

SUMMARY SHEET



Audit and Auditors



Contents

1	Introduction.....	2
2	Important terms	2
2.1	Members of Company	2
2.2	Difference between the public company and private Company	2
3	Section 139 -Appointment of auditors.....	3
3.1	How are auditors appointed in non-government companies?	3
3.1.1	What is a proper Manner and Procedure for selection of Auditors?.....	4
3.1.2	How are the first auditors of non-government company appointed?.....	4
3.1.3	Term of Individual auditor and Firms as auditor	5
3.2	Appointment of Auditors in Government companies	6
3.2.1	Appointment of first auditor in Government Companies	6
3.3	Casual Vacancy of Auditor	7
4	Section 140 - Removal, Resignation of Auditor and Giving of Special Notice	7
4.1	Removal of Auditor	7
4.2	Resignation of Auditor	8
4.3	Removal on Orders by Tribunal	8
5	Section 141 - Eligibility, qualifications, and disqualifications of auditors. —	9
5.1	Eligibility of Auditor.....	9
5.2	Qualification and Disqualification of Auditor	9
5.3	Disqualification.....	10
6	Section 142 - Remuneration of auditors.	10
7	Section 143 - Powers and duties of auditors and auditing standards.	10
7.1	Power of auditor	10
7.2	Duties of Auditor.....	10
7.3	Auditing Standards.....	11
7.4	Duties of Auditor – Reporting Frauds	11
7.5	Power and Duties of Financial Auditor Applies to Cost Auditor and Secretarial Auditor	12
8	Section 144 - Auditor not to render certain services	12
9	Section 145 - Auditor to sign audit reports, etc.....	12
10	Section 146 - Auditors to attend general meeting	12
11	Section 147 - Punishment for contravention	13
11.1	What is the Punishment to Companies?	13
11.2	What is the Punishment to Auditors?.....	13

12 Section 148 - Central Government to specify audit of items of cost in respect of certain companies
13

12.1 Who shall specify Audit of Items of Cost in Respect of Certain Companies?.....13

12.2 What are the items for which cost data needs to be maintained?13

12.3 What is the criteria for Cost Audit?14

12.4 Who Shall Conduct Cost Audit?14

12.5 Process of appointment of Cost Accountant.14

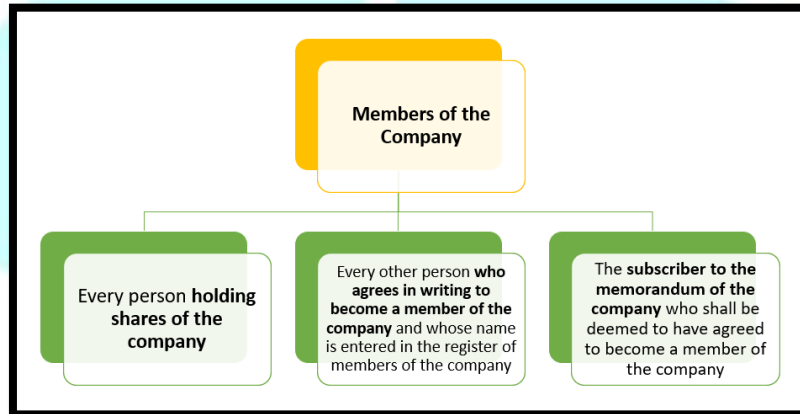
1 Introduction

In the Companies Act, 2013 as per the Syllabus mentioned, Specific reference to Chapter III, Chapter IV, Chapter VIII, Chapter X, Chapter XI, Chapter XII and Chapter XXVII is mentioned.

- In this lesson, we will cover Chapter X - Audit and Auditors, which comprises of section 139 to section 148.
- Before understanding the provisions of this chapter, let us learn few some basic terms which will help in better understanding of this lesson.

2 Important terms

2.1 Members of Company



The **Memorandum of Company** in short is like constitution of company.

2.2 Difference between the public company and private Company

Before proceeding with the provisions of this chapter, it is essential to understand the differences between public company and Private company.

Basis	Public Company	Private Company
Number of Members	Minimum 7 and there is no limit for Maximum members.	Minimum 2 and Maximum 200 members.
Transfer of shares	The shares of a publicly traded company are freely transferable , i.e., freely tradable in an open market called the stock exchange.	Shares of a private company are not freely transferable , as the articles of association contain restrictions.
Use of suffix	A public company must compulsorily include the words " Limited " in its name.	A private company must include " Private Limited " as a suffix in its name.

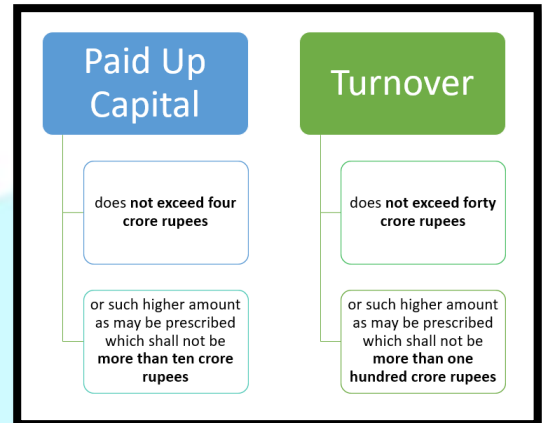
Public Companies are of two types namely Listed and unlisted companies.

1. **Listed Companies:** It is that company whose securities are listed on recognized stock exchange.
2. **Unlisted Companies:** It is that company whose securities are not listed on recognized stock exchange.

