted under **section 177**, but constituted by the company voluntarily, then such audit committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent; but in such cases board may or may not consider the recommendation of such committee.

### **Manner of Rotation in Case of Auditors Appointed Prior to Commencement of this Act and Continuing After Such Commencement [Rule 6(3)]**

For the purpose of the rotation of auditors in case of an auditor (whether an individual or audit firm), the period for which the individual or the firm has held office as auditor prior to the commencement of the Act shall be taken into account for calculating the period of five consecutive years or ten consecutive years, as the case may be.



**Example:** Dass & Dass Co, a Chartered Accountants firm was appointed as auditor of Modern Furniture on 28th September 2012. The firm can continue to assume the office of auditor till AGM conducted for financial year 2021-22.

### Illustration explaining rotation in case of individual auditor

Number of consecutive years for which an individual auditor has been functioning as auditor in the same company [till the first AGM held after the commencement of provisions of <b>section 139(2)</b> ]	Maximum number of consecutive years for which he may be appointed in the same company (including transitional period)	Aggregate period which the auditor would complete in the same company in view of column I and II
I	II	III
5 years (or more than 5 years)	3 years	8 years or more
4 years	3 years	7 years
3 years	3 years	6 years
2 years	3 years	5 years
1 years	4 years	5 years

Here,

- Individual auditors shall include other individuals or firms whose name or trademark or brand is used by such individuals, if any.
- consecutive years shall mean all the preceding financial years for which the individual auditor has been the auditor until there has been a break by five years or more.

### Illustration explaining rotation in case of audit firm

Number of consecutive years for which an audit firm has been functioning as auditor in the same company [till the first AGM held after the commencement of provisions of <b>section 139(2)</b> ]	Maximum number of consecutive years for which the firm may be appointed in the same company (including transitional period)	Aggregate period which the firm would complete in the same company in view of column I and II
I	II	III
10 years (or more than 10 years)	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 years	9 years	10 years

Here,

- Audit Firm shall include other firms whose name or trademark or brand is used by the firm or any of its partners.
- Consecutive years shall mean all the preceding financial years for which the firm has been the auditor until there has been a break by five years or more.

### **Manner of rotation in case of same network and common partner [Rule 6(3)]**

The incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms. The term same network includes the firms operating or functioning, hitherto or in future, under the same brand name, trade name or common control.

For the purpose of rotation of auditors, **a break (cooling period) in the term for a continuous period of five years** shall be considered as fulfilling the requirement of rotation. But if a partner (common partner), who is in charge of an audit firm and also certifies the financial statements of the company, retires from the said firm and joins another firm of chartered accountants, such other firm shall also be **ineligible to be appointed for a period of five years i.e., cooling period.**

### **Manner of rotation in case of joint auditors [Rule 6(4)]**

Where a company has appointed two or more individuals or firms or a combination thereof as joint auditors, the company may follow the rotation of auditors in such a manner that both or all of the joint auditors, as the case may be, do not complete their term in the same year.

#### **Illustration 1**

Modem Furniture Limited (MFL), despite not mandated by **Section 177** of the Act, read with Companies (Meetings of Board and its Powers) Rules, 2014 to constitute an audit committee; on their own on voluntary basis constitute such audit committee.

Such a committee recommended to the Board the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent; but board didn't consider the recommendation of such committee. Examine the legal validity of act of audit committee and board of MFL



**Answer** - Rule 6(1) read in conjunction with rule 6(2) of the Companies (Audit & Auditors) Rules, 2014 provides that in case where Audit committee not required to be constituted under **section 177**, but constituted by company, then also such audit committee shall recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on expiry of the term of such incumbent; but in such cases board may or may not consider the recommendation of said audit committee. Hence, the act of the audit committee and board at MFL is legally valid.

### First Auditors [Sub-Section 6]

The first auditor of a company, other than a **government Company**, shall be:

- Appointed by the Board of directors
- Within 30 days** of the date of registration of the company and
- The auditor so appointed shall **hold office until the conclusion of the first AGM**.

### Illustration 2

Unicorn Steel Private Limited is incorporated as on 02.06.2022, board of directors of the company held board meeting as on 15.06.2022 to appoint Jain Ajmera & Associates as a first auditor of the company for a term of 5 years. As per **section 139(6)** of the Companies Act, 2013, the board shall appoint the first director within 30 days from the date of registration of the company. Evaluate the legal validity:

**Options**

- Valid
- Invalid
- Valid after approval of shareholder in General Meeting
- Valid only after approval of Central Government

**Answer-b**

**Reason** - As per **section 139(6)**, the first auditor appointed by the Board of Director shall hold office until the conclusion of the first AGM. If the Board fails to exercise its powers i.e., appointment of first auditor, it shall

- Inform the members of the company and
- The company may appoint the **first auditor within 90 days at an extraordinary general meeting (EGM) and**
- Such auditor shall hold office till the conclusion of the first AGM

### Illustration 3

The Managing Director of PQR Limited wanted to appoint Mr. Ganpati, a practicing Chartered Accountant, as first auditor of the company. He himself, without consulting the board, appointed Shri Ganpati as auditor. Evaluate legal validity



**Answer-Section 139(6)** of the Companies Act, 2013 provides that "the first auditor or auditors of a company shall be appointed by the Board of directors within 30 days from the date of registration of the company". Hence in the instant case, the appointment of Mr. Ganpati by the Managing Director himself is invalid due to violation of **Section 139(6)** of the Companies Act, 2013.

## AUDITOR OF GOVERNMENT COMPANY [Sub-Section 5 & 7]

### First Auditor [sub-section 7]

The first auditor is to be appointed by **Comptroller and Auditor General of India (CAG)** within 60 days from the date of registration of the company, who shall hold office till the conclusion of the first annual general meeting; in case of

- i. A Government company or
- ii. Any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments.

**Author's Note:** If Comptroller and Auditor General of India fails in this respect, the Board is to appoint the auditor **within next 30 days** Further if the Board also fails to do so, it has to inform the members of the company who have to make the appointment **within 60 days at an extraordinary general meeting (EGM)**. Mind it, even appointed by Board or by embers at EGM, the first auditor shall hold office till the conclusion of the first annual general meeting

### Subsequent Auditor [Sub-Section 5]

In respect of financial year, the Comptroller and Auditor General of India shall appoint a **duly qualified auditor within 180 days** from the commencement of the financial year, who shall hold office till conclusion of annual general meeting: in case of:

- a. A Government company or
- b. Any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments.

### Filling Up Casual Vacancy [Sub-Section 8]

**Other Than Company Whose Accounts Are Subject to Audit by An Auditor Appointed by the CAG**



The Board may fill any **casual vacancy in the office of an auditor within 30 days**. Any auditor appointed in a casual vacancy shall hold office until the conclusion of the **next annual general meeting**.

**Author's Note:** Where such vacancy is caused by the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board

### **Company Whose Accounts Are Subject to Audit by An Auditor Appointed by the CAG**

Casual vacancy of an auditor shall be **filled by the Comptroller and Auditor General of India within 30 days**.

Further, in case the CAG **does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within the next 30 days**.

**Example:** Prakash Carriers Limited appointed Mr. Raman as its auditor in the Annual General Meeting held on 30 September, 2022. Initially, he accepted the appointment. But he resigned from his office on 31 October, 2022 for personal reasons. The Board of directors seeks advice for filling up the vacancy by appointment of Mr. Albert as auditor.

In the present case, as the auditor has resigned, the casual vacancy created can be filled up by the Board appointing Mr. Albert. However, the appointment of Mr. Albert must be approved by the company by passing of an ordinary resolution at a general meeting of the company which must be convened by the Board within 3 months of the recommendation of the Board. Mr. Albert will be entitled to hold office till the conclusion of the next Annual General Meeting.

### **Re-Appointment of Retiring Auditor [Sub-Section 9 And 10]**

As per **sub-section 9**, a retiring auditor may be **re-appointed at an AGM if:**

- a. He is not disqualified for re-appointment,
- b. He has not given a notice in writing to the company of his unwillingness to be re-appointed; and
- c. A special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed.

Further as per **sub-section 10**, where at any AGM, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

**Author's Note:** Even in case of continuation of the auditor due to deeming provision of **sub-section 10**, the conditions specified under **sub-section 9** shall be checked.



## Audit Committee's Recommendation [Sub-Section 11]

**Sub-section 11** prescribes the confirming provision, that where a company is required to constitute an Audit Committee under **section 177**, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee.

