

- **Quick and Inexpensive:** Faster and cheaper than litigation.

18. Mediation & Conciliation Under Companies (Mediation and Conciliation) Rules, 2016

- **Panel of Experts:** The Central Government maintains a panel of mediators and conciliators for dispute resolution.
- **Qualifications for Mediators:** A person must have 15 years of continuous practice as a professional (Chartered Accountant, Company Secretary, etc.).

19. Ethics and Conduct of Mediators/Conciliators (Rule 28)

- **Ethical Guidelines:** Mediators must act impartially, ensuring fairness and confidentiality.
- **Consequences of Non-Attendance:** Non-attendance of parties leads to termination of mediation or conciliation.

20. Settlement Agreement (Rule 25)

- **Procedure:** If a settlement is reached, it must be documented and signed by the parties and their counsels.

This summary covers compounding provisions under FEMA, mediation, and conciliation processes, along with specific case studies and key points from the Companies Act.

Ch-8

Introduction to Audit and Corporate Governance Audit

Audit Overview

- **Definition:** Audit is an independent, systematic examination of an organization's financial statements, books, records, documents, and vouchers to ensure they provide a true and fair view.
- **Purpose:** It offers assurance to management and stakeholders on the company's financial health and compliance.
- **Legal Framework:**
 - Sections 139 to 147 of the Companies Act, 2013
 - **Audit Rules, 2014**
 - Applies to statutory, cost, internal, and secretarial audits.

Types of Audits

- **Financial Audit:** Includes Statutory Audit, Cost Audit, Internal Audit.
- **Compliance Audit:** Includes Secretarial Audit, CSR Audit, Corporate Governance Audit, and other specialized audits (e.g., Insider Trading, Cyber, Social, Forensic, Environmental).

Corporate Governance Audit (CGA)

Definition and Importance

- **Corporate Governance** ensures transparency, accountability, and ethical management of business practices.
- **Need for CGA:** Ensures the implementation of corporate governance principles, helping to avoid financial scandals and enhance stakeholder trust.

Provisions and Legal Framework

- Governed under the **Companies Act, 2013** and **SEBI (LODR) Regulations, 2015**.

- **Clause 49** (previously under Listing Agreement) and **Schedule II** of LODR Regulations guide corporate governance audits for listed companies.
- **Objective:** To evaluate the effectiveness of governance practices and ensure transparency, integrity, and accountability.

Need for Corporate Governance Audit (CGA)

- **Monitoring Mechanism:** It ensures that management is accountable to the board and stakeholders, which improves market valuation and capital inflow.
- **Benefits:**
 - Improves company valuation.
 - Increases capital flows (domestic & global).
 - Enhances transparency, benefiting customers and investors.

Scope of Corporate Governance Audit

1. **Financial & Non-financial Disclosures:** Ensure transparency in reporting.
2. **Stakeholder Rights:** Check fairness in stakeholder treatment.
3. **Board of Directors:** Analyze composition, independence, and role of directors.
4. **Control Environment:** Audit accounting, internal/external audits, and risk management.
5. **Transparency in Financials:** Review the accuracy and fairness of disclosures.
6. **Executive Compensation:** Ensure fair compensation practices.

Role of Audit Committee in Corporate Governance

- **Mandate:** According to **Section 177** of the Companies Act, 2013 and **LODR Regulations, 2015**, listed companies must form an Audit Committee.
 - **Composition:** Minimum of 3 directors, with majority being **Independent Directors (IDs)**.
 - **Responsibilities:**
 - Oversee the financial reporting process.
 - Approve auditor appointments and remuneration.
 - Review financial statements and audit reports.
 - Monitor risk management systems.
 - Evaluate internal controls and audit effectiveness.

Audit Committee Requirements under LODR Regulations

- **Independent Directors:** Two-thirds must be IDs.
- **Financial Literacy:** All members must be financially literate; at least one should have accounting expertise.
- **Chairperson:** Must be an independent director and present at AGM to answer shareholder queries.
- **Role in Corporate Governance:**
 - Oversee the financial reporting process.
 - Recommend appointments and remunerations of auditors.
 - Review quarterly and annual financial statements.
 - Monitor risk management and internal controls.

Illustrative Checklist for Auditing Corporate Governance Systems

Accountability

- **Separation of Ownership & Control.**
- **Board Accountability:** Ensure management is accountable to the board and board is accountable to shareholders.
- **Meetings:** Sufficient number of meetings held for healthy discussions.

Fairness

- **Shareholder Treatment:** Ensure minority shareholders' rights are protected.
- **Resolutions:** Check defined procedures for resolution of violations.

Transparency

- **Disclosure:** Timely and accurate disclosure of financial and non-financial information.
- **Insider Trading:** Ensure compliance with insider trading regulations.

Responsibility

- **Board's Role:** Ensure review of corporate strategy, performance, and risk policy.

Shareholder Interests

- **Rights:** Shareholders should have the right to participate in major decisions.
- **Capital Structures:** Ensure equitable disclosure and practices in capital structure.

Audit Report and Compliance Certificate

- **Compliance Certificate:** Issued by **Practicing Company Secretaries** or **Auditors** regarding adherence to corporate governance practices.
- **Annexed with Director's Report:** The certificate outlines the compliance status and provides recommendations for improvements.

This framework ensures comprehensive auditing of corporate governance activities, aligning company practices with ethical, transparent, and accountable standards.

Corporate Governance Due Diligence - Coverage

1. Board Independence & Governance

- **Board Composition:**
 - Is the chairperson executive or non-executive?
 - If the chairperson is executive, does 50%+ of the board consist of independent directors?
 - If non-executive chairperson is a promoter or related to a promoter, does the board consist of 50%+ independent directors?
 - If non-executive chairperson is not a promoter or related, does the board consist of 1/3rd independent directors?
- **Proportion of Independent Directors:** Percentage of independent directors on the board.
- **Gender Diversity:** At least one woman director on the board.
- **Top 1000 Listed Entities:** At least one independent woman director.
- **Board Size:** Minimum of six directors for top 2000 listed entities.
- **Lead Independent Director:** If chairperson and CEO roles are not separated.
- **Induction Policy:** Written procedure for inducting independent directors.