Private Companies are of two types of namely **Small Company** and **One Person Company** as explained below.

Definition of Small Company

- **Paid-up share capital** of which does **not exceed four crore rupees**, or such higher amount as may be prescribed which **shall not be more than ten crore rupees AND**
- **Turnover** in immediately preceding financial year does **not exceed forty crore rupees** or such higher amount as may be prescribed which shall not be more than one hundred crore rupees.



One Person Company - According to **Section 2 (62) of the Companies Act, 2013**, One Person Company means a company which has only one person as a member.

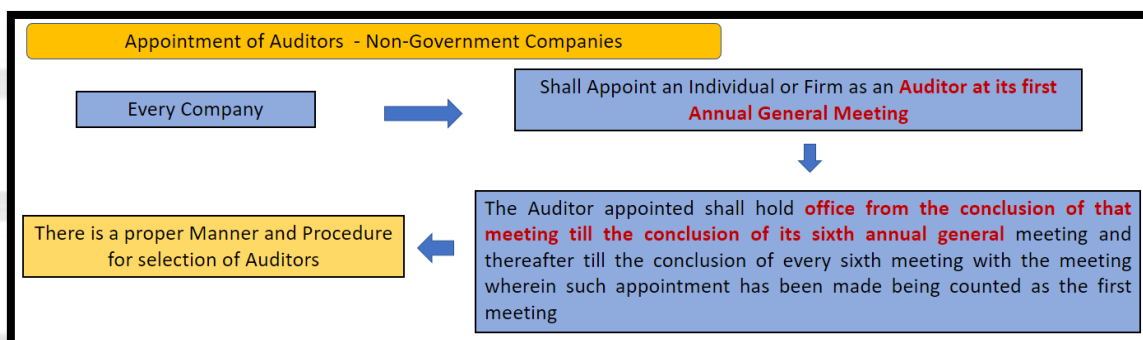
- It is incorporated as a private company which has only one member. Therefore, a corporation can be registered even when it only has one shareholder or member.
- **OPC cannot convert voluntarily into any kind of company unless two years** have expired from the date of incorporation of One Person Company, except **when paid-up capital is increased beyond 50 lakh rupees or its average annual turnover during the relevant period exceeds 2 crore rupees.**

3 Section 139 -Appointment of auditors.

Let us understand few basic terms before proceeding with section.

- Companies are of two types namely, Government Companies and Non-Government Companies
- The procedure for appointment of auditors is different in both. Let us discuss them one by one in the subsequent section.

3.1 How are auditors appointed in non-government companies?

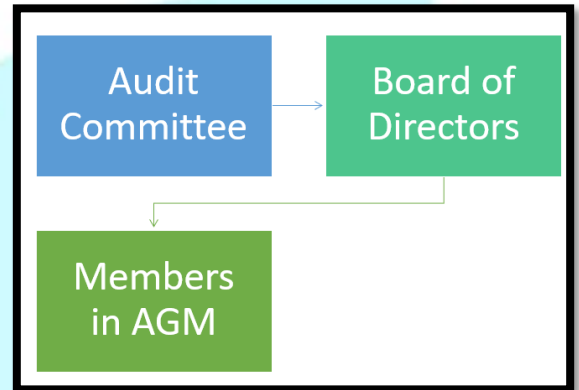


- **Term of Auditors in Non-government Companies** – The auditors have a tenure of **5 years**. (From the conclusion of the meeting in which auditor is appointed till the conclusion of every sixth meeting). This is discussed in detail in **the subsequent sections**.

3.1.1 What is a proper Manner and Procedure for selection of Auditors?

If a company has **Audit Committee**, then Audit committee **shall recommend the name of an individual** or a firm as auditor to the Board for consideration **otherwise the Board** shall consider and recommend an individual or a firm as auditor to the members in the **annual general meeting for appointment**.

If the Initial recommendation was made by **audit Committee to the Board**, then Board can send back or approve that recommendation.



1. If the **Board agrees with the recommendations of the Audit Committee**, it shall place the matter for consideration by **members in the annual general meeting**.
2. In **case of rejection**, Audit committee will reconsider the firm or Individual whose name was proposed earlier and may withdraw its recommendation. In such a case **the board send its own recommendation for consideration of the members in the annual general meeting**.
3. **Parameters for selection of auditor** –
 - **In case of Individual and in case of Firm** - The Audit Committee or the Board (as the case will be) shall take into consideration **the qualifications and experience of the individual or firm** are good enough to act as an auditor.
4. **Auditor to give consent** - The auditor to be appointed before the appointment **must give a written consent** and a certificate be obtained from him.
5. **Informing the Registrar** - Once the certificate is obtained and Auditor is appointed, the company shall file a notice of such appointment with the Registrar **within fifteen days of the meeting in which the auditor is appointed**.

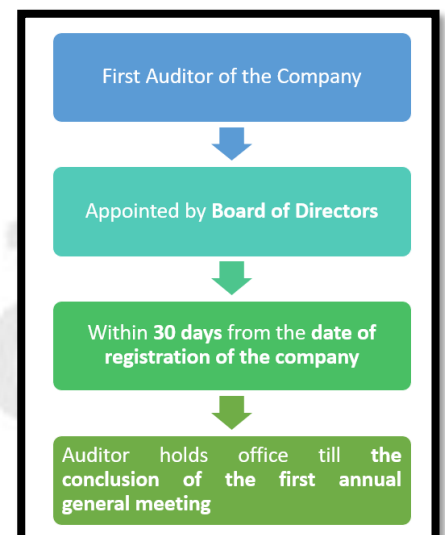
3.1.2 How are the first auditors of non-government company appointed?