## Removal, Resignation of Auditor and Giving of Special Notice [Section 140]

**Section 140** of the Companies Act, 2013 provides for removal, resignation of auditor and giving of special notice. According to this section:

### Removal Of Auditor Before His Term [Sub-Section 1 Read with Rule 7 of the Companies (Audit & Auditors) Rules, 2014]

#### Manner And Procedure

The auditor appointed under **section 139** may be removed from his office before the expiry of his term only by-

- a. A special resolution of the company and
- b. After obtaining the previous approval of the Central Government (powers are delegated to Regional Director) by making an application in **Form ADT- 2** that shall be accompanied with the prescribed fees as provided for this purpose under the Companies (Registration Offices and Fees) Rules, 2014.

**Author's Note:** The application shall be made to the Central Government within 30 days of the resolution passed by the Board. The Company shall hold the general meeting within 60 days of receipt of approval of the Central Government for passing the special resolution.

**Example:** Mr. Suresh, a Chartered Accountant, was appointed by the Board of Directors of AB Limited as the First Auditor. The company in the General Meeting removed Mr. Suresh without seeking the approval of the Central Government and appointed Mr. Gupta as an auditor in his place. The first auditor appointed by the Board of Directors can be removed in accordance with the provision of **Section 140(1)** of the Companies Act, 2013. Hence, the removal of the first auditor in this case is invalid. The company contravened the provision of the Act.

In case of a Specified IFSC public company and Specified IFSC private company, where, within a period of sixty days from the date of submission of the application to the Central Government under this **subsection**, no decision is communicated by the Central Government to the company, it would be deemed that the Central Government has approved the application and the



company shall appoint a new auditor at a general meeting convened within three months from the date of expiry of the sixty days period.

**Giving Opportunity of Being Heard (Audi Alteram Partem)**

Before taking any action for removal of the auditor before the expiry of his term, the auditor concerned shall be given a reasonable opportunity of being heard. The Latin maxim, 'Audi Alteram Partem' is the principle of natural justice where every person gets a chance of being heard to respond to the charge, evidence or action against them.

**Illustration 4**

**Special Resolution to remove auditor at general meeting shall be passed within form the approval from central government.**

- a. 30 days
- b. 1 month
- c. 60 days
- d. 3 months

**Answer - c**

**Reason -** Rule 7(3) of the Companies (Audit & Auditors) Rules, 2014 that states the company shall hold the general meeting within sixty days of receipt of approval of the Central Government for passing the special resolution.

**Summary Of Steps for Removal of Auditor**



**Companies (Audit and Auditors) Rules, 2014]**  
**File A Statement (Sub-Section 2 Read with Rule 8]**

If the Auditor has resigned from the company, he shall file a statement in the **Form ADT-3 with the company and the Registrar within a period of 30 days from**



the date of such resignation. The auditor shall indicate the reasons and other facts as may be relevant with regard to his resignation, in the statement.

### Statement to CAG In Case of Government Company [Sub-Section 2]

The auditor shall file such statement with the Comptroller and Auditor-General of India (CAG) along with the company and the Registrar indicating the reasons and other facts as may be relevant with regard to his resignation, in case if he is auditor of:

- i. A Government company or
- ii. Any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments.

### Summary

Particulars	In case of Government Co.	In other cases,
Form of statement	ADT-3	ADT-3
Time Period for filling	Within 30 days of resignation	Within 30 days of resignation
Statement filled with	Company, Registrar & CAG	Company and registrar

### Penalty For Contravention [Sub-Section 3]

If the auditor does not comply with **aforsaid provision of filing statement, then;**

a. He or it shall be liable to a penalty of **50,000** or an amount equal to the remuneration of the auditor, **whichever is less**

and

b. In case of continuing failure, with a **further penalty of 500** for each day after the first during which such failure continues, subject

### Appointing Auditor Other Than the Retiring Auditor [Sub- Section 4]

#### Special Notice for Resolution

If the retiring auditor has **not completed a consecutive tenure of 5 years** (or **10 years in case** of firm, as the case may be), special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor, or providing expressly that a retiring auditor shall not be re-appointed.

#### Copy Of Special Notice to Retiring Auditor

On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor.



### Representation of Auditor

Where notice is given of such a resolution and the retiring auditor makes with respect thereto representation in writing to the company (not exceeding a reasonable length) and requests its notification to members of the company, the company shall, unless the representation is received by it too late for it to do so,

- a. In any notice of the resolution given to members of the company, state the fact of the representation having been made; **and**
- b. Send a copy of the representation to every member of the company to whom notice of the meeting is sent, whether before or after the receipt of the representation by the company.

### If A Copy of The Representation Is Not Sent to Members

If a copy of representation is not sent to member as aforesaid,

- a. Either because it was received too late or of the company's default, the auditor may (without prejudice to his right to be heard orally) require that the representation shall be read out at the meeting
- b. A copy of such representation shall be filed with the Registrar.

**Second proviso to section 140(4)** read with Rule 78 of the National Company Law Tribunal Rules, 2016, provides, if the Tribunal i.e., NCLT is satisfied:

- a. On an application in **Form No. NCLT. 1** may be filed by the director on behalf of the company or the aggrieved auditor to the Tribunal
- b. That the rights conferred by the provisions of **section 140** are being abused by the auditor
- c. Then, the copy of the representation need not be sent and the representation need not be read out at the meeting.

### Auditor Acts in A Fraudulent Manner or Abetted or Colluded in Any Fraud [Sub-Section 5]

**Tribunal May Order the Company to Change Its Auditor/S.**

Without prejudice to any action under the provisions of this Act or any other law for the time being in force, the Tribunal (ie. NCLT) either on

- a. Its own (Suo-moto); or
- b. An application (in **Form No. NCLT 9**) made to it by the Central Government;
- c. An application (in **Form No. NCLT 9**) made to it by any person concerned,

If it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors.



**Rule 78(3)** of the National Company Law Tribunal Rules, 2016 provides exactly similar provision to what is stated as first proviso to **Sub-section 5 of Section 140**, if the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall within fifteen days of receipt of such application make an order that the auditor shall not function as an auditor and the Central Government may appoint another auditor in his place.

### Ineligibility Of Auditor to Be Appointed and Criminal Liability

An auditor, whether individual or firm, against whom final order has been passed by the Tribunal under **section 140**, shall;

- a. **Not be eligible to be appointed** as an auditor of any company for **a period of 5 years from** the date of passing of the order **and**
- b. Also be liable for action under **section 447** of the Companies Act 2013.

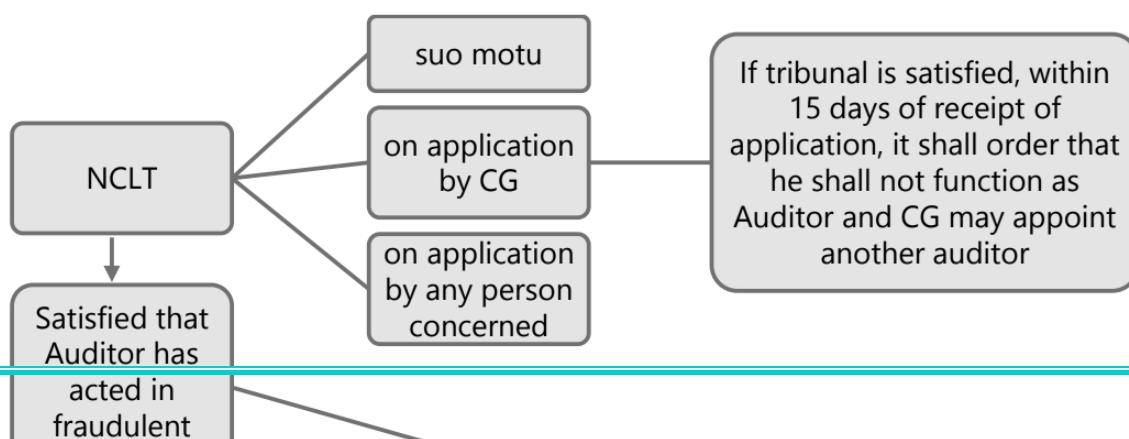
**Author's Note:** In case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers. The word "auditor" also includes a firm of auditors.

### Illustration 5

FLP Ltd, engaged in the business of real estate and energy, defaulted on its borrowings which amounted to thousands of crores. During the year ended 31st March 2023, a fraud was uncovered in respect of various transactions of the company and it was observed by the Central Government that the auditors of the company were involved in such fraud. Please suggest what can be the course of action in this case.

**Answer -** The Central Government may apply to the Tribunal in respect of such matters highlighting that the auditors miserably failed to fulfil their duties as auditors of the company. If the Tribunal is satisfied that the auditors were involved in the fraud with the company, the Tribunal may direct the company to change its auditors and those auditors shall not be eligible to be appointed as auditor of any company for 5 years and also liable for action under **section 447** of the Companies Act 2013.