- **Nominations Disclosure:** Disclosures regarding the basis of independent director nominations.
- **Independent Directors' Appointment Letter:** Existence of formal appointment letters.
- **Tenure of Independent Directors:** Any specified maximum tenure.
- **Independent Directors' Meetings:** Details on separate meetings of independent directors.
- **Orientation/Training:** Details of orientation programs for directors.
- **D&O Insurance:** Details on Directors and Officers insurance provided.
- **Resignation/Appointment Gap:** Time between resignation and new appointment of independent directors.
- **Affirmative Statement:** Annual and appointment-specific statements from independent directors confirming their independence.

2. Board Systems and Procedures

- **Agenda Circulation:** Process for circulation of board meeting agendas.
- **Board Meeting Details:** Frequency and structure of board meetings.
- **Attendance:** Record of board meeting attendance.
- **Video Conferencing:** Usage of video conferencing for board meetings.
- **Applicable Laws:** List of relevant laws maintained by the company.
- **Compliance Certificates:** Information/certificates on statutory compliances presented to the board.
- **Communication of Decisions:** Process for communicating board decisions to departments.
- **Code of Conduct:** Written code of conduct for directors, senior management, and employees.
- **Succession Planning:** Policy on succession planning at senior management levels.
- **Action Taken Report:** Policy on tracking and reporting actions taken.
- **Board Effectiveness Review:** Policy for evaluating the effectiveness of the board.
- **Directors' Share Dealing:** Transparency on share dealings by directors and their relatives.

3. Board Committees

- **Committee Details:** Names, terms of reference, and meeting details for board committees.
- **Committee Chairperson:** Information on the chairperson of each board committee.
- **Independent Directors in Audit Committee:** Proportion of independent directors in the audit committee.
- **Audit Committee Risk Assessment:** Process for risk assessment by the audit committee.
- **Related Party Transactions:** Process for reviewing related party transactions by the audit committee.
- **Financial Experts in Audit Committee:** Presence of financial experts in the audit committee.
- **Audit Communication Mechanism:** Communication between internal auditor, audit committee, and CFO.
- **Auditor Rotation:** Rotation of auditors or audit partners.
- **Investor Grievances:** Details of pending investor grievances.

4. Transparency and Disclosure Compliance

- **Annual Report Disclosures:**
 - Remuneration of board members.
 - Related party transactions.
 - Material cases pending against the company.
 - Directors' appointments.
 - CEO/CFO compliance under LODR regulations.
- **Insider Trading Disclosures:** Compliance with insider trading regulations.
- **Secretarial Standards Compliance:** Adherence to ICSI's Secretarial Standards.
- **Audit Reports:** Adverse remarks in audit, cost audit, or secretarial audit reports.
- **Director's Inter-relationship:** Disclosure of directors' relationships.
- **Corporate Disclosure Policy:** Existence of a formal corporate disclosure policy.

5. Consistent Shareholder Value Enhancement

- **Growth in Net Worth:** Increase in shareholder value over time.
- **Dividend History:** Details of dividend payments and policies.
- **Dividend Policy:** Existence of a formal dividend policy.
- **Earnings Per Share (EPS):** Review of EPS growth.
- **Public Shareholding:** Details of public shareholdings.
- **Investor Satisfaction Survey:** If any surveys are conducted to gauge investor satisfaction.

6. Other Stakeholders' Value Enhancement

- **Vendor/Supplier/Customer Satisfaction:** Results of satisfaction surveys.
- **Personnel Policies:** Policies on employee engagement and participation.
- **Employee Stock Ownership Plan (ESOP):** Policy on ESOPs.
- **Prevention of Sexual Harassment:** Policy in place.
- **Vendor Development:** Policy on vendor development.

7. Corporate Social Responsibility (CSR)

- **CSR Policy:** Existence of a CSR policy.
- **CSR Report:** Availability of a CSR/Sustainability report.
- **Energy Conservation:** Initiatives for energy efficiency.
- **Water/Waste Management:** Sustainable water use and waste management practices.
- **CSR Budget:** Allocation of budget for CSR activities.

This framework for **Corporate Governance Due Diligence** ensures a comprehensive review of a company's governance structures, policies, and practices, ensuring that they are aligned with best practices, legal requirements, and stakeholder expectations.

Secretarial Audit and Internal Audit Overview

1. Secretarial Audit

Definition and Importance:

- **Secretarial Audit:** An independent audit of the non-financial aspects of a company, ensuring compliance with laws, regulations, and internal procedures.
- **Purpose:** Ensures compliance with laws under the Companies Act, Securities laws, FEMA, and industry-specific regulations, while promoting good governance practices.
- **Scope:** Focuses on verifying compliance with legal and procedural requirements, examining the governance structure, and assessing internal processes and systems.

Applicability of Secretarial Audit:

- **Section 204(1):** Applies to listed companies and other companies as prescribed.
 - **Companies requiring Secretarial Audit:**
 - Public companies with **paid-up capital of ₹50 crores or more.**
 - Public companies with **turnover of ₹250 crores or more.**
 - Companies with **outstanding loans or borrowings** of ₹100 crores or more.
- **SEBI LODR Regulations (Regulation 24A):** Mandatory for listed entities and material unlisted subsidiaries.
 - **Form MR-3** for compliance under both Companies Act and SEBI regulations.
 - Secretarial Audit includes verifying compliance with **SEBI regulations** and ensuring smooth functioning of the corporate governance mechanism.

Purpose of Secretarial Audit:

- Verifies compliance with legal frameworks such as **Companies Act, SEBI regulations, Secretarial Standards**, etc.
- Helps in detecting non-compliance early and facilitates corrective actions.
- Builds a strong governance framework, preventing penalties and enhancing market reputation.

