# Secretarial Audit

Lesson 13

## KEY CONCEPTS

■ Secretarial Audit ■ Secretarial Audit Process ■ CSAS-4 ■ Code of Conduct ■ Board Composition ■ Board Processes ■ Detection of Fraud ■ Audit Report

## Learning Objectives

**To understand:**

- Secretarial Audit as a proactive governance measure that will have a positive effect on corporate entities.
- Secretarial Audit as a form of Compliance Auditing that is used in carrying out auditing of compliances with all laws, rules and regulatory requirements applicable to the company.
- The process of conducting Secretarial Audit and various aspects of legal compliance requirements.
- Various aspects of the reporting of fraud with specific reference to Secretarial Audit.

## Lesson Outline

- Secretarial Audit and its need
- ICSI CSAS-4
- Applicability of Secretarial Audit
- Secretarial Audit and Company Secretary in Practice
- Scope of Secretarial Audit
- Secretarial Audit- the process
- Verification of Compliances
- Panel Provisions
- Reporting of Fraud
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings
- Other References (Including Websites/Video Links)

## REGULATORY FRAMEWORK

- The Companies Act, 2013 and rules mentioned thereunder
- SEBI (LODR) Regulations, 2015
- ICSI CSAS-4

## INTRODUCTION

The term "Secretarial Audit" refers to the mechanism which is connected with the audit of the non-financial aspects of the company. It gives necessary comfort to the investors, management, regulators and other stakeholders, as to the compliance of all applicable laws by the company and certifies the existence of adequate systems and processes for ensuring compliance of laws in the company.

Secretarial Audit is not just an audit of the diligent compliance or that of the adherence to the law in true letter and spirit but has proved to be a strong founding pillar of the governance framework of the Indian Corporate Sector and a futuristic torchlight for the entire Indian Economy. Secretarial Audit, as a result of faith of the law makers and the Regulatory Authorities in the Governance Professionals or as the law puts it, in the practicing company secretaries, bestows a huge responsibility on the Secretarial Auditors.

In the era of minimum government, maximum governance, the Secretarial Audit postulates for an independent verification of the records, books, papers and documents by a Company Secretary to check the compliance status of the company according to the provisions of various statutes, laws and rules & regulations and also to ensure the compliance of legal and procedural requirements and processes followed by the company. Secretarial Audit is, therefore, an independent and objective assurance intended to add value and improve operations of a company. It helps to accomplish the organisation's objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control, and governance processes.

> The implementation of Secretarial Audit and the Annual Secretarial Compliance Report was an important milestone for the Profession of Company Secretaries. It opened up new vistas for Practising Company Secretaries. As for Companies, it was altogether a transformation with respect to adopting good corporate governance practices and thereby instilling confidence among the various stakeholders. It also boosted the overall confidence of the investors.

## SECRETARIAL AUDIT & COMPANY SECRETARY IN PRACTICE (PCS)

A Company Secretary in practice is a professional who is well-versed in matters of statutory, procedural and practical aspects of laws applicable to companies, both listed and unlisted public and private companies. A strong knowledge base makes him a competent professional to conduct Secretarial Audit. In terms of section 204(1), only a member of the Institute of Company Secretaries of India holding certificate of practice (Company Secretary in Practice) can conduct Secretarial Audit and issue the Secretarial Audit Report to the company.

Students are advised to refer the Auditing Standards issued by the Institute of Company Secretaries along with the Guidance Note on Auditing Standards, the updated Guidance Note on Secretarial Audit, Guidance note on the Annual Secretarial Compliance Report for the detailed checklist on the other aspects relating to Secretarial Audit which is not covered in this study material.

> **Test Yourself:**
>
> **Question:** Who can conduct Secretarial Audit?
>
> **Answer:** Only a member of the Institute of Company Secretaries of India holding certificate of practice (company secretary in practice) can conduct Secretarial Audit and furnish the Secretarial Audit Report to the company. [Section 204(1) of Companies Act, 2013]

## SECRETARIAL AUDIT-LEGAL PROVISIONS

The genesis of the Secretarial Audit can be traced to the Companies (Amendment) Act, 1988 which amended Section 161 of the Companies Act, 1956. This amendment introduced the requirement of certification of annual return of listed Companies by a Practising Company Secretaries. Thereafter, Companies (Amendment) Act, 2000 amended Section 383A of the Companies Act, 1956. By this amendment, it was mandated that companies which had a paid-up share capital of Rs.10 lakh or more and which did not require to employ a Whole-time Company Secretary had to obtain a Certificate from a Practising Company Secretaries on an annual basis regarding the compliance of the various provisions of the Act.