### Summary Of Sub-Section 5



**Arsh Joshi**

## Eligibility, Qualifications and Disqualifications of Auditors [Section 141]

**Section 141** of the Companies Act, 2013 provides for eligibility, qualifications and disqualifications of auditors.

### Qualification Of an Auditor [Sub-Section 1 And 2]

#### Auditor Shall Be CA in Practice [Sub-Section 1]

A person shall be eligible to be appointed as an auditor of a company only if he is a chartered accountant as defined in clause (b) of **sub-section (1)** of **section 2** of the Chartered Accountants Act, 1949 who holds a valid certificate of practice under **sub-section (1)** of **section 6** of that Act.

**Author's Note:** Since **section 139** allows a firm also to be appointed as an auditor, hence proviso to **section 141(1)** prescribe clearly that only those firms wherein majority of partners practicing in India, are qualified for appointment by its firm name.

### Who shall sign if firm appointed as Auditor [Sub-section 2]

Where a firm including a Limited Liability Partnership is appointed as an auditor of a company, only the partners who are Chartered Accountants shall be authorized to act and sign on behalf of the firm.

### Disqualifications of Auditors [Sub-Section 3 Read With Rule 10 Of Companies (Audit and Auditors) Rule, 2014]



## Following persons shall not be qualified for appointment as auditor of a company

- a. A body corporate other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008;
- b. An officer or employee of the company.
- c. A person who is a partner, or who is in the employment, of an officer or employee of the company;

### Illustration 6

Mr. Anil, a Chartered accountant, is a partner of a firm and has been appointed as an auditor of Laxman Ltd. in the Annual General Meeting of the company held in September 2022 in which he accepted the assignment. Subsequently, in January 2023, he offered Bharat, another Chartered Accountant, who is the Manager Finance of Laxman Ltd., to join the firm of Anil as a partner.

**Answer-** Section 141(3)(c) of the Companies Act, 2013 prescribes that any person who is a partner or in employment of an officer or employee of the company will be disqualified to act as an auditor of a company. Sub-section (4) of Section 141 provides that an auditor who becomes subject, after his appointment, to any of the disqualifications specified in sub-sections (3) of Section 141, shall be deemed to have vacated his office as an auditor.

In the present case, Anil is auditor of M/s Laxman Limited and any employee of Laxman Limited cannot become the Partner of the firm where Anil is a Partner. In case that happens, he/the firm shall be deemed to have vacated the office of the auditor of M/s Laxman Limited.

- d. A person who himself or his partner is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company (i.e., fellow subsidiary) or his relative or partner

### Illustration 7

"Mr. Ashish", a practicing Chartered Accountant, is holding securities of "XYZ Ltd." having face value of 900/-. Whether Mr. Ashish is qualified for appointment as an Auditor of "XYZ Ltd."?

**Answer-** As per section 141 (3)(d) (i) an auditor is disqualified to be appointed as an auditor if he, or his partner is holding any security or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such



holding company. In the present case, Mr. Ashish is holding a security of 900 in XYZ Ltd, therefore he is not eligible for appointment as an Auditor of "XYZ Ltd".

**Author's Note:** In earlier act Le. Companies Act 1956 the holding securities of par value up to the limit of 1000 by the auditor was not the disqualification criteria. Under current Act i.e., Companies Act 2013, not a single rupee of holding by an auditor is allowed.

e. A person who's relative (defined u/s 2(77) is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company (ie. fellow subsidiary) of face value exceeding ₹1,00,000.

### Illustration 8

"Mr. P" is a practicing Chartered Accountant and "Mr. Q", the relative of "Mr. P is holding securities of "ABC Ltd." having face value of \*90,000/- . Whether "Mr. P" is qualified for being appointed as an auditor of "ABC Ltd."?

**Answer:** As per section 141 (3)(d)(i), an auditor is disqualified to be appointed as an auditor if he, or his relative or partner holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company. Further as per proviso to this Section, the relative of the auditor may hold the securities or interest in the company of face value not exceeding of 1,00,000. In the present case, Mr. Q. (relative of Mr. P, an auditor), is having securities of 90,000 face value in ABC Ltd., which is as per requirement of proviso to section 141(3)(d)(i). Therefore, Mr. P will not be disqualified to be appointed as an auditor of ABC Ltd.

Though rule 10(1) says, a relative of an auditor may hold securities in the company of face value not exceeding rupees one lakh but here rather than a literal interpretation, reasonable construction is required. And holding of all the relatives together shall be checked against the threshold.

Further, even if a relative of one of the partners of any firm holds securities or interests exceeding the threshold then, not only such partner, even firms shall not be eligible to be appointed as auditor.

The threshold condition specified above shall, wherever relevant, be also applicable in the case of a company not having share capital or other securities. If the relative acquires any security or interest above the prescribed threshold i.e., 1,00,000, the corrective action to maintain the limits as specified above shall be taken by the auditor within 60 days of such acquisition or interest.

### Illustration 9



"BC & Co." is an audit firm having partners "Mr. B" and "Mr. C" and "Mr. A", relative of "Mr. C", is holding securities of "MWF Ltd." having face value of \*1,10,000. Whether "BC & Co." is qualified for appointment as auditor of "MWF Ltd."?

**Answer-** As per **section 141(3)(d)(i)** an auditor is disqualified to be appointed as an auditor if he, or his relative or partner holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company. Further as per proviso to this Section, the relative of the auditor may hold the securities or interest in the company of face value not exceeding of 1,00,000. In the instant case, BC & Co, will be disqualified for appointment as an auditor of MWF Ltd as the relative of Mr. Cie. partner of BC & Co., is holding the securities in MWF Ltd which is exceeding the limit mentioned in proviso to **section 141(3)(d)(i)**

- f. A person who himself, or whose partner or relative is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of 5 Lakh
- g. A person who or who's relative or partner has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of one lakh rupees
- h. A person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company.

The term "business relationship shall be construed as any transaction entered into for a commercial purpose, but except-

Commercial transactions which are in the nature of professional services permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;

Commercial transactions which are in the ordinary course of business of the company at arm's length price like sale of products or services to the auditor as customer by the companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.

- i. A person who's relative is a director or is in the employment of the company as a director (as defined u/s 2(34) or key managerial personnel (as defined u/s 2(51):
- j. A person who is in full time employment elsewhere



k. A person or a partner of a firm holding appointment as its auditor, if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than 20 companies.

**Note:** While calculating the ceiling limit of 20, the one person companies, small companies and private companies having paid-up share capital less than 100 crore rupees shall be excluded.?

The exceptions provided above shall be applicable only to those Private Companies which has not committed a default in filing its financial statements under **section 137** of the said act or annual return under **section 92** of the said act with the registrar

Before appointment is given to any auditor, the company must obtain a certificate from him to the effect that the appointment, if made, will not result in an excess holding of company audit by the auditor concerned over the limit laid down in **section 141(3)(g)** of the Companies Act, 2013

### Illustration 10

"ABC & Co." is an audit firm having partners "Mr. A", "Mr. B" and "Mr. C". Chartered Accountants. "Mr. A", "Mr. B" and "Mr. C" are holding appointments as auditors in 4, 6 and 10 companies respectively.

- i. Provide the maximum number of audits remaining in the name of "ABC & Co."
- ii. Provide the maximum number of audits remaining in the name of individual partner Le. Mr. A. Mr. B and Mr. C.

**Answer:** In the instant case, Mr. A is holding appointments in 4 companies, Mr. B is having appointments in 6 companies and Mr. C has appointments in 10 companies. In aggregate all three partners are having 20 audits.

As per **section 141(3)(g)** of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor if he is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies other than one person companies, dormant companies, small companies and private companies having paid-up share capital less than 100 crore.

As per **section 141 (3)(g)**, this limit of 20 company audits is per person. In the case of an audit firm having 3 partners, the overall ceiling will be  $3 \times 20 = 60$  companies' audits. Sometimes, a Chartered Accountant may be a partner in a number of auditing firms. In such a case, all the firms in which he is partner or proprietor will be together entitled to 20 company audits only on his account.

Therefore, ABC & Co. can hold appointment as an auditor of 40 more companies:

Total Number of audits for which the firm would be eligible =  $20 \times 3 = 60$



Number of audits already taken by all the partners  
In their individual capacity =  $4+6+10$  =20

Remaining number of audits available to the firm =20

With reference to above provisions, an auditor can hold more appointment as auditor (i.e. ceiling limit as per **section 141(3)(g)** already holding appointments as an auditor). Hence

- i. Mr. A can hold:  $20 - 4 = 16$  more audits.
- ii. Mr. B can hold  $20-6= 14$  more audits and
- iii. Mr. C can hold  $20-10 = 10$  more audits.