Benefits:

- **Governance Foundation:** Effective compliance programs promote good governance.
- **Risk Mitigation:** Helps reduce the risk of penalties, fraud, and operational inefficiencies.
- **Employee and Customer Loyalty:** Ethical practices lead to increased stakeholder trust.
- **Market Capitalization:** Strong governance frameworks improve shareholder returns.

2. Internal Audit

Definition and Role:

- **Internal Audit:** An independent, objective assurance and consulting activity designed to add value and improve operations by assessing internal controls, risk management, and governance processes.
- **Goal:** Helps organizations achieve their objectives by ensuring the effectiveness of risk management, control, and governance processes.

Scope of Internal Audit:

- **Financial Control Systems:** Reviewing financial management practices and ensuring reliability in financial reporting.
- **Operational Areas:** Assessing efficiencies and identifying opportunities for improvement.
- **Compliance:** Ensuring adherence to company policies, regulations, and applicable laws.

- **Risk Management:** Facilitating risk identification, evaluation, and mitigation strategies.

Core Areas of Contribution:

1. **Independent Review:** Appraises control systems across financial and operational functions.
2. **Compliance Check:** Ensures policies and regulations are followed.
3. **Risk Management:** Assesses the organization's approach to risk, recommending improvements.
4. **Fraud Prevention:** Detects inefficiencies, fraud risks, and waste, ensuring company assets are safeguarded.

Legal Framework for Internal Audit:

- **Section 138 of the Companies Act, 2013:** Specifies companies required to appoint an internal auditor.
 - **Criteria:**
 - Listed companies.
 - Public companies with **paid-up capital \geq ₹50 crores or turnover \geq ₹200 crores.**
 - Companies with **outstanding loans \geq ₹100 crores.**
- **Rule 13 of Companies (Accounts) Rules, 2014:** Expands the requirement for **internal audits** in specific companies.

Qualifications for Internal Auditors:

- Chartered Accountants, Cost Accountants, or **Company Secretaries.**
- Internal auditors should possess a deep understanding of the company's operations, culture, systems, and governance structure.

Key Points of Internal Audit and Secretarial Audit

- **Secretarial Audit** focuses on ensuring compliance with **legal frameworks** and improving corporate governance, ensuring the company follows all rules and regulations in its operations.
- **Internal Audit** reviews **internal controls, risk management, and operational efficiency** to help the company achieve its goals and improve its processes.
- Both audits aim to strengthen **transparency, compliance, and corporate governance**, ensuring a fair, ethical, and efficient corporate environment.

These audits not only enhance business efficiency but also mitigate **legal, operational, and financial risks**, adding significant value to the company.

Corporate Social Responsibility (CSR) Audit Overview

1. CSR Overview

Definition:

- **Corporate Social Responsibility (CSR)** is the commitment by businesses to contribute positively to society, focusing on environmental sustainability, social welfare, and ethical business practices.
- **Purpose:** CSR ensures that businesses go beyond profit-making, engaging in activities that contribute to the betterment of communities and the environment.

Legal Framework:

- **Companies Act, 2013 - Section 135:** CSR is mandatory for companies meeting certain criteria based on **net worth, turnover, or net profit.**
- Companies meeting any of the following thresholds must comply with CSR regulations:
 - **Net worth \geq ₹500 crores.**
 - **Turnover \geq ₹1000 crores.**
 - **Net profit \geq ₹5 crores.**

2. CSR Committees and Policies

CSR Committee Requirements:

- Minimum **three directors** with at least **one independent director.**
- **Policy Adoption:** Companies must adopt a CSR policy that aligns with the provisions of the Companies Act, 2013.
- **Spending Requirement:** Companies are required to spend at least **2% of their average net profit** over the past three financial years on CSR activities.

Key CSR Activities (Schedule VII of the Companies Act, 2013):

- Eradicating hunger and promoting healthcare.
- Education, special education, and vocational skills.
- Gender equality, women empowerment, and social welfare.
- Environmental sustainability, protection of flora, fauna, and conservation.
- Promotion of national heritage and arts.
- Armed forces and veterans' welfare.

3. Objective of CSR Audit

Primary Goals:

- To **ensure compliance** with the Companies Act, 2013, and CSR regulations.
- To **monitor the implementation** of CSR policies and activities.
- To **evaluate internal controls** and governance structures in CSR programs.
- To **assess the project lifecycle** and the use of allocated budgets for CSR activities.

4. Methodology of CSR Audit

Key Steps in CSR Audit:

1. **Review CSR Policy:** Examine CSR strategy, governance structure, and ongoing projects.
2. **Stakeholder Interaction:** Interview beneficiaries, project teams, and management.
3. **Compliance Checks:** Review the CSR expenditure, including project costs, overheads, and traceability.
4. **Impact Evaluation:** Assess the social impact of CSR initiatives on communities.

5. CSR Audit Coverage

The CSR audit covers various aspects of the company's CSR strategy, including:

- **Human Rights:** Compliance with international human rights standards.
- **Community Development:** Social welfare and development projects.
- **Environmental Impact:** Efforts related to sustainability and ecological balance.
- **Employee Welfare:** Ensuring a safe, non-discriminatory work environment.

6. Takeover Audit

Definition:

- A **Takeover Audit** ensures compliance with the **SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011** and the **Companies Act, 2013**, focusing on timely disclosures, pricing, open offers, and the regulatory compliance during the takeover process.

Key Areas Covered:

1. **Identification & Categorization:** Identify the acquirer, promoter, PAC (Persons Acting in Concert), and related parties.
2. **Disclosure Compliance:** Ensure timely disclosures relating to share acquisitions, transfers, and encumbrances.
3. **Monitoring:** Track promoter holdings and action on regulatory requirements.
4. **Open Offer:** Ensure timely intimation to stock exchanges and compliance with SEBI regulations.

Types of Takeover Audit:

- **Pre-Acquisition Audit:** Ensures compliance before the acquisition takes place.
- **Post-Acquisition Audit:** Ensures the post-acquisition processes comply with SEBI regulations and legal frameworks.