Suppose a company is constituted for the first time, then how are its auditors appointed ?

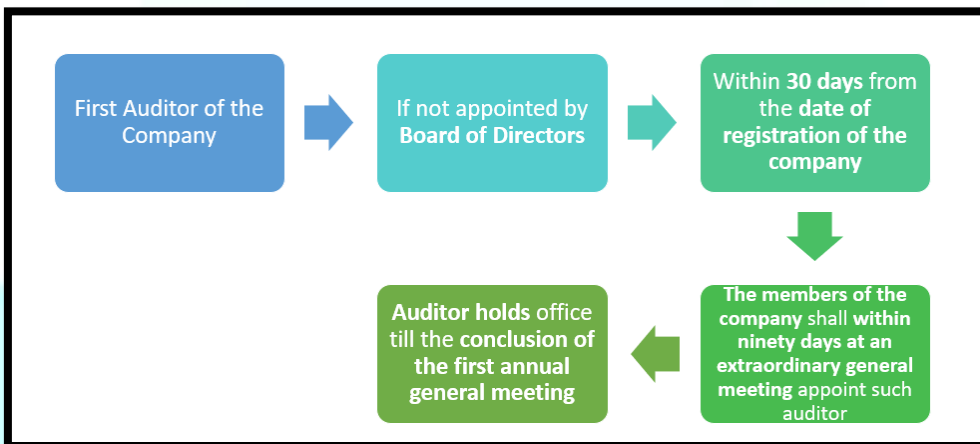
- There is a separate process for the appointment of first auditors of the company which is dealt in detail in this section.
- In the above section (3.1), we have discussed the appointment of auditors of the company during the normal course of its functioning.

Mode of appointment of first auditor of the company.

1. **The first auditor of a company** shall be appointed by the Board of Directors **within thirty days** from the date of registration of the company and **such auditor shall hold** office till the conclusion of the first annual general meeting. (As shown in the image)
2. In the case of failure of the Board to appoint such auditor with 30 Days, it shall inform **the members of the company**, who shall **within**

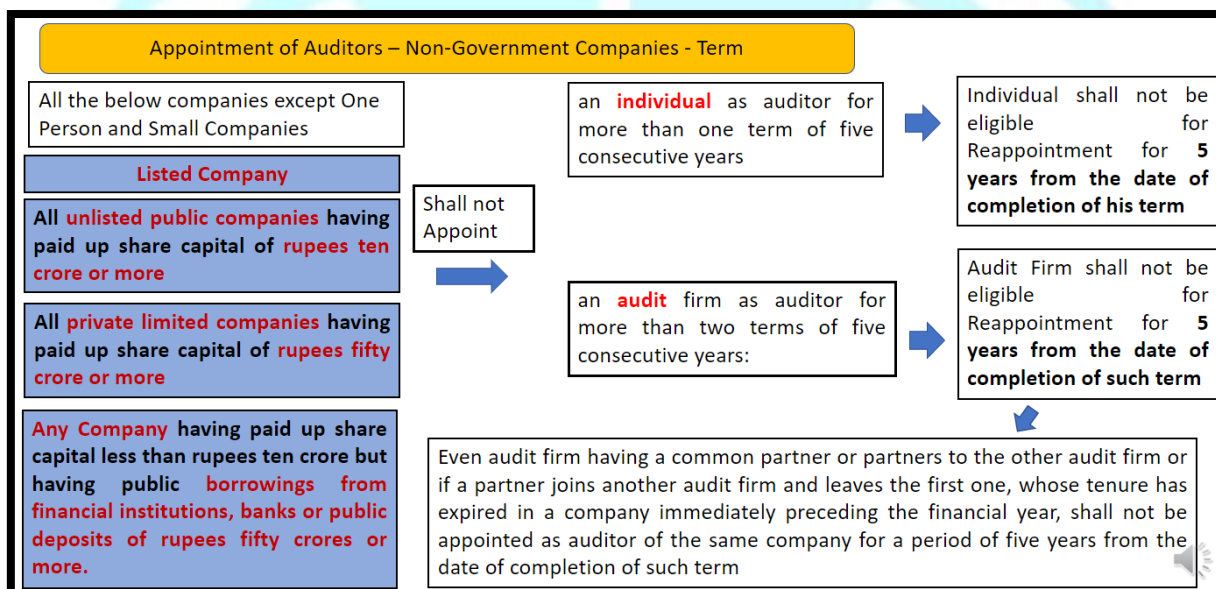


ninety days at an extraordinary general meeting appoint such auditor and such auditor shall hold office till the conclusion of the first annual general meeting.



3.1.3 Term of Individual auditor and Firms as auditor

The term of Individual and firm as an auditor is dealt in detail in the image below.



The above image depicts the companies that are supposed to appoint an auditor. The provision is applicable only to such companies. The entire image can be summed up in simple words as described in the below table.