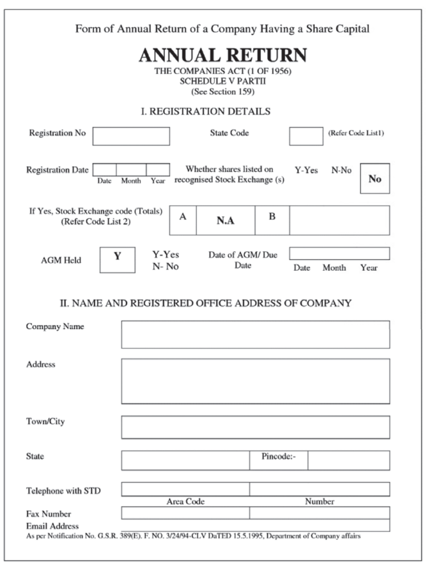
This certificate was to be attached with the Board's Report. In 2002, Naresh Chandra Committee Report on Corporate Audit and Governance recommended introduction of Compliance Audit. Later in the year 2003, the Ministry of Corporate Affairs (MCA) introduced the Companies (Amendment) Bill, 2003, which introduced the concept of Secretarial Audit by giving powers to Central Government to order, at any time, the secretarial compliance audit of the company for any period. Similarly, the Concept Paper published by MCA in 2004, contemplated to enact a new Company Law in which the concept of the Secretarial Compliance Audit was included. Later on, Corporate Governance Voluntary Guidelines, 2009 was released in December 21, 2009, which insisted on adoption of Secretarial Audit for public companies and private companies, particularly the bigger ones. Para V of the Guidelines stated that: "Since the Board has the overarching responsibility of ensuring transparent, ethical and responsible governance of the company, it is important that the Board processes and compliance mechanisms of the company are robust.

To ensure this, the companies may get the Secretarial Audit conducted by a competent professional. The Board should give its comments on the Secretarial Audit in its report to the shareholders." Thereafter, the 21st report of the Parliamentary Standing Committee on Finance on the Companies Bill, 2009 also specified about Secretarial Audit. The extract from the said report is reproduced below:

*"Para 7.8 of Chapter VII: Secretarial Audit may also be mandated for bigger companies, including all listed companies; as it, inter alia, provides necessary assurance to the investors that the affairs of the Company are being conducted in accordance with the legal requirements."*

At last, Secretarial Audit for bigger Companies has been notified from 1st April 2014 under the Companies Act, 2013 (the Act). As the Public shareholders subscribe to the shares of listed entities and public companies, it is necessary that the interest of the public is protected from the impact of non-compliances of the various provisions of the Act and other Corporate Laws. Besides, this would insulate the directors and other stakeholders like employees, suppliers, banks and financial institutions from the ill effects of non-compliance.

**Secretarial Audit Journey**



Form of Annual Return of a Company Having a Share Capital

**ANNUAL RETURN**

THE COMPANIES ACT (1 OF 1956)
SCHEDULE V PARTII
(See Section 159)

I. REGISTRATION DETAILS

Registration No | State Code | (Refer Code List1)

Registration Date (Date Month Year) | Whether shares listed on recognised Stock Exchange (s) | Y-Yes N-No | **No**