7. Penalties for Violation of SEBI (SAST) Regulations

Failure to Comply with the SEBI (SAST) Regulations, 2011 can lead to severe penalties, including:

- **Divestment of Shares:** Directing the acquirer to divest shares acquired in violation.
- **Transfer Restrictions:** Prohibiting transfers or voting rights of shares.
- **Public Disclosure:** Compelling the acquirer to make open offers or face interest payments for delays.
- **Regulatory Sanctions:** Imposing fines, banning access to capital markets, or requiring divestment to ensure compliance with the permissible shareholding limit.

8. Key Takeaways for Companies

- **CSR Audit** ensures that a company's CSR activities align with legal requirements, thus maintaining **compliance** and fulfilling its social responsibilities.
- **Takeover Audits** safeguard the interests of investors by ensuring that all regulatory processes during business acquisitions are followed properly.
- Both **CSR** and **Takeover Audits** provide independent verification, enhance corporate transparency, and contribute to **good governance** practices.

These audits allow companies to evaluate their operations from both a **compliance** and a **governance** perspective, helping mitigate risks, optimize operations, and promote social responsibility and ethical practices.

Insider Trading Audit Overview

1. Insider Trading Compliance under SEBI (Prohibition of Insider Trading) Regulations, 2015

Regulatory Framework:

- The **SEBI (Prohibition of Insider Trading) Regulations, 2015** focus on preventing insider trading and ensuring fair disclosure of **unpublished price sensitive information (UPSI)**.

Key Compliance Requirements:

- **Initial Disclosures:** Promoters, key managerial personnel (KMP), and directors must disclose their trades.
- **Continual Disclosures:** If a trade exceeds ₹10 lakh in value in a calendar quarter, promoters, directors, and employees must notify the company, which will then inform the stock exchange within 2 trading days.

- **Trading Plans:** Individuals must submit pre-approved trading plans for any planned trades, and compliance officers must ensure adherence to these plans.
- **Pre-Clearance:** Trading in the company's securities must be pre-approved by a compliance officer.
- **Code of Conduct:** The company must have a code for dealing with UPSI, including protocols for fair disclosure.

2. Insider Trading Compliance Checklist

Key checkpoints to verify compliance with insider trading regulations:

1. **Compliance Officer Appointment:** The company must appoint a compliance officer responsible for overseeing insider trading regulations.
2. **Structured Digital Database:** A database should be maintained for UPSI, including the identities of persons sharing and receiving sensitive information. This data must be kept for at least 8 years.
3. **Code of Conduct:** The company must have a **code of practices and procedures** for fair disclosure and a separate internal code for dealing with securities.
4. **Trading Plan Submission:** The company must ensure that all trading plans comply with Regulation 5, and approval is monitored by the compliance officer.
5. **Disclosure of Trading:** KMPs and directors must disclose trades exceeding ₹10 lakh, and the company must notify the stock exchanges within 2 trading days.
6. **Disciplinary Actions:** The company's code of conduct should outline actions like wage freezes or suspensions for violations, including remitting any penalties to SEBI's Investor Protection Fund.
7. **Monitoring and Reporting:** The compliance officer reviews and reports on trading activities regularly to the board or audit committee.
8. **Protection for Whistleblowers:** The code should ensure protection against retaliation for employees reporting violations, regardless of whether the information is considered by SEBI.

Industrial and Labour Law Audit Overview

1. Labour Law Audit Scope

Purpose:

- **Industrial and Labour Law Audit** helps ensure compliance with relevant labour laws and regulations, detecting non-compliance, and mitigating potential risks.
- The audit aims to promote employee-employer relations and improve governance, ensuring the company follows legal obligations related to employment and industrial practices.

Scope:

- Compliance checks are performed for various **labour laws**, including central, state, and local regulations. Auditors review specific company practices related to **workforce management, employee rights, and working conditions**.

2. Illustrative Labour Law Compliance Checkpoints

The audit focuses on the following major labour legislations:

- **Factories Act, 1948:**
 - Ensure registration, licenses, and compliance with safety, welfare, and health provisions.

- Verify maintenance of registers (e.g., Muster Roll, Accident Registers, Half-Yearly Returns).
- **Industrial Disputes Act, 1947:**
 - Verify the constitution of the **Works Committee, Grievance Redressal and Dispute Resolution** processes.
 - Ensure compliance with retrenchment, notice periods, and compensation procedures.
- **Payment of Wages Act, 1936:**
 - Ensure timely payment of wages, compliance with deductions, and maintenance of records (e.g., Wage Register, Muster Roll).
- **Minimum Wages Act, 1948:**
 - Verify the payment of minimum wages, working hours, overtime compensation, and maintaining required records.
- **Employees' State Insurance Act, 1948:**
 - Confirm registration with ESI authorities, timely contribution payments, and benefit provisions for employees.
- **Employees' Provident Fund and Miscellaneous Provisions Act, 1952:**
 - Verify compliance with EPF contribution, record-keeping, and reporting to the Provident Fund Commissioner.
- **Payment of Bonus Act, 1965:**
 - Verify the computation and payment of bonuses to employees as per the applicable rules.
- **Maternity Benefit Act, 1961:**
 - Ensure compliance with maternity leave, pay, and other benefits for female employees.
- **Child and Adolescent Labour (Prohibition and Regulation) Act, 1986:**
 - Verify the employment of minors and ensure the prohibition of child labour.
- **Equal Remuneration Act, 1976:**
 - Verify equal remuneration practices for both men and women in similar roles.

3. Contract Labour Compliance

Key Regulations under the Contract Labour (Regulation and Abolition) Act, 1970:

- Ensure proper registration of contractors, maintenance of wage registers, and compliance with payment of wages and employee welfare measures.
- Verify adherence to conditions on payment of wages, leave, medical facilities, and ESI/EPF contributions for contract labour.