Entities	Term	Cooling Off period for Reappointment
Individual as Auditor	One term of five consecutive years	5 years
Firm as Auditor	Two terms of five consecutive years	5 years

Rules are prescribed for rotation of auditors

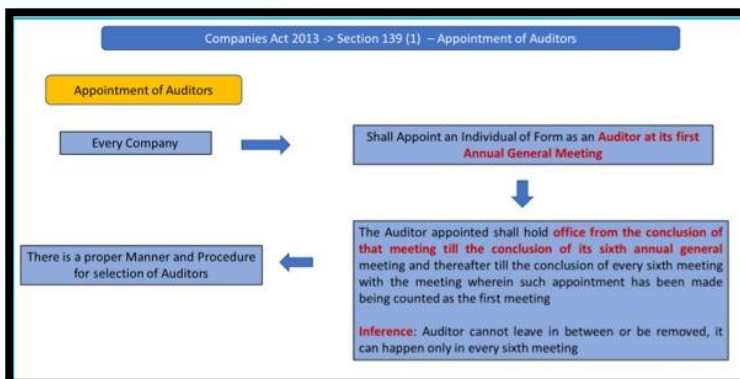
1. **Cooling off Period** - A break in the term for a *continuous period of five years* shall be considered as fulfilling the requirement of rotation

2. **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.**

3.2 Appointment of Auditors in Government companies

As mentioned above, the process of appointment of auditors is different in **Government and Non-government companies.** Till now we have discussed about Non-government Companies, under this section let us deal with Government Companies.

- Despite what is mentioned in Section 139 (1), (As described in the image)



In the case of a

1. Government company or
2. Any other Company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments or
3. Partly by the Central Government and partly by one or more State Governments

The process of appointment of auditors in these companies is discussed below.

Who appoints the auditor in government Companies?

The Comptroller and Auditor-General of India shall appoint an **auditor** within a period of **one hundred and eighty days** from the commencement of the financial year.

Tenure of Auditor

The auditor shall hold office till the **conclusion of the annual general meeting.**

Question	Answer
Who appoints Auditor In government companies	The Comptroller and Auditor-General of India
When is Auditor appointed?	Within a period of 180 days from the commencement of the financial year.
Tenure of Auditor	From the day of appointment till the conclusion of the first annual general meeting.

3.2.1 Appointment of first auditor in Government Companies

1. **The first auditor** shall be appointed by the Comptroller and Auditor-General of India **within sixty days** from the date of registration of the company
2. In case the **Comptroller and Auditor-General of India** does not appoint such auditor within the said period, the Board of Directors of the company shall appoint such auditor **within the next thirty days**
3. In the case of failure of the Board to appoint such auditor within the next thirty days, it shall inform **the members of the company** who shall appoint such auditor **within the sixty days at an extraordinary general meeting, who shall hold office till the conclusion of the first annual general meeting.**

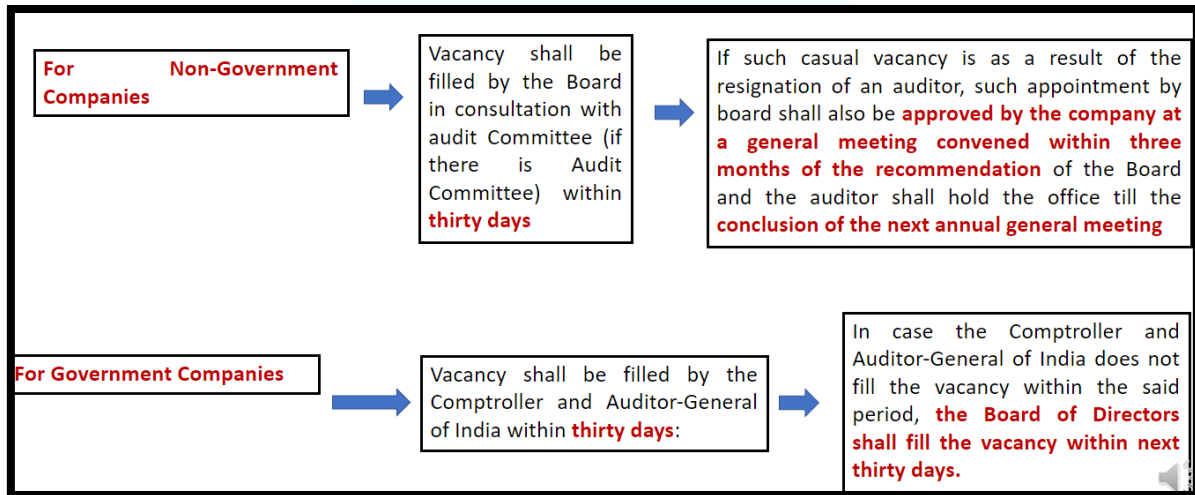


Note: Remember the appointment of first auditor of the Government company as **60-30-60 Rule**.

3.3 Casual Vacancy of Auditor

Casual Vacancy of the Auditor means a vacancy caused due to death, resignation, and disqualification.

Who shall appoint the auditor in case of casual vacancy?



The above image answers the questions such as **who appoints the auditors** and **the procedure to appoint them**.

Concept Check

Q. What is the minimum number of people with which company can be formed?

- A. 2
- B. 1
- C. 3
- D. 4
- E. 8

Answer: Option B

4 Section 140 - Removal, Resignation of Auditor and Giving of Special Notice

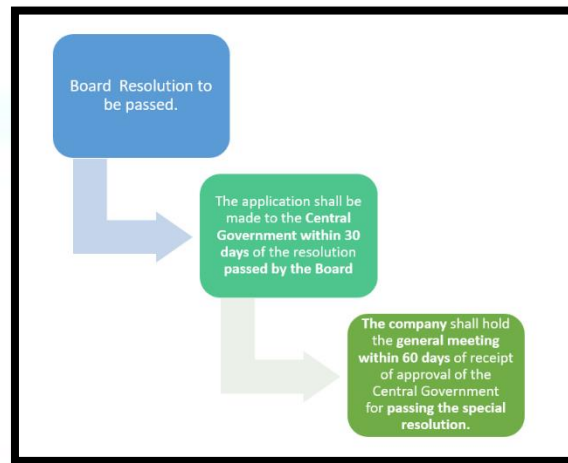
Having discussed the appointment of auditors, auditors can be removed or resign as auditor before the expiry of their term. First let us discuss the removal of auditor in the subsequent section.