**Author's Note:** It has been assumed that the companies given in the question are not one person companies, dormant companies, small companies and private companies having paid-up share capital less than 100 crore.

l. a person who has been convicted by a court of an offense involving fraud and a period of 10 years has not elapsed from the date of such conviction;

m. A person who, directly or indirectly, renders any service referred to in **section 144** to the company or its holding company or its subsidiary company.

### Vacation Of Office by An Auditor [Sub-Section 4]

If a person appointed as an auditor of a company incurs any of the disqualifications specified in **Section 141(3)** after his appointment, he shall vacate his office as Auditor. Such vacation shall be deemed to be a casual vacancy in the office of the auditor.

## Remuneration Of Auditors [Section 142]

**Section 142** of the Companies Act, 2013 provides for remuneration of auditors.

### Who Will Fix the Remuneration?

#### Subsequent Auditors

The remuneration of auditors has to be fixed by the company in general meeting or in such manner as the general meeting may determine.

#### First Auditor

While the remuneration of the first auditor shall be fixed by the board, which appointed him.



## Inclusion And Exclusions

### Components

a. The remuneration so fixed is, in addition to the fee payable to an auditor to,

#### **Includes**

b. The expenses, if any, incurred by him in connection with the audit of the company (i.e., out of pocket expense) and

c. Any facility extended to him.

### Exclusion

It is not to include any remuneration paid to him for any other service rendered by him at the request of the company.

**Example:** SHRD Private Ltd is engaged in the business of software and consultancy. The company has an annual turnover of 2,000 crore but its profit margins are not very good as compared to the industry standards. For the financial year ended 31 March 2019, the company proposed appointment of its statutory auditors at its Board meeting, however, the remuneration was not finalized. The statutory auditors completed the engagement formalities including the engagement letter between the company and the auditors and it was decided that the engagement letter be signed without fee i.e., with the clause that the fee be mutually decided. In this situation, an engagement letter with such an arrangement is valid.

## **Powers And Duties of Auditors and Auditing Standards** **[Section 143]**

### **Powers Of Auditors [Sub-Section 1]**

#### **Access To Books of Account and Vouchers**

Every auditor of a company shall have a right of access at all times to the books of accounts and vouchers of the company, whether kept at the registered office of the company or at any other place.

#### **Entitled to have necessary information and explanation**

He shall be entitled to require from the officers of the company such information and explanations as the auditor may consider necessary for the performance of his duties as auditor.

#### **Access to record of all its subsidiaries**

The auditor of a company which is a holding company shall also have the right of access to the records of all its subsidiaries and associate companies in so far as



it relates to the consolidation of its financial statements with that of its subsidiaries and associate companies.

## Duties Of Auditors

### Matters Of Inquiry [Sub-Section 1]

The auditor shall inquire into the following matters, namely

- a. Whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members,
- b. Whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;
- c. Where the company is not being an investment company or a banking company, whether so much of the assets of the company consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company.
- d. Whether loans and advances made by the company have been shown as deposits;
- e. Whether personal expenses have been charged to revenue account;
- f. Where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the
- g. account books and the balance sheet are correct, regular and not misleading.

### Report to members [Sub-Section 2 and 3]

The auditor shall make a report to the members of the company on the following:

- a. On the accounts examined by him; and
- b. On every financial statement which are required by or under this Act to be laid before the company in general meeting; and

**Author's Note:** The auditor while making the report shall take into account the provisions of the Act, the accounting and auditing standards and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under **section 143(11)**. The auditor shall express his opinion on the accounts and financial statements examined by him. He shall express an opinion, according to him and to the best of his information and knowledge, whether they said accounts/financial statements give a true and fair view of the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year and such other matters as may be prescribed.



**Further, sub-section 3 requires, the auditors' report shall also state:**

- a. Whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;
- b. Whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;
- c. Whether the report on the accounts of any branch office of the company audited under **sub-section (8)** by a person other than the company's auditor has been sent to him under the proviso to that subsection and the manner in which he has dealt with it in preparing his report
- d. Whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;
- e. Whether, in his opinion, the financial statements comply with the accounting standards;
- f. The observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;
- g. Whether any director is disqualified from being appointed as a director under **sub section (2) of section 164**;
- h. Any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;
- i. Whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls;
- j. Such other matters as may be prescribed.

In context of clause j stated above, Rule 11 of the Companies (Audit & Auditors) Rules, 2014 ie. Other Matters to be Included in the Auditor's Report. requires



the auditor's report shall also include their views and comments on the following matters, namely.

- (i) Whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;
- (ii) 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;
- (iii) Whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.
- (iv) Whether the management has represented that, to the best of its knowledge and belief, other than as disclosed in the notes to the accounts, no funds have been:
  - 1. Advanced or loaned or invested (either from borrowed funds or share premium or any other sources or kind of funds) by the company to or in any other person(s) or entity(ies), including foreign entities ("Intermediaries"), with the understanding, whether recorded in writing or otherwise, that the Intermediary shall, whether, directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the company ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries;
  - 2. Received by the company from any person(s) or entity(ies), including foreign entities ("Funding Parties"), with the understanding, whether recorded in writing or otherwise, that the company shall, whether, directly or indirectly, lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Funding Party ("Ultimate Beneficiaries") or provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries; and
  - 3. Based on such audit procedures that the auditor has considered reasonable and appropriate in the circumstances, nothing has come to their notice that has caused them to believe that the representations under sub-clause (i) [i.e., pt 1] and (ii) [Le pt 2] contain any material mis-statement.
- (v) Whether the dividend declared or paid during the year by the company is in compliance with **section 123** of the Companies Act, 2013.
- (vi) Whether the company, in respect of financial years commencing on or after the 1st April, 2022, 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.

**Author's Note:** As per **sub-section 4 to section 143**, where any of the matters is answered in the negative or with a qualification, the auditor's report shall state the reason for the same.

Clause (i) of **Sub-Section (3) of Section 143** (i.e., "Whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls) shall not apply" to a private company, which is a one-person company or a small company; or  
ii. Which has turnover less than rupees fifty crore as per latest audited financial statement and which has aggregate borrowings from banks or financial institutions or anybody corporate at any point of time during the financial year less than rupees 25 crore.

The aforesaid exceptions, modifications and adaptations shall be applicable to a Private company which has not committed a default in filing of its financial statements under **section 137** or annual return under **section 92** of the said Act with the Registrar.

### **Illustration 11**

**MNO Ltd. is a listed company engaged in the business of trading of various products. The company also plans to start manufacturing of certain products which are currently traded.**

**During the course of its audit, the auditors completed all the procedures related to audit of financial statements. However, the auditor got stuck on one procedure because of which audit has not got concluded, Auditors are waiting for certain additional information - Director's report and Management Discussion and Analysis (MD&A) for their review. However, the management is not ready with this information and wants the auditors to complete their work without review of this information. Please advise as per the legal requirements.**

**Answer-**In the given case, the requirement of the auditors regarding additional information i.e., Director's report and MD&A without which they have not been able to conclude the audit doesn't look valid. The auditor is required to audit the financial statements and express an opinion on the same. The auditor does not audit this additional information.

Hence the auditor should conclude the work without delay because of this additional information.



### **Compliance With Auditing Standards [Sub-Section 9 And 10]**

Every auditor shall comply with the auditing standards. The Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the ICAI, in consultation with and after examination of the recommendations made by the National Financial Reporting Authority (NFRA).

It is further provided that until any auditing standards are notified, any standard or standards of auditing specified by the ICAI shall be deemed to be the auditing standards.

### **Additional matters to be reported in case of specified companies [Sub-Section 11]**

In respect of such class or description of companies, as may be specified in the general or special order by the Central Government, may in consultation with the NFRA directly, the auditor's report shall also include a statement on such matters as may be specified therein.

**Author's Note:** CARO 2020 issued by MCA should be complied by the statutory auditor of every company, on which it applies.

### **Reporting Of Frauds by Auditors [Sub-Section 12, 13 And 15 Read with Rule 13 Of the Companies (Audit and Auditors) Rules, 2014]**

#### **Fraud Involving Amount of One Crore or More [Sub-Section 12 Read with Rule 13(2)]**

Notwithstanding anything contained in this section, if an auditor of a company, in the course of the performance of his duties as auditor,

- a. Has reason to believe that an offense involving fraud
- b. Which involves or is expected to involve individually an amount of rupees one crore or above
- c. Is being or has been committed against the company by officers or employees of the company,
- d. He shall immediately report the matter to the Central Government within such time and in such a manner as may be prescribed.