4. Additional Considerations for Labour Law Audits

- **Social Security Compliance:** Ensure compliance with social security schemes like **Employees' Provident Fund (EPF), Employees' State Insurance (ESI), and Maternity Benefits.**
- **Health & Safety:** Ensure adherence to safety regulations and welfare measures, including the provision of restrooms, medical care, and accident registers.
- **Dispute Management:** Verify the resolution of industrial disputes and compliance with notification requirements for layoffs, retrenchment, and shutdowns.

Conclusion

Both **Insider Trading Audits** and **Industrial and Labour Law Audits** are critical to maintaining transparent, ethical business practices. **Insider Trading Audits** ensure that a company complies with securities regulations, protecting shareholders and maintaining fairness in the market. **Labour Law Audits**, on the other hand, safeguard the rights of employees and ensure compliance with various labour regulations, fostering a fair and compliant working environment.

Cyber Audit Overview

Objective:

Cyber security audits assess the effectiveness of cybersecurity policies, identify and mitigate potential risks, and ensure protection of sensitive data, network security, and incident response mechanisms within an organization.

Key Areas Covered:

1. **Asset Management:** Ensures that all information technology assets (hardware, software, etc.) are tracked and secured.
2. **Awareness Training:** Verifies that employees are trained in recognizing security threats and following protocols.
3. **Data Security:** Evaluates measures to protect sensitive data, including encryption, and data loss prevention systems.
4. **Resource and Recovery Planning:** Ensures that the company is prepared for data breaches or system failures with effective backup and recovery plans.
5. **Communication:** Ensures that processes and protocols for communication during an incident are well defined.

Cybersecurity Audit Process:

1. **Management:** Involves assessing whether company management is aware of and actively managing cybersecurity risks, making informed decisions based on risk assessments.
2. **Risk Management:** Risk assessment processes evaluate how to minimize cyber risks and identify ways to address them effectively.
3. **Internal Audit:** Internal auditors assess the current cybersecurity controls, evaluate their effectiveness, and report to the board for any potential gaps or weaknesses.

Illustrative Checkpoints for Cybersecurity Audit

Personnel Security:

1. **ID Badges:** Ensures that employees wear ID badges with appropriate access levels.
2. **Background Checks:** Verifies that contractors undergo appropriate background checks before being granted access to systems.
3. **Access Cutoff:** Verifies that access to systems is immediately cut off when an employee or contractor leaves.

Physical Security:

1. **Access Controls:** Ensures policies exist to restrict unauthorized physical access to critical systems or facilities.
2. **Controlled Areas:** Verifies whether secure areas are protected by appropriate measures (locks, security officers, video surveillance).

Account and Password Management:

1. **Authentication:** Ensures that access to systems is granted only to authorized personnel.
2. **Password Policies:** Ensures that strong, secure passwords are enforced and that they are changed regularly.

Confidentiality of Data:

1. **Data Protection:** Verifies that sensitive data is properly protected through encryption or other methods.
2. **Retention and Disposal:** Ensures that data retention policies are followed, and proper disposal measures are in place for old data.

Compliance and Audit:

1. **Policy Review:** Verifies that security policies are regularly reviewed and updated.
2. **Disaster Plans:** Ensures that disaster recovery plans are in place and regularly tested for effectiveness.
3. **Audit Procedures:** Verifies whether audit processes are in place to ensure compliance with security policies and procedures.

Environmental Audit Overview

Objective:

An environmental audit evaluates how well an organization complies with environmental laws and regulations, ensuring that their operations minimize environmental risks and damage.

Types of Environmental Audits:

1. **Environmental Compliance Audits:** Focus on ensuring the organization complies with laws and regulations related to air and water pollution, waste management, and more.
2. **Environmental Management Systems Audits:** Focus on assessing the organization's commitment to sustainability through systematic approaches to managing its environmental impact.

Environmental Audit Process:

1. **Pre-Audit or Planning:** Involves gathering background information, defining the audit's scope, and forming the audit team.
2. **On-Site or Field Audit:** The auditor reviews operational practices, meets with key staff, and inspects facilities to ensure compliance with environmental laws.
3. **Post-Audit:** The auditor evaluates findings, prepares reports on environmental impact, and submits recommendations for improvements.

Illustrative Environmental Audit Checklist

Environmental Policy:

1. **Policy Documentation:** Verifies whether the company has a documented environmental policy based on significant environmental impacts.
2. **Commitments:** Ensures the policy includes commitments to pollution prevention, compliance with legislation, and continual improvement.

3. **Public Access:** Confirms that the environmental policy is accessible to both employees and the public.

Environmental Aspects:

1. **Identification of Aspects:** Ensures that the company has a procedure for identifying its significant environmental impacts, such as waste, water usage, and energy consumption.
2. **Monitoring and Reporting:** Ensures that environmental aspects are regularly reviewed and monitored, and that necessary corrective actions are taken.

Legal Compliance:

1. **Regulatory Requirements:** Verifies that the company identifies and complies with all applicable environmental regulations.
2. **Licenses and Permits:** Ensures that the company has obtained all necessary environmental permits (e.g., for waste disposal, air emissions).

Information Systems Audit Overview

Objective:

Information systems auditing is designed to evaluate whether an organization's IT systems safeguard assets, maintain data integrity, and use resources efficiently. This includes assessing the system's compliance with regulatory requirements and the effectiveness of its controls.

Key Areas of Information Systems Audit:

1. **System Architecture:** Reviewing the overall design of the IT system, including its infrastructure and dependencies on business processes.
2. **Access Control:** Assessing the mechanisms in place to limit access to sensitive data and applications.
3. **Security Controls:** Evaluating the system's security measures, including anti-malware, firewalls, and encryption protocols.
4. **Backup/Restore Procedures:** Ensuring that proper backup systems are in place to protect against data loss.

Systems Audit Checklist

Management Controls:

1. **Security Policies:** Ensures the company has robust security policies and that they are regularly updated to address emerging risks.
2. **Business Continuity:** Verifies that the company has business continuity plans in place, including disaster recovery strategies.