4.1 Removal of Auditor

The auditor appointed for the company (government or non-government company) may be removed from his office before the expiry of his term **only by a special resolution of the company**, after obtaining the **previous approval of the Central Government** in the prescribed manner.

Prescribed Manner to Remove the Auditor as per Rules

1. The application to the **Central Government** for removal of auditor shall be made **within thirty days of the resolution** passed by the Board.
2. The company shall hold the general meeting **within sixty days** of receipt of approval of the Central Government for passing **the special resolution**.



4.2 Resignation of Auditor

- In case of Government Companies and Non-Government Companies** - The auditor who has resigned from the company shall file within a **period of thirty days** from the **date of resignation**, a statement with the company and the Registrar **indicating the reasons and other facts related to his resignation**.
- In case of Government Companies** - In case of government company, **the auditor shall additionally also file a statement** within a **period of thirty days** from the date of resignation with the **Comptroller and Auditor-General of India**, indicating the reasons and other facts related to his resignation.

Type of Firms	File a statement	Time Period
Non-Government Companies	With Company + Registrar	Within 30 Days from the date of resignation file a statement.
Government Companies	With Company + Registrar + CAG (Comptroller and Auditor-General of India)	Within 30 Days from the date of resignation file a statement.

What is the penalty for auditor for non-compliance for above provisions?

- If the auditor does not comply with the above provisions, he or it shall be liable to a **penalty of fifty thousand rupees** or an amount **equal to the remuneration of the auditor, whichever is less**
- In case of continuing failure, an additional **penalty of five hundred rupees** for each day of violation during which such failure continues, subject to a **maximum of 2 lakh rupees**.

4.3 Removal on Orders by Tribunal

In the above section, we have seen the removal of auditor by the company. In this section we shall discuss the removal of auditor on order by tribunal. This is a special case.

Tribunal can act on application by Any Person or Central Government

- Application to tribunal by any person** - Tribunal on application made to it by **any person** concerned finds out that auditor of a company has acted in a fraudulent manner then it can direct the company to change its auditors.

2. **Application to tribunal by Central government** - Tribunal on receiving application by the Central Government against the auditor finds out that auditor has acted in fraudulent manner and feels that the change of the auditor is required **then within fifteen days of receipt of such application** it shall make an order that auditor shall not function as an auditor anymore and the Central Government may appoint another auditor in his place.
3. **Auditor not eligible for reappointment** - The auditor, **whether individual or firm**, against whom final order has been passed by the Tribunal shall not be eligible to be appointed as an auditor of any company for a **period of five years from the date of passing of the order**.

5 Section 141 - Eligibility, qualifications, and disqualifications of auditors. —

A person with only certain bare minimum qualifications can become an auditor. The eligibility criteria is specified by the Companies Act, 2013.

5.1 Eligibility of Auditor

- **Individual** - A person shall be eligible for appointment as an auditor of a company **only if he is a chartered accountant**.
- **Firm** - A firm whereof majority of partners practicing in India are chartered Accountants may be appointed by **its firm name to be the auditor of a company**.

Entity	Eligibility for Auditor
Individual as an Auditor	only if he is a Chartered Accountant .
Firm as an auditor	A firm where the majority of partners practicing in India are Chartered Accountants may be appointed by its firm name to be the auditor of a company.

- **Example:** In a firm of five people, two of them are not Chartered accountant (CA), three are chartered accountant (CA), then such a firm can be appointed as an Auditor **as majority of partners are CA**.
- When a firm 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**.

5.2 Qualification and Disqualification of Auditor

Qualification : Following shall not be appointed as auditors

1. An officer or employee of the company or anyone who is further employee of any officer or employee of company
2. A person who is partner in the company
3. A person or a firm who has business relationship with the company
4. A person who's relative is director or key management personnel in the company
5. A person who in full time employment in some other company
6. IF person or partner of firm is already holding appointment of more than twenty companies (**These twenty companies shall not include one person companies, small companies and private companies having paid-up share capital less than one hundred crore rupee**)
7. A person convicted by court for a fraud or any other offence **till 10 years from date of conviction**
8. 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.
9. A person who himself or his relative or partner is (**holding securities of more than 1 lakh**) or (**Indebted/Owes more than 5 lakh to the company**) or (**has given a guarantee of more than 1 lakh** for a third person who owes money to the company or its subsidiary)

The above image depicts the persons who shall not be appointed as auditors.

5.3 Disqualification

When will casual vacancy occur?

If a person appointed as an auditor of a company incurs **any of the disqualifications mentioned above after his appointment**, then he shall vacate his office as such auditor and such vacation shall be deemed to be a **casual vacancy** in the office of the auditor.

6 Section 142 - Remuneration of auditors.

1. **Remuneration of First Auditor** - For the first Auditor appointed by the Board, **the remuneration shall be fixed by the Board.**
2. **Remuneration of Auditors appointed in AGM-** The remuneration for auditors appointed in **Annual General Meeting** may be fixed in **the general meeting**

The remuneration to the auditor shall be in addition to the fee payable to an auditor or expenses to be reimbursed to the auditor.