In this regards Rule 13(2) the auditor shall report the matter to the Central Government in following manner

- a. The auditor shall report the matter to the Board or the Audit Committee; as the case may be, immediately but **not later than 2 days of his knowledge of the fraud, seeking their reply or observations within 45 days;**



- b. On receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board or the Audit Committee along with his comments (on such reply or observations of the Board or the Audit Committee) to the Central Government **within 15 days from the date of receipt of such reply or observations**;
- c. In case the auditor fails to get any reply or observations from the Board or the Audit Committee within the **stipulated period of 45 days**, he shall forward his report to the Central Government along with a note containing the details of his report that was earlier forwarded to the Board or the Audit Committee for which he has not received any reply or observations;
- d. The report shall be sent to the Secretary, Ministry of Corporate Affairs (MCA) in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an email in confirmation of the same;
- e. The report shall be on the letter-head of the auditor containing postal address, e-mail address and contact telephone number or mobile number and be signed by the auditor with his seal and shall indicate his Membership Number, **and**
- f. The report shall be in the form of a statement as specified in **Form ADT-4**.

### **Fraud Involving Amount Less Than One Crore**

#### **Report To Audit Committee or Board [First Proviso to Sub-Section 12 Read with Rule 13(3)]**

In case of a fraud involving lesser than an amount of rupees one crore, the auditor shall report the matter to the audit committee (if constituted under **section 177**) or to the Board (in other cases) immediately **but not later than two days of his knowledge** of the fraud and he shall report the matter specifying the following:

- a. Nature of Fraud with description;
- b. Approximate amount involved; and
- c. Parties involved.

#### **Disclosure in Board's Report [Second Proviso to Sub-section 12 read with Rule 13(4)]**

The audit committee or the Board shall disclose the following details about such frauds (reported to them, but not to the Central Government i.e., when amount involved is less than 1 crore), in the Board's report:

- a. Nature of fraud with description;
- b. Approximate amount involved;
- c. Parties involved, if remedial action not taken; and



d. Remedial actions taken.

### Exception of bonafide faith [Subsection 13]

No duty to which an auditor of a company may be subject to shall be regarded as having been contravened by reason of his reporting the matter referred to in **sub-section (12)** if it is done in good faith.

### Penalty for non-compliance of section 143(12) [Sub-section 15]

If any auditor, cost accountant, or company secretary in practice does not comply with the provisions of **sub-section (12)**, he shall

- a. Be liable to a penalty of five lakh rupees in case of a listed company, and
- b. Be liable to a penalty of one lakh rupees in case of any other company.

### Summary of quantum of penalty

liable	In case of	Quantum
auditor, cost accountant, or company secretary in practice does not comply with the provisions of <b>section 143(12)</b>	listed company	five lakh rupees
	any other company	five lakh rupees

### Illustration 12

NSH Ltd is engaged in the business of retail and is listed on the National stock exchange. The company recently acquired a business undertaking to expand its business. During the year, certain transactions amounting to thousands of rupees were carried out by the employees/ directors of the company which the management found suspicious and appointed a forensic consultant to carry out their review. Pursuant to this review process, certain suspicious transactions were identified by the management and the management reported these transactions to the appropriate authorities. During the course of statutory audit, such transactions were also made known to the statutory auditors. How should the auditor deal with such matters?

**Answer-**As per **Section 143(12)** of the Companies Act, 2013, the auditor is required to report to the Audit Committee or to the Board of Directors and, where applicable, to the Central Government an offense of fraud in the company by its officers or employees only if he is the first person to identify/note such instance in the course of performance of his duties as an auditor. In this case, the suspicious transactions have been identified by the management first and information about the same has been given by the management to the auditor. Accordingly, the auditor should report about this matter to the Auditor.



Committee/Board of Directors but the auditor would not be required to report the same to the Central Government.

**Author's Note:** The auditors need to report about this matter appropriately in their CARO report.

## **Audit Of Government Companies [Sub-Section 5, 6 & 7]**

### **Powers vested with CAG [Sub-section 5]**

**Sub-section 5** provides, in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments;

- a. CAG shall appoint the auditor under **section 139(5) or 139(7)** and
- b. Direct such auditor the manner in which the accounts of the Government company are required to be audited and
- c. Thereupon the auditor so appointed shall submit a copy of the audit report to the CAG.

**The audit report among other things, shall include the following**

- a. The directions, if any, issued by the CAG;
- b. The action taken thereon; and
- c. Its impact on the accounts and financial statements of the company.

### **Comment by CAG and Supplementary Audit [Sub-section 6]**

**Sub-section 6** provides that, the CAG shall **within 60 days from the date of receipt of the audit report has a right to;**

- a. Conduct a supplementary audit of the financial statement of the company by such person or persons as he may authorize in this behalf; and for the purposes of such audit, require information or additional information to be furnished to any person or persons, so authorized, on such matters, by such person or persons, and in such form, as the CAG may direct, and
- b. Comment upon or supplement such audit reports.

**Author's Note:** Any comments given by the CAG upon, or supplement to, the audit report shall be sent by the company to every person entitled to copies of audited financial statements under **section 136(1)** and also be placed before the AGM of the company at the same time and in the same manner as the audit report.

### **Test Audit [Sub-section 7]**

For Government Company or Company controlled by State Government or Central Government, the CAG may, if he considers necessary, by an order, cause a test audit to be conducted of the accounts of such a company, without prejudice to



the provisions related to Audit and Auditors. The provisions of **section 19A** of the Comptroller and Auditor-General's (Duties, Powers and Conditions of Service) Act, 1971, shall apply to the report of such test audit.

### **Audit Of Accounts of Branch Office of Company [Sub- Section 8 Read with Rule 12 Of the Companies (Audit & Auditors) Rules, 2014]**

#### **Branch Office in India**

Where a company has a branch office, the accounts of that office shall be audited either by:

- a. The company's auditor appointed under **section 139**, or
- b. By any other person qualified for appointment as an auditor of the company under **section 139**.

#### **Branch office outside India**

If the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by.

- a. The company's auditor or
- b. By an accountant or
- c. By any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country.

### **Duties And Powers of The Company's Auditor with Reference to The Audit of The Branch and The Branch Auditor [Rule 12 Of the Companies (Audit & Auditors) Rules, 2014]**

The duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in **sub-sections (1) to (4) of section 143**.

The branch auditor shall submit his report to the company's auditor.

The provisions regarding reporting of fraud by the auditor shall also extend to such branch auditor to the extent it relates to the concerned branch.

### **Application Of Provisions of Section 143 To Cost Accountants and Company Secretary [Sub-Section 14]**

The provisions of this section shall mutatis mutandis apply to:

- a. The cost accountant conducting cost audit under **section 148**; or
- b. The company secretary in practice conducts a secretarial audit under **section 204**.

**Sub-rule 5 to rule 13** of the Companies (Audit & Auditors) Rules, 2014 provide exactly confirmatory provision



## Auditor Not to Render Certain Services [Section 144]

An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be.

But such services shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company), namely

- a. Accounting and bookkeeping services;
- b. Internal audit;
- c. Design and implementation of any financial information system;
- d. Actuarial services;
- e. Investment advisory services;
- f. Investment banking services;
- g. Rendering of outsourced financial services;
- h. Management services; and
- i. Any other kind of services as may be prescribed

### Snapshot of prohibited services

Accounting and book keeping services	Investment advisory services	Investment banking services
Internal audit	Actuarial services	Management services
Rendering of outsourced financial services	Design and implementation of any financial information system	Any other kind of services as may be prescribed

### Students are advised to take note;

1. However no other kind of services has been prescribed till date under clause i specified above.
2. Here it is worth noting that as per proviso to **section 148(3)**, no person (or firm including LLP) appointed under **section 139** as an auditor of the company shall be appointed for conducting the audit of cost records or vice-versa.