Operational Controls:

1. **Monitoring:** Ensures that physical and digital assets are regularly monitored to prevent unauthorized access or tampering.
2. **Environmental Controls:** Verifies that IT facilities have proper environmental controls, such as air-conditioning, power backups, and appropriate security measures.

Application Controls:

1. **Input/Output Controls:** Ensures that the systems manage and process data accurately, with proper controls in place for input, processing, and output of sensitive information.

Mandatory SEBI Audits:

1. **SEBI Annual System Audit** (CIR/CDMRD/DEICE/01/2015):
 - Ensures Business Continuity Plans (BCP) and Disaster Recovery (DR) systems are effective and can continue market operations in case of disruptions.
2. **SEBI System Audit for Stock Brokers and Trading Members** (SEBI/HO/CDMRD/DEICE/CIR/P/2016/70):
 - Ensures that stock brokers meet system audit frameworks for secure operations within commodity and securities exchanges.
3. **SEBI System Audit for Mutual Funds and AMCs** (SEBI/HO/IMD/DF2 CIR/P/2019/57):
 - Mandates that asset management companies undergo system audits to ensure operational integrity in tech-driven investment activities.
4. **Annual System Audit of Market Infrastructure Institutions (MII)** (SEBI/HO/MRD1/ICC1/CIR/P/2020/03):
 - Ensures MIIs comply with cybersecurity norms and operational integrity, including assessments of IT systems used for market operations.

Conclusion:

Cyber audits, environmental audits, and information systems audits are essential for safeguarding an organization's integrity, ensuring compliance with regulations, and managing operational and environmental risks effectively. These audits provide key insights into the effectiveness of an organization's processes, policies, and procedures, and help identify areas of improvement to enhance operational resilience.

Forensic Audit Overview

Definition:

A forensic audit involves the application of accounting, auditing, and investigative skills to detect fraud, embezzlement, and other financial crimes. The goal is to uncover evidence that can be used in court proceedings, making it a crucial tool in legal matters related to financial misconduct.

Phases of Forensic Audit:

1. **Investigation Services:**
 - The forensic auditor investigates financial records, identifies discrepancies, and uncovers fraudulent activities.
 - Focuses on identifying and addressing defects in accounts.
2. **Litigation Services:**
 - In cases where fraud is unresolved internally, forensic auditors support legal proceedings by providing consultation, assisting lawyers, and offering evidence in court.

Areas of Forensic Audit:

1. **Criminal Investigations:** Fraud, bribery, and corruption cases.

2. **Professional Negligence Cases:** Examining mismanagement or negligence in professional duties.
3. **Fraud Investigation & Risk/Control Reviews:** Investigating asset misappropriation, financial misstatements, etc.
4. **Arbitration & Settlement of Insurance Claims:** Assisting in resolving disputes and claims related to fraud.
5. **Dispute Settlement:** Legal disputes requiring expert financial evidence.

Purpose of Forensic Audit:

1. **Corruption:**
 - **Conflicts of Interest:** Identifying instances where an individual exploits their position for personal gain, such as approving fraudulent expenses.
 - **Bribery:** Investigating instances where money is exchanged to influence decisions.
 - **Extortion:** Identifying situations where individuals demand money or other benefits to make favorable decisions.
2. **Asset Misappropriation:**
 - The most common fraud, including theft, fake invoices, and misuse of company resources.
3. **Financial Statement Fraud:**
 - Fraudulent reporting to artificially inflate a company's performance, often driven by market pressure or management bonuses.

Procedure of Forensic Auditing Investigation:

1. **Accepting the Investigation:**
 - Forensic auditors assess the fraud and ensure they have the skills and expertise needed before accepting the case.
2. **Planning the Investigation:**
 - Auditors define the scope, objectives, and fraud symptoms, such as delayed financial submissions or unusual changes in accounts.
3. **Gathering Evidence:**
 - Use of analytical procedures, discussions, substantive techniques, and forensic data analysis (FDA) to gather evidence.
 - Methods like reconciliations, cash counts, and reviews of documentation are employed to identify fraudulent activity.
4. **Reporting:**
 - After gathering evidence, forensic auditors provide a report detailing findings, evidence, and conclusions on the fraud, along with recommendations to prevent recurrence.
5. **Court Proceedings:**
 - Forensic auditors assist in litigation by providing expert testimony in court to clarify the findings and legal implications.

Illustrative Checklist for Forensic Audit:

1. **Fraud Detection:**
 - Whether the fraud was perpetrated at the management level or employee level.
 - Identify the motive behind the fraud and the internal controls on cash transactions and invoice generation.
2. **Nature of Fraud:**
 - Whether it involves corruption, asset misappropriation, or financial misstatements.

- Check if the entries passed are correctly reflected in financial statements.
3. **Symptoms of Fraud:**
- Delays in tax filings, bank reconciliations, internal control lapses, and discrepancies in financial statements.

Fraud Triangle and Risk:

1. **Fraud Triangle:**

- **Pressure (Motive):** Financial or personal pressures leading to fraud.
- **Opportunity:** The ability to carry out fraud due to weak controls.
- **Rationalization:** Justifying dishonest actions, like "borrowing" company funds for personal use.

2. **Fraud Risk Assessment:**

- Identifying vulnerabilities within the organization and aligning procedures to mitigate risks.

Forensic Audit Report Structure:

1. **Executive Summary:** Overview of the audit and findings.
2. **Audit Objective:** Goals and purpose of the forensic audit.
3. **Audit Implementation:** How the audit was carried out.
4. **Risk Analysis:** Identifying internal and external risks, including financial and operational.
5. **Audit Process:** Detailed explanation of audit steps, evidence collection, and analysis.
6. **Findings:** Specific details of fraud (e.g., conflicts of interest, bribery, theft).
7. **Recommendations:** Measures to prevent future fraud, improve controls, and address systemic issues.
8. **Conclusion:** Final thoughts on the fraud, its impact, and proposed changes to governance.