7 Section 143 - Powers and duties of auditors and auditing standards.

7.1 Power of auditor

1. **Right of Access** - Auditor would always have a right of access to the books of account and vouchers of the company and **to inquire into following matters**
 - a. Company has taken securities against loans given to various entities
 - b. All the transactions are done in the interest of the company
 - c. All the accounting is being done as per accounting standards
2. **Access to subsidiary and associate companies-** The auditor of a company which is a holding company shall also have the right of access to the records of all subsidiaries and associate companies wherever it is required for consolidation of Annual Statements.

7.2 Duties of Auditor

The duties of auditor are described below.

1. The auditor shall present a **report in the general meeting with respect to the financial statements of the company** that he has examined the financial statements and they represent **true and fair picture of the company**
2. The auditor report shall also mention
 - I. whether, in his opinion, the financial statements comply with the accounting standards
 - II. whether any director is disqualified from being appointed as a director
 - III. any qualification, reservation or adverse remark relating to the maintenance of accounts
 - IV. whether the company has adequate internal financial controls in place to mitigate risk (**Exception: This point is not valid (Auditor need not include this in report) for a private company which is**
 - i. which is a one-person company or a small company or
 - ii. which has **turnover < than rupees fifty crores** as per latest audited financial statement **and** which has **aggregate borrowings from banks or financial institutions < than 25 crores**
 - V. whether the company has disclosed the impact, if any, of pending litigations on the financial Position of company
 - VI. Whether Company has made provision for any foreseeable losses in future
 - VII. whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

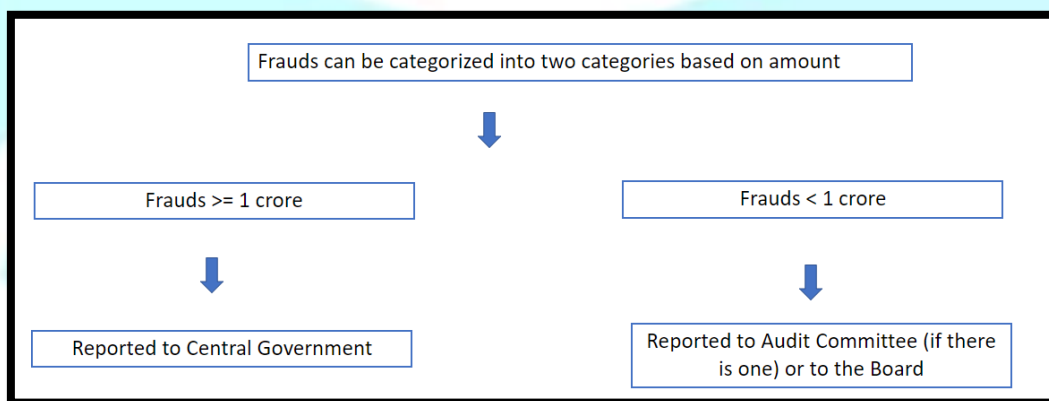
7.3 Auditing Standards

Every auditor shall comply with the auditing standards.

Who makes auditing Standards?

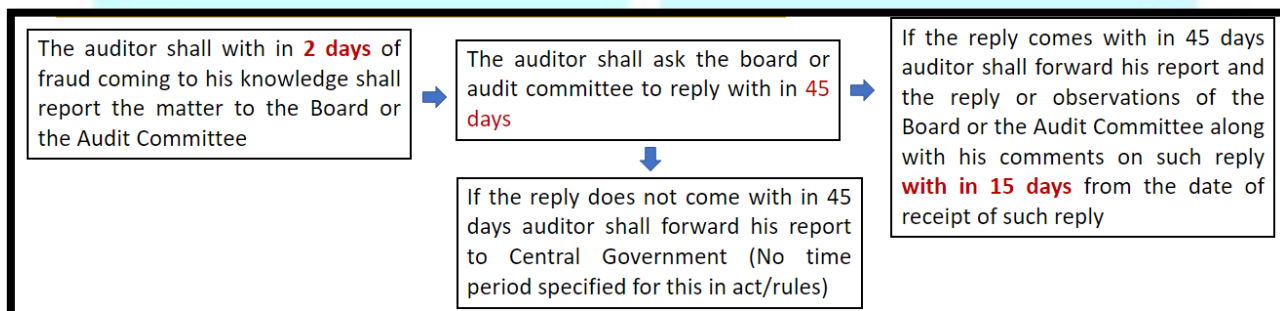
- The **Central Government** may prescribe the standards of auditing, as recommended by the **Institute of Chartered Accountants of India**, in consultation with **National Financial Reporting Authority**.
- The auditing standards notified by Central government may be notified after certain modifications in the standards recommended by ICAI.
- If the central government has not prescribed any auditing standards, then **auditing standards stated by ICAI will have to be complied by the Companies**.

7.4 Duties of Auditor – Reporting Frauds



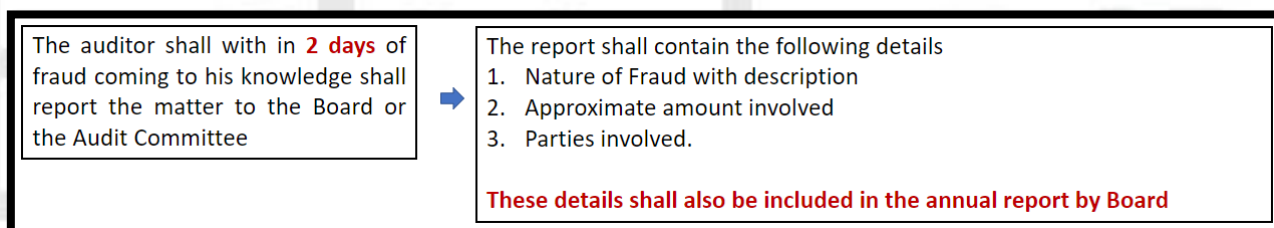
1. The reporting fraud is >= than 1 crore in the company by its officers or employees

Timeline/Format for sending report to Central government is shown below.