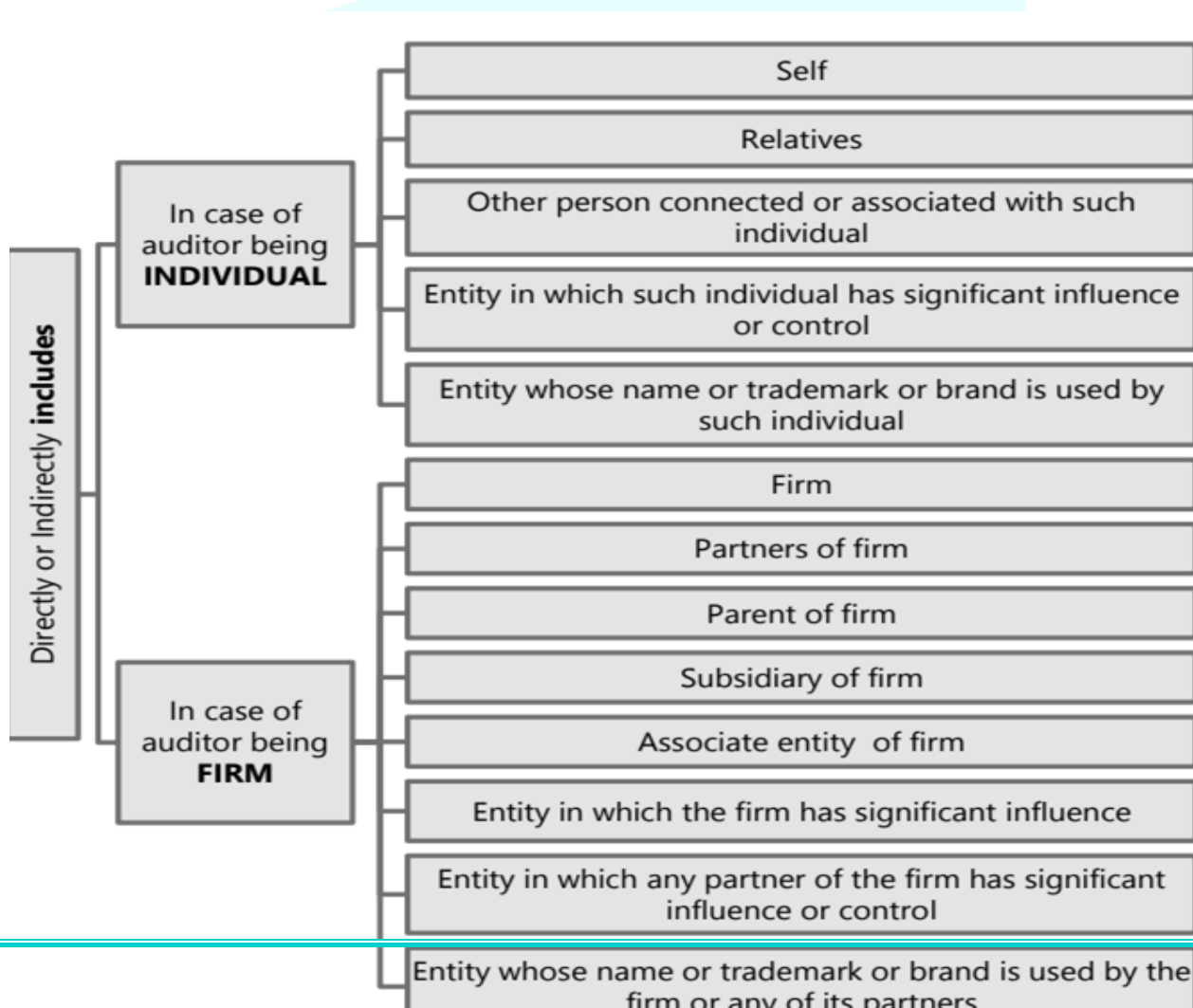


3. The term "directly or indirectly" shall include rendering of services by the auditor

- In case of auditor being an individual, either himself or through his relative or any other person connected or associated with such individual or through any other entity, whatsoever, in which such individual has significant influence or control, or whose name or trademark or brand is used by such individual;
- In case of auditor being a firm, either itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trademark or brand is used by the firm or any of its partners.

**Example:** MNP Ltd is a medium-sized company engaged in the business of pharmaceuticals. For the year ended 31st March 2018, the company is looking for appointment of GST (Goods and Services Tax) auditor. The company wants to appoint somebody for this work who is familiar with the business of the company i.e., who would have worked with the company in the past so that lesser efforts are required to get the GST audit completed. The company has options of statutory auditors that can be appointed for this work for the betterment of the company.

**Summary of what shall be included in directly and indirectly**



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## Auditors To Sign Audit Reports, Etc. [Section 145]

**Section 145** of the Companies Act, 2013 provides for auditors to sign audit reports, etc. The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of **sub-section (2) of section 141**

(i.e., in case of firm including LLP is appointed as an auditor of a company, only the partner who are Chartered Accountants shall be authorized to act and sign on behalf of the firm).

The qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company, mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

### Illustration 13

Whether the entire audit report needs to be read before the company in general meeting?

**Answer-**No, as per **section 145** of the Companies Act 2013, qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

## Auditors To Attend General Meeting [Section 146]

**Section 146** of the Companies Act, 2013 provides for auditors to attend general meetings.

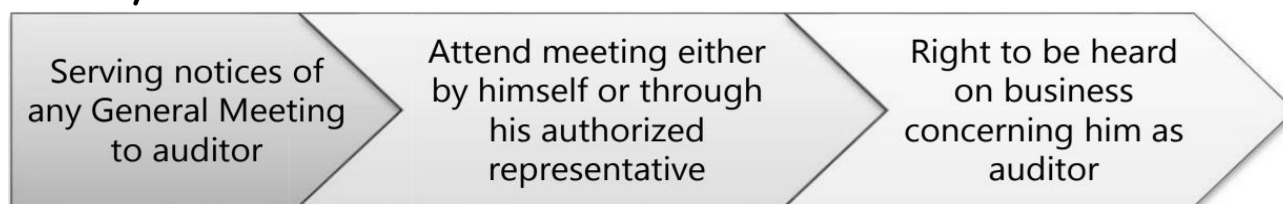
All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company.

The auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorized representative, who shall also be qualified to be an auditor, any general meeting.

The auditor shall have the right to be heard at such a meeting on any part of the business which concerns him as the auditor.



### Summary of the section 146



**Example:** Modern Furniture Limited (MFL) convened its general meeting on 21st March 2023, the notice of the same was not served to the auditor. Since company is obligated under **section 146** to forward a notice of general meeting to auditor as well, hence non- serving of notice to auditor by MFL is in contravention to **section 146** and liable for penalty under **section 147**.

### Illustration 14

Regarding the general meeting for which notice is served on auditor,

- Whether the auditor is mandatorily required to attend the said general meeting?
- If yes, whether he is required to attend the meeting personally?

**Answer-** Answer to first part is yes, while no in case of second, because as per **section 146** of the Companies Act 2013, the auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorized representative, who shall also be qualified to be an auditor, any general meeting.

## Punishment [Section 147] For Contravention

**Section 147** of the Companies Act, 2013 provides for punishment for contravention.

### Contravention By Company [Sub-Section 1]

#### Penalty On Company

If any of the provisions of **sections 139 to 146** (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.

#### Penalty on officer/s who is/are in default

If any of the provisions of **sections 139 to 146** (both inclusive) is contravened, every officer of the company who is in default shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

### Summary of quantum of penalty

Liabile	Minimum (in ₹)	Maximum (in ₹)
---------	----------------	----------------



Company	25,000	5,00,000
Every officer of the company who is in default	10,000	1,00,000

### Contravention By Auditor [Sub-Section 2 And 3]

#### Penalty On Auditor [Sub-Section 2]

If an auditor of a company contravenes any of the provisions of **section 139, section 144 or section 145**, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees or four times the remuneration of the auditor, whichever is less.

#### Summary of quantum of penalty

Liabe	Liabe for	Minimum (in ₹)	Maximum (in ₹)
Auditor	Contravenes any of the provisions of <b>section 139, 144 or 145, Company</b>	25,000	Lower of i. 5,00,000 or ii. 4 times the remuneration

### Penalty for knowing/wilful contravention [Proviso to Sub-section 2]

If an auditor has contravened any of the provisions of **section 139, section 144 or section 145**, knowingly or wilfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with the imprisonment for a term which may extend to 1 year and with the fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less.

#### Summary of quantum of penalty

Liabe	Liabe for	Minimum (in ₹)	Maximum (in ₹)
Auditor	Knowing or wilful contravenes any of the provisions of <b>section 139, 144 or 145, Company</b>	Fine of 25,000	Fine, Lower of 5,00,000 Or 8 times the remuneration
		and	
		Imprisonment for a term which may extend to 1 year	

### Refund of remuneration and payment of damages [Sub-section 3]

Where an auditor has been convicted under **sub-section 2**, he shall be liable to:

a. Refund the remuneration received by him to the company; and



b. Pay for damages to the company, statutory bodies or authorities or to members or creditors of the company for loss arising out of incorrect or misleading statements of particulars made in his audit report.