Conclusion:

Forensic audits play a vital role in detecting financial crimes, uncovering fraud, and providing actionable evidence in legal proceedings. By systematically investigating financial records and using investigative techniques, forensic auditors help organizations protect their assets, maintain compliance, and resolve disputes effectively.

Social Audit Overview

Definition:

A **social audit** is a process of measuring, understanding, reporting, and improving an organization's social and ethical performance. It involves evaluating a company's activities, especially its social responsibility initiatives, to identify areas of improvement in societal impact, transparency, and governance. Social audits focus on understanding the gap between an organization's goals and its real-world outcomes, particularly in terms of social, economic, and environmental contributions.

Key Objectives of Social Audit:

1. **Increasing the efficacy and effectiveness of local development programs.**
2. **Scrutiny of policy decisions** to ensure alignment with stakeholders' interests, particularly those of the marginalized groups.

3. **Estimating opportunity costs** for stakeholders from delayed access to public services.
4. **Provision of information** to improve programs designed for community development.
5. **Assessing physical and financial gaps** between needs and available resources.
6. **Creating awareness** among beneficiaries and service providers about local social services.

Rights of Social Auditor:

1. Seek clarifications from the implementing agency on decisions, activities, schemes, income, and expenditures.
2. Scrutinize existing schemes and activities of the implementing agency.
3. Access relevant registers and documents of development activities.

Social Audit Coverage:

A social audit examines the impact of an organization on the community, addressing concerns like:

- **Charitable Contributions:** Donations, volunteer activities, and other corporate social responsibility efforts.
- **Environmental Impact:** Efficient energy use, waste management, and sustainability initiatives.
- **Work Environment:** Employee wages, benefits, and workplace conditions.

Implications of Social Audit:

- **Governance Impact:** Social auditing ensures accountability and transparency, enhancing decision-making through stakeholder involvement.
- **Amplifies Marginalized Voices:** Ensures that the perspectives of marginalized groups are heard, improving community engagement in governance.
- **Improves Local Governance:** Strengthens the transparency and accountability mechanisms in local bodies, ensuring that decisions are made with community consent and understanding.

Steps in Social Audit Process:

1. **Clarity of Purpose:**
 - Define the goals and objectives of the local elected body or organization undergoing the audit.
2. **Identify Stakeholders:**
 - Focus on the roles and responsibilities of stakeholders, ensuring that marginalized social groups have a voice.
3. **Define Performance Indicators:**
 - Establish clear and measurable performance indicators that all stakeholders understand and agree upon.
4. **Data Collection & Regular Meetings:**
 - Regularly collect data on performance and organize meetings for stakeholders to review progress.
5. **Commitments to Action:**
 - Review findings and make commitments on changes based on the social audit findings.
6. **Transparency and Reporting:**
 - Share findings with all stakeholders through reports and visible communication (e.g., posting on boards).

Implementation Requirements:

1. **Empowerment of People:**
 - Ensure beneficiaries have authority and rights to participate, using mechanisms like Gram Sabha in villages and the Right to Information (RTI) Act in cities.
2. **Proper Documentation:**
 - All documents, from proposals to financial statements and inspection reports, should be properly documented and accessible.
3. **Access to Information:**
 - Ensure transparency by making documents available online, allowing easy public access to the information.
4. **Punitive Action for Non-Compliance:**
 - Legal actions should be implemented for non-conformance to the social audit process to ensure accountability.

ICSI Social Audit Standards:

The **Institute of Company Secretaries of India (ICSI)** has established social audit standards for **social enterprises** engaged in various social initiatives, as per SEBI regulations. These standards guide the auditing process to ensure comprehensive and transparent evaluation.

ICSI Social Audit Standards:

1. **SAS-01:** Eradicating hunger, poverty, malnutrition, and inequality.
2. **SAS-02:** Promoting health care, sanitation, and safe drinking water.
3. **SAS-03:** Promoting education, employability, and livelihoods.
4. **SAS-04:** Promoting gender equality and empowerment of women and marginalized communities.
5. **SAS-05:** Ensuring environmental sustainability, climate change mitigation, and conservation of flora and fauna.
6. **SAS-06:** Protection of national heritage, art, and culture.
7. **SAS-07:** Promoting rural sports, Olympic, and Paralympic sports.
8. **SAS-08:** Supporting incubators of social enterprises.
9. **SAS-09:** Strengthening the non-profit ecosystem in fundraising and capacity building.
10. **SAS-10:** Promoting livelihoods for the rural and urban poor.
11. **SAS-11:** Slum area development, affordable housing, and resilient city building.
12. **SAS-12:** Disaster management, including relief, rehabilitation, and reconstruction.
13. **SAS-13:** Promotion of financial inclusion.
14. **SAS-14:** Facilitating access to land and property assets for disadvantaged communities.
15. **SAS-15:** Bridging the digital divide, data protection, and addressing misinformation.
16. **SAS-16:** Promoting the welfare of migrants and displaced persons.

Benefits of Social Audit:

1. **Enhances Social Reputation:** Builds trust and a positive image among stakeholders, especially the community.

2. **Encourages Social Performance:** Motivates organizations to improve their social welfare activities.
3. **Strengthens Stakeholder Relationships:** Improves relationships with stakeholders by meeting their expectations and ensuring long-term cooperation.
4. **Effective Comparison of Activities:** Allows for comparing the effectiveness of different social initiatives to identify the most impactful ones.

Conclusion:

Social audits are essential tools for ensuring transparency and accountability in organizations involved in social responsibility programs. They enable organizations to evaluate and report on their social impact, allowing for improvements in governance and enhancing stakeholder trust. Through a structured audit process, social enterprises can effectively align their actions with societal needs, ensuring a positive and sustainable impact.

ICSI Auditing Standards – An Overview

Introduction to ICSI Auditing Standards:

The **Companies Act, 2013** introduced the concept of **Secretarial Audit** for larger companies to ensure third-party professional assurance in governance, compliance, and disclosure matters. **Practicing Company Secretaries (PCS)**, holding a **Certificate of Practice (CoP)**, are specifically responsible for performing such audits, marking the first time that Company Secretaries were authorized to conduct audits under the Companies Act.