2. Reporting Frauds < 1 Crore in the company by its officers or employees

Timeline/Format for sending report to Board or the audit Committee



What is the Penalties for not Reporting Frauds?

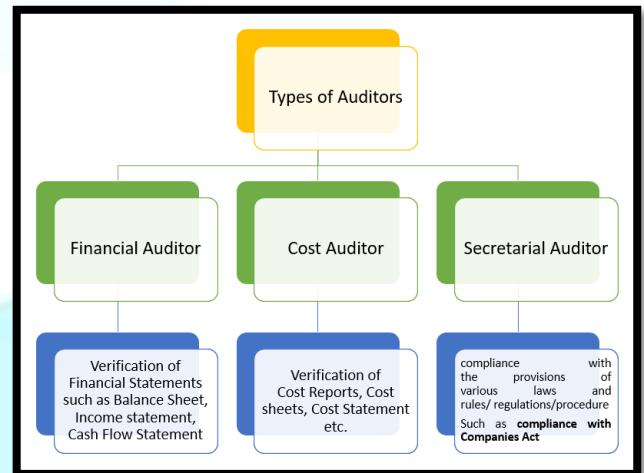
If the above frauds are not reported, then penalty is as follows

1. In case of Listed Company – 5 lakh rupees
2. Other Company – 1 lakh

7.5 Power and Duties of Financial Auditor Applies to Cost Auditor and Secretarial Auditor

The different types of auditors and their main functions are discussed below.

Till now in this chapter, we meant **Financial Auditor by the word Auditor**. All the provisions and rules discussed in **section 143** also applies to **Cost Auditor and Secretarial Auditor**.



8 Section 144 - Auditor not to render certain services

Auditor shall provide services as are approved by the **Board of Directors or the audit committee**

Auditors **shall not** provide the following services **directly or indirectly** to the company or **its holding company or subsidiary company**

1. Accounting and bookkeeping services
2. Internal audit.
3. Design and implementation of any financial information system.
4. Actuarial services.
5. Investment advisory services, investment banking services and financial services.
6. Management service

9 Section 145 - Auditor to sign audit reports, etc.

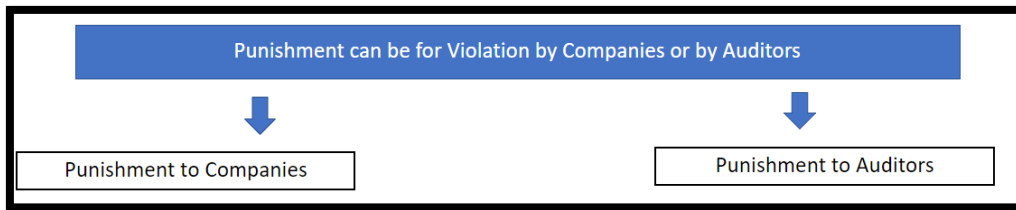
1. **Sign Audit report** - The person appointed as an auditor of the company shall sign the auditor's report.
2. **Observations or comments on financial transactions** which have any adverse effect on the functioning of the company mentioned in the auditor's report **shall be read before the company** in a general meeting and shall be open to inspection by any member of the company

10 Section 146 - Auditors to attend general meeting

All notices related to **any general meeting** shall be **forwarded to the auditor of the company**

1. **Attend all general meeting** - The auditor shall **(unless otherwise exempted by the company)** attend **all general meeting**. If auditor is not able to attend the meeting, then he shall send his authorized representative and that authorized representative shall also be qualified to be an auditor.
2. **Right to be heard** - In general meeting auditor shall have the right to be heard or put across his view on any part of the business which concerns him as the auditor.

11 Section 147 - Punishment for contravention



11.1 What is the Punishment to Companies?

1. **Fine** - The company shall be punishable with fine of **minimum of twenty-five thousand rupees**, but which may be **extended to five lakh rupees**
2. **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
3. If the directors of the company have acted in a fraudulent manner or colluded in any fraud, then the **criminal or civil liability** in such a case shall be of both the firm and the directors

11.2 What is the Punishment to Auditors?

Violation of any of provision of the following sections by auditor Section 139 - Appointment of Auditors Section 144 – Auditor not to render certain services Section 145 – Auditor to Sign Audit Reports, etc.	→	If the violation is just due to lax attitude but is not intended to willfully deceive the company and its shareholders, then auditor shall be punishable with fine 1. Minimum - twenty-five thousand rupees 2. Maximum - Five lakh rupees or four times the remuneration of the auditor, whichever is less
		If the violation is intended to willfully deceive the company and its shareholders, then auditor shall be punishable with 1. Imprisonment for a term up to one year And 2. Fine I. Minimum - Fifty thousand rupees II. Maximum - Twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less

If the **auditor** has been punished either due to lax attitude or for **willfully deceiving the company and its shareholders**, then **additionally he is liable to do the following also**

1. He shall **refund the remuneration** received by him to the company
2. **Pay for damages** for loss arising out of **incorrect or misleading statements made in his audit report**.
3. **The Central Government shall specify any authority or an officer** for ensuring prompt payment of damages by the auditor

12 Section 148 - Central Government to specify audit of items of cost in respect of certain companies

12.1 Who shall specify Audit of Items of Cost in Respect of Certain Companies?

Central Government to Specify Audit of Items of Cost in Respect of Certain Companies.