**Author's Note:** For operation of **sub-section 3**, the **sub-section 4** empowers the Central Government, to specify any statutory body or authority or an officer for ensuring prompt payment of damages to the company or the persons, by notification.

Such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.

### **Contravention By Audit Firm [Sub-Section 5]**

Where, in case of audit of a company being conducted by an audit firm, It is proved that the partner or partners of the audit firm has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability, Whether civil or criminal as provided in the Companies Act, 2013, or in any other law for the time being in force, For such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally.

**Author's Note:** 1. In case of criminal liability of an audit firm, in respect of liability other than fine, the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud shall only be liable.

2. Since acts constitute fraud, hence shall also be liable under **section 447**. Provisions of **section 447**, explained and decoded under book chapter 3 i.e., 'Prospectus and allotment of securities' of this module. Students may refer to the same.

### **Central Government to Specify Audit of Items of Cost in Respect of Certain Companies [Section 148]**

**Cost Records [Sub-Section 1 Read with Rule 3 And 5 Of the Companies (Cost Records and Audit) Rules, 2014]**

#### **Who Shall Prepare Cost Records? [Rule 3]**

Notwithstanding anything contained in the provisions related to audit and auditor (Chapter X), the Central Government may, by order, in respect of such class of companies engaged in the production of such goods or providing such services as may be prescribed, direct that particulars relating to the utilization of material

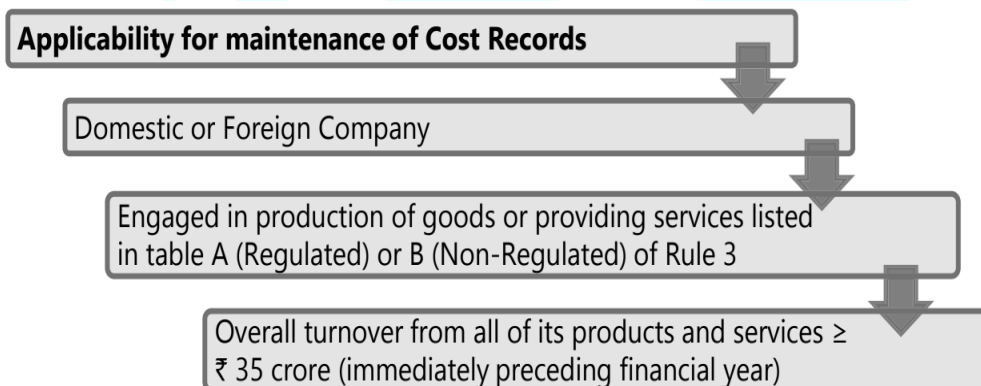


or labour or to other items of cost as may be prescribed shall also be included in the books of account kept under **section 128** by that class of companies.

The Central Government shall, before issuing such order in respect of any class of companies regulated under a special Act, consult the regulatory body constituted or established under such special Act.

For the purposes of **sub-section (1) of section 148** of the Act, rule 3 of the Companies (Cost Records and Audit) Rules, 2014 provides, the class of companies (including foreign companies defined in **clause (42) of section 2** of the Act) engaged in the production of the goods or providing services, specified in the Table A (6 Regulated Sectors) and/or Table B (33 Non-Regulated Sector), having an overall turnover from all its products and services of rupees thirty five crore or more during the immediately preceding financial year, shall include cost records for such products or services in their books of account

**Author's Note:** Nothing contained in Rule 3 shall apply to a company which is classified as a micro enterprise or a small enterprise including as per the turnover criteria under **sub-section (9) of section 7** of the Micro, Small and Medium Enterprises Development Act, 2006.



### Form and manner of Cost Records [Rule 5]

Every company covered by rule 3 explained above under these rules including all units and branches thereof, shall, in respect of each of its financial year, maintain cost records in **form CRA-1**.

The cost records shall be maintained on a regular basis in such a manner as to facilitate calculation of per unit cost of production or cost of operations, cost of sales and margin for each of its products and activities for every financial year on monthly or quarterly or half-yearly or annual basis.

The cost records shall be maintained in such manner so as to enable the company to exercise, as far as possible, control over the various operations and costs to achieve optimum economies in utilization of resources and these records shall also provide necessary data which is required to be furnished under these rules.



## Cost Audit [Sub-Section 2 To 7 Read with Rule 4 Of the Companies (Cost Records and Audit) Rules, 2014]

If the Central Government is of the opinion, that it is necessary to do so, it may, by order, direct that the audit of cost records of class of companies, which are covered aforesaid (under **sub-section 1** i.e., required to prepare cost records) and which have a net worth of such amount as may be prescribed or a turnover of such amount as may be prescribed, shall be conducted in the manner specified in the order.

As per **sub-section 4**, an audit conducted under this **section (cost audit u/s 148)** shall be in addition to the audit conducted under **section 143**. The cost statements, including other statements to be annexed to the cost audit report, shall be approved by the Board of Directors before they are signed on behalf of the Board by any of the directors authorized by the Board, for submission to the cost auditor to report thereon.

Sub-rule 1 to rule 4 provides every company specified in the item (A) of rule 3 shall be required to get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees fifty crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is rupees twenty five crore or more.

Whereas sub rule 2 provides every company specified in item (B) of rule 3 shall get its cost records audited in accordance with these rules if the overall annual turnover of the company from all its products and services during the immediately preceding financial year is rupees one hundred crore or more and the aggregate turnover of the individual product or products or service or services for which cost records are required to be maintained under rule 3 is rupees thirty-five crore or more.

Further sub-rule 3 to rule 4 provides exception from cost audits. The requirement for cost audit shall not apply to a company which is covered in rule 3, and

- a. Whose revenue from exports, in foreign exchange, exceeds seventy five percent of its total revenue; or
- b. Which is operating from a special economic zone.
- c. Which is engaged in generation of electricity for captive consumption through Captive Generating Plant. For this purpose, the term "Captive Generating Plant" shall have the same meaning as assigned in rule 3 of the Electricity Rules, 2005.

### Summary of Rule 4 i.e. Applicability of Cost Audit

Companies that are covered under rule 3 and engaged in any of						
6 Regulatory Sectors (Table A)			33 Non-Regulatory Sectors (Table B)			
Overall annual turnover from <b>all its products and services</b> during the immediately preceding financial year is <b>rupees fifty</b>	Revenue exceeds 75%	Special Economic Zone	Captive consumption.	Revenue exceeds 75%	Special Economic Zone	Captive consumption.
						Overall annual turnover from <b>all its products and services</b> during the immediately preceding financial year is <b>rupees one hundred crore or</b>



## Cost Auditor [Sub-Section 3 And 5]

### Who Can Be Appointed as Cost Auditor? [Sub-Section 3]

Only a Cost Accountant, as defined under **section 2(28)** of the Companies Act, 2013, can be appointed as a cost auditor.

Clause (b) of **sub-section (1) of section 2** of the Cost and Works Accountants Act, 1959 defines "Cost Accountant". It means a Cost Accountant who holds a valid certificate of practice under **sub-section (1) of section 6** of the Cost and Works Accountants Act, 1959 and is in full-time practice. Cost Accountant includes a Firm of Cost Accountants and an LLP of cost accountants.

First Proviso to **sub-section 3** provides that a person appointed under **section 139** as an auditor of the company (i.e., company auditor) shall not be appointed for conducting the audit of cost records.

### Illustration 15

Can a professional LLP which have CAs and CMAs as its partners, appointed as Cost Auditor u/s 148 as well as Statutory Independent Auditor u/s 139

**Answer:** No, because as per proviso to **section 148(3)**, no person (or firm including LLP) appointed under **section 139** as an auditor of the company shall be appointed for conducting the audit of cost records or vice-versa.

## Qualifications, Disqualifications, Rights, Duties and Obligations of Cost Auditor [Sub-Section 5]

The qualifications, disqualifications, rights, duties and obligations applicable to auditors (ie. applicable to company auditor) shall, so far as may be applicable, apply to a cost auditor appointed under **section 148** and it shall be the duty of the



company to give all assistance and facilities to the cost auditor appointed under this section for auditing the cost records of the company.

**Author's Note:** The provisions of **sub-section (12) of section 143** of the Act and the relevant rules made thereunder shall apply mutatis mutandis to a cost auditor during performance of his functions under **section 148** of the Act and rule notified thereunder.