As part of their role, the PCS must provide a **Secretarial Audit Report** (in **Form MR-3**), as per **Section 204(1)** of the Companies Act and **Rule 9** of the Companies (Appointment & Remuneration Personnel) Rules, 2014. Additionally, PCSs are tasked with detecting and reporting frauds during the audit process.

ICSI's Role in Enhancing Auditing Standards:

Initially, performing secretarial audits, especially the detection of frauds, posed several challenges. To address these issues and strengthen the auditing capabilities of PCSs, the **Institute of Company Secretaries of India (ICSI)** took the initiative to develop auditing techniques and tools.

In response, ICSI established an **Auditing Standards Board**, which issued the **Company Secretaries Auditing Standards (CSAS)** to promote the best practices among its members. These standards were effective from **1st April 2021**.

Importance of ICSI Auditing Standards:

Adhering to ICSI's auditing standards ensures:

1. **Good Governance:** Fostering transparent and compliant organizational practices.
2. **Effective Fraud Detection:** Enhancing the PCS's ability to detect fraud and non-compliance.
3. **Uniformity in Auditing:** Promoting consistency and best practices across secretarial audits.

ICSI Auditing Standards (CSAS):

The four key standards introduced by ICSI are:

1. **CSAS-1: Auditing Standard on Audit Engagement:**
 - **Purpose:** Defines the auditor's role and responsibilities with respect to audit engagements.
 - **Content:** Specifies the process of entering into an agreement with the appointing authority for conducting the audit.

2. **CSAS-2: Auditing Standard on Audit Process and Documentation:**
 - **Purpose:** Lays down the responsibilities of the auditor regarding the audit process.
 - **Content:** Outlines the duties of the auditor in conducting the audit and maintaining proper documentation.
3. **CSAS-3: Auditing Standard on Forming of Opinion:**
 - **Purpose:** Guides the auditor on how to form an opinion based on the audit findings.
 - **Content:** Establishes the framework for the auditor to base their opinion on the subject matter of the audit.
4. **CSAS-4: Auditing Standard on Secretarial Audit:**
 - **Purpose:** Covers the methodology and framework for conducting the secretarial audit.
 - **Content:** Specifies the procedures and processes for conducting a secretarial audit.

Mandatory Applicability of ICSI Auditing Standards:

The mandatory applicability of the ICSI Auditing Standards (CSAS-1 to CSAS-4) was initially scheduled for **1st April 2021**. However, due to the developments arising from the **COVID-19 pandemic**, the enforcement was extended for audit engagements accepted by auditors **on or after 1st April 2021**. These standards have been **recommendatory** for audit engagements accepted **on or after 1st July 2019** and **mandatory** for audit engagements accepted **on or after 1st April 2021**.

ICSI Auditing Standards – Future Focus:

Future lessons will delve deeper into each of the **CSAS-1 to CSAS-4** standards, providing detailed insights into how they help shape the audit process, improve compliance, and foster transparency within organizations.

Ch-9

Regulatory Framework and Audit Engagement

Key Regulations:

- **Companies Act, 2013:** Sections 92, 138, 139, 141, 142, 149, 178, 179, 204.
- **Companies Secretaries Act, 1980:** Schedule I and II.
- **ICSI CSAS-1:** Auditing Standard on Audit Engagement.

Meaning of Audit Engagement:

- An **audit engagement** is a **contractual arrangement** where an **auditor** is appointed to perform an audit of a company's transactions.
- It is formalized through an **engagement letter** between the **auditee** (company) and the **auditor**.

ICSI's CSAS-1 defines:

- **Audit Engagement:** A formal arrangement specifying terms of reference, scope of audit, remuneration, and limiting conditions, if any.

Mandatory Applicability of CSAS-1:

- **Mandatory for Audit Engagements accepted on or after: April 1, 2021.**

Scope of CSAS-1:

- **Applicability:** CSAS-1 applies to auditors undertaking audit engagements under any statute.
- **Focus:** It covers the **auditor's role and responsibilities**, including the process of entering into an agreement with the **appointing authority**.

Offer and Acceptance of Audit Engagement:

- **Offer:** The engagement may be initiated by the **auditee** or the **auditor**. It involves defining scope, fees, timeline, and terms.

Example Offer:

- **Company:** "We wish to engage you for internal audit for FY 2022-23, covering internal controls, compliance, governance, etc., with a fee of INR 5,00,000."
- **Acceptance:** After reviewing, the **auditor** accepts, possibly adding additional terms such as presenting findings before the **audit committee** or requiring access to records.

Steps in Audit Engagement:

1. **Selection and Screening of Auditee:**
 - Evaluate risks, client history, and performance factors before accepting the engagement.
 - Factors include **reputation, performance risk, commercial terms**, etc.
2. **Pre-engagement Meeting:**
 - **Discuss terms**, prior audits, reporting frameworks, internal controls, audit process, timelines, and potential conflicts of interest.
 - Confidentiality obligations must be emphasized.
3. **Signing Engagement Letter:**
 - After discussions, the engagement letter is signed, formalizing the terms of the audit.
4. **Certificate by Auditor:**
 - Before acceptance, auditors must confirm compliance with ICSI guidelines, no conflicts of interest, and no legal restrictions.

Preconditions for Accepting/Continuing Professional Engagement:

- **Audit Preconditions:**
 - Ensure the **reporting framework** is acceptable.
 - Confirm that **management acknowledges** its responsibilities for preparing accurate non-financial statements, establishing internal controls, and providing access to all relevant information.
- **Limitations on Scope:**
 - If the **scope** of the audit is limited in a way that would affect the auditor's opinion, the auditor should not accept the engagement, unless mandated by law.

Criteria for Declining or Withdrawing from Engagement:

- **Client-Related Factors:**
 - **Independence risk:** If client information impacts the auditor's independence.
 - **Capacity issues:** If the firm cannot provide adequate service due to technical skill gaps or resources.