12.2 What are the items for which cost data needs to be maintained?

Central Government may direct companies (having an **overall turnover \geq 35 crores** from all its products and services the immediately preceding financial year) that **Cost data for specific items** related to the **utilization of material or labor** shall also be included in the books of account.

- The **products** for which cost data needs to be maintained is mentioned below.

Specific Items for which cost data needs to be maintained

1. **Category A** -> Regulated Sectors such as Telecom, Pharma, Petroleum, Fertilizers, sugar
2. **Category B** -> Non-Regulated Sectors such as Machinery, Turbo jets, Steel, Coffee, Tea, Minerals, Rubber, Roads and Railways, Radars, Tanks, Arms and Ammunitions, Paper, Tyres, Milk Power, Glass etc.

12.3 What is the criteria for Cost Audit?

Cost audit is different from **cost data** that needs to be maintained. Central government may direct for cost audit to be done in companies mentioned below.

The central government can also direct for **cost audit** of companies meeting below requirements shall be conducted

1. For the items **under Category A** need to conduct cost audit if
 - I. The **overall annual turnover** of the company from all its products and services during the **immediately preceding financial year is ≥ 50 crore** **And**
 - II. The **aggregate turnover** of the individual product or products or services for which cost records are required to be maintained **is ≥ 25 crore**.
2. For the items **under category B**, need to conduct cost audit if
 - I. The **overall annual turnover** of the company from all its products and services during the **immediately preceding financial year is ≥ 100 crore** **And**
 - II. The **aggregate turnover** of the individual product or products or service or services for which cost records are required to be maintained **is ≥ 35 crore**.

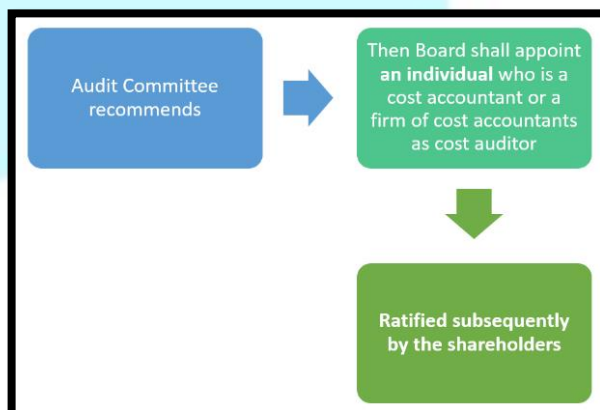
12.4 Who Shall Conduct Cost Audit?

The audit shall be conducted by a **Cost Accountant**.

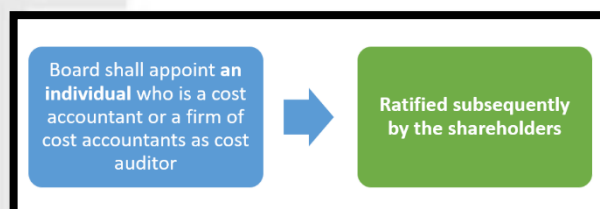
12.5 Process of appointment of Cost Accountant.

1. In the case of companies which are required to constitute an audit committee-

- The Board shall appoint **an individual** who is a cost accountant or a firm of cost accountants as cost auditor on the recommendations of the Audit committee
- **The Audit committee** shall also recommend the remuneration of the cost auditor and same shall be considered and **approved by the Board of Directors** and **ratified subsequently by the shareholders**.



2. 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 as cost auditor and the remuneration of such cost auditor shall be ratified by **shareholders subsequently**.

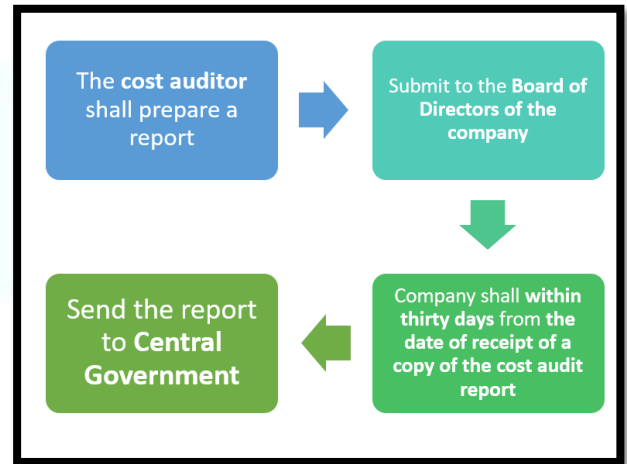


3. No Person appointed as **Financial Auditor of the company** shall be appointed for conducting the audit of cost records.

4. Auditor conducting the cost audit shall **comply with the cost auditing standards** which are specified by the **Institute of Cost Accountants of India**.

Submission of Cost Audit to Central Government

1. The cost auditor shall prepare a report and submit to the **Board of Directors of the company**.
2. Company shall **within thirty days from the date of receipt of a copy of the cost audit report** should send the report to **Central Government**.
3. **Central Government** feels some additional information is required then it can ask the company to provide the same within such time as may be specified by that Government.



Concept Check

Q. If the Tribunal passes an order to change the auditor of the company because of auditor acting in fraudulent manner, then auditor shall not be eligible to be appointed as an auditor of any company for a period of _____ years

- A. 5
- B. 2
- C. 10
- D. 15
- E. 8

Answer: Option A

EduTap