### **Who Shall Appoint a Cost Auditor? (Sub-Section 3 Read with Rule 14 Of the Companies (Audit and Auditors) Rules, 2014]**

Rule 14 of the Companies (Audit and Auditors) Rules, 2014 provides that in the case of companies which are required to constitute an audit committee

- a. The Board shall appoint an individual, who is a cost accountant, or a firm of cost accountants in practice, as cost auditor on the recommendations of the Audit committee, which shall also recommend remuneration for such cost auditor;
- b. The remuneration recommended by the Audit Committee under (A) shall be considered and approved by the Board of Directors and ratified subsequently by the shareholders.

Whereas in the case of other companies which are not required to constitute an audit committee, the Board shall appoint an individual who is a cost accountant or a firm of cost accountants in practice as cost auditor and the remuneration of such cost auditor shall be ratified by shareholders subsequently.

### **Manner And Procedure - Appointment, Removal and Resignation [Rule 6 Of Companies (Cost Records and Audit) Rules, 2014]**

#### **Time Limit for Appointment**

The Cost Auditor shall **within one hundred and eighty days of the commencement of every financial year, appoint a cost auditor.**

#### **Written Consent and Certificate**

Before such appointment is made, the written consent of the cost auditor to such appointment, and a certificate following shall be obtained from him or her.

- a. The individual or the firm, as the case may be, is eligible for appointment and is not disqualified for appointment under the Act, the Cost and Works Accountants Act, 1959 and the rules or regulations made thereunder;
- b. The individual or the firm, as the case may be, satisfies the criteria provided in **section 141** of the Act, so far as may be applicable;
- c. The proposed appointment is within the limits laid down by or under the authority of the Act, and
- d. The list of proceedings against the cost auditor or audit firm or any



partner of the audit firm pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.

### Notice of appointment

Every company shall inform the cost auditor concerned of his or its appointment as such and file a notice of such appointment with the Central Government within a period of thirty days of the Board meeting in which such appointment is made or within a period of one hundred and eighty days of the commencement of the financial year, whichever is earlier, through electronic mode, in form CRA-2, along with the fee as specified in Companies (Registration Offices and Fees) Rules, 2014.

### Tenure of appointment as cost auditor

Every cost auditor appointed as such shall continue in such capacity till the expiry of one hundred and eighty days from the closure of the financial year or till, he submits the cost audit report, for the financial year for which he has been appointed.

### Removal of cost Auditor

The cost auditor appointed under these rules may be removed from his office before the expiry of his term, through a board resolution after giving a reasonable opportunity of being heard to the Cost Auditor and recording the reasons for such removal in writing.

**Author's Note:** Form CRA-2 to be filed with the Central Government for intimating appointment of another cost auditor shall enclose the relevant Board Resolution to the effect Nothing shall prejudice the right of the cost auditor to resign from such office of the company.

### Filling of casual vacancy in the office of a cost auditor

Any casual vacancy in the office of a cost auditor, whether due to resignation, death or removal, shall be filled by the Board of Directors within thirty days of occurrence of such vacancy and the company shall inform the Central Government in form CRA-2 within thirty days of such appointment of cost auditor

**Cost auditor to comply with cost auditing standards [Second Proviso to Sub-section 3]**



The auditor conducting the cost audit shall comply with the cost auditing standards.

Here, the expression "cost auditing standards" mean such standards as are issued by the Institute of Cost Accountants of India (erstwhile ICWAI), constituted under the Cost and Works Accountants Act, 1959, with the approval of the Central Government.

## Cost Audit Report

### Form and timing to submit cost audit report

The report on the audit of cost records shall be submitted by the cost accountant to the Board of Directors of the company.

Every cost auditor, who conducts an audit of the cost records of a company, shall submit the cost audit report along with his or its reservations or qualifications or observations or suggestions, if any, **in form CRA-3**.

Every cost auditor shall forward his **duly signed report within a period of one hundred and eighty days from the closure** of the financial year to which the report relates and the Board of Directors shall consider and examine such report, particularly any reservation or qualification contained therein,

**Author's Note:** The Companies which have got extension of time of holding Annual General Meeting under **section 96 (1)** of the Companies Act, 2013, **may file form CRA-4 within the resultant extended period of filing financial** statements under **section 137** of the Companies Act, 2013.

### Filing of cost audit report with Central Government [Sub-section 6 and 7 read with rule 4 of the Companies (Filing of Documents and forms in Extensible Business Reporting Language) Rules, 2015]

A company shall

- Within 30 days from** the date of receipt of a copy of the cost audit report
- Furnish the Central Government with such report
- Along with full information and explanation on every reservation or qualification contained therein.

**Rule 4** of the Companies (Filing of Documents and forms in Extensible Business Reporting Language) Rules, 2015, provides a company which is required to furnish cost audit report and other documents to the Central Government under **sub-section 6** of the **section 148** of the Act and rules made thereunder, shall file such report and other documents using the XBRL taxonomy given in Annexure III for the financial year commencing on or after 1 April 2014 in e-form CRA-4 specified under the Companies (Cost Records and Audit) Rules, 2014.



If, after considering the cost audit report and the information and explanation furnished by the company, the Central Government is of the opinion that any further information or explanation is necessary, it may call for such further information and explanation and the company shall furnish the same within such time as may be specified by that Government

### Summary of different form pertaining to cost records and cost audits

Form	Purpose
CRA-1	The manner in which cost records to be maintained
CRA-2	For intimation of appointment of cost auditor by company to the Central Government
CRA-3	Cost Audit Report
CRA-4	Filing of the cost audit report with the Central Government

### Contravention And Punishment Thereof [Sub-Section 8]

If any default is made in complying with the provisions of **section 148**;

- The company and every officer of the company who is in default shall be punishable in the manner as provided in **section 147(1)**;
- The cost auditor of the company who is in default shall be punishable in the manner as provided in **sub-sections (2) to (4) of section 147**.

**Note:** The provision of **section 147** explained in details under heading 10, earlier in this chapter.

### NFRA [National Financial Reporting Authority] And Auditor Monitoring and Enforcing Compliance with Auditing Standards

Rule 8 of The National Financial Reporting Authority Rules, 2018 empowers NFRA for the purpose of monitoring and enforcing compliance with auditing standards under the Act by a company or a body corporate governed under rule 3.

#### NFRA may:

- Review working papers (including audit plan and other audit documents) and communications related to the audit;
- Evaluate the sufficiency of the quality control system of the auditor and the manner of documentation of the system by the auditor, and
- Perform such other testing of the audit, supervisory, and quality control procedures of the auditor as may be considered necessary or appropriate.

Rule 8 further provides that:

#### NFRA may require:



1. Require an auditor to report on its governance practices and internal processes designed to promote audit quality, protect its reputation and reduce risks including risk of failure of the auditor and may take such action on the report as may be necessary.
2. Seek additional information or may require the personal presence of the auditor for seeking additional information or explanation in connection with the conduct of an audit.
3. Send a separate report containing proprietary or confidential information to the Central Government for its information.
4. Where the NFRA finds or has reason to believe that any law or professional or other standard has or may have been violated by an auditor, it may decide on the further course of investigation or enforcement action through its concerned Division.

**NFRA shall;**

1. Perform its monitoring and enforcement activities through its officers or experts with sufficient experience in audit of the relevant industry.
2. Publish its findings relating to non-compliances on its website and in such other manner as it considers fit, unless it has reasons not to do so in the public interest and it records the reasons in writing.

**NFRA shall not**

Publish proprietary or confidential information, unless it has reasons to do so in the public interest and it records the reasons in writing.

**Overseeing The Quality of Services And Suggesting Measures For Improvement**

Further Rule 9 of The National Financial Reporting Authority Rules, 2018 empowers NFRA for overseeing the quality of services and suggesting measures for improvement

- a. On the basis of its review, the NFRA may direct an auditor to take measures for improvement of audit quality including changes in their audit processes, quality control, and audit reports and specify a detailed plan with time-limits.
- b. It shall be the duty of the auditor to make the required improvements and send a report to the NFRA explaining how it has complied with the directions made by the NFRA.
- c. The NFRA shall monitor the improvements made by the auditor and take such action as it deems fit depending on the progress made by the auditor.
- d. The NFRA may refer cases with regard to overseeing the quality of service of auditors of companies or bodies corporate referred to in **rule 3 to the Quality Review Board constituted under the Chartered Accountants Act, 1949** or call for



any report or information in respect of such auditors or companies or bodies corporate from such Board as it may deem appropriate.

e. The NFRA may take the assistance of experts for its oversight and monitoring activities.

### **Filing Of Return with NFRA**

**Rule 5 requires every auditor of classes of companies** and bodies corporate governed by the NFRA, shall file a return with the Authority i.e., NFRA on or before 30th November every year in **Form NFRA-2**.