If Yes, Stock Exchange code (Totals) (Refer Code List 2) | A | N.A | B |

AGM Held | **Y** | Y-Yes N- No | Date of AGM/ Due Date | Date Month Year

II. NAME AND REGISTERED OFFICE ADDRESS OF COMPANY

Company Name

Address

Town/City

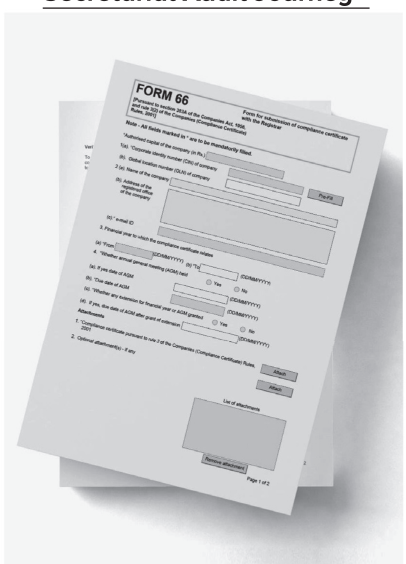
State | Pincode:-

Telephone with STD | Area Code | Number

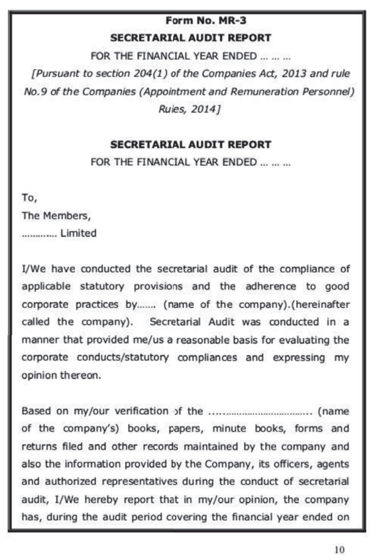
Fax Number

Email Address

As per Notification No. G.S.R. 389(E). F. NO. 3/24/94-CLV DaTED 15.5.1995, Department of Company affairs



FORM 66



**Form No. MR-3**

**SECRETARIAL AUDIT REPORT**

FOR THE FINANCIAL YEAR ENDED ... ... ...

*[Pursuant to section 204(1) of the Companies Act, 2013 and rule No.9 of the Companies (Appointment and Remuneration Personnel) Rules, 2014]*

**SECRETARIAL AUDIT REPORT**

FOR THE FINANCIAL YEAR ENDED ... ... ...

To,
The Members,
............ Limited

I/We have conducted the secretarial audit of the compliance of applicable statutory provisions and the adherence to good corporate practices by....... (name of the company).(hereinafter called the company). Secretarial Audit was conducted in a manner that provided me/us a reasonable basis for evaluating the corporate conducts/statutory compliances and expressing my opinion thereon.

Based on my/our verification of the ................................... (name of the company's) books, papers, minute books, forms and returns filed and other records maintained by the company and also the information provided by the Company, its officers, agents and authorized representatives during the conduct of secretarial audit, I/We hereby report that in my/our opinion, the company has, during the audit period covering the financial year ended on

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## THE COMPANIES ACT, 2013

Section 204(1) of the Companies Act, 2013 read with rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 provides that-

a) Every Listed Company;

b) Every public company having a paid-up share capital of fifty crore rupees or more; or

c) Every public company having a turnover of two hundred fifty crore rupees or more;

d) Every company having outstanding loans or borrowings from banks or public financial institutions of one hundred crore rupees or more.

shall annex with its Board's report made in terms of sub-section (3) of section 134 of the Act, a Secretarial Audit report given by a Practising Company Secretaries., in form No. MR-3, as attached as **Annexure -A**.

*Explanation to this sub-rule clarifies that the paid-up share capital, turnover, or outstanding loans or borrowings as the case may be, existing on the last date of latest audited financial statement shall be taken into account.*

Section 204 (2) - It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

Section 204 (3) - The Board of Directors, in their report made in terms of sub-section (3) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary in practice in his report under sub-section (1).

Section 204 (4) - If a company or any officer of the company or the company secretary in practice, contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be liable to a penalty of 2,00,000 rupees.

**Applicability of Section 204 to a Company which is a subsidiary of a Public Company:**

Section 2(71) of the Companies Act, 2013 defines a "Public Company" as a company which –

(a) is not a private company; and

(b) has a minimum paid-up share capital as may be prescribed.

The proviso to the definition states that "provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles."

***Illustration:***

*PPP Pvt. Ltd. was incorporated in the year 2010 as Private Company. Its paid up capital is Rs. 35 crore, but the annual turnover for the financial year ended on 31st March, 2023, first time crossed from Rs. 240 crores to Rs. 300 crores. SSS Ltd, a public company, controls the composition of the Board of Directors of PPP Pvt. Ltd, hence in terms of Section 2(87) of Companies Act, 2013, PPP Pvt. Ltd is treated as subsidiary company of SSS Ltd. A newly appointed Company Secretary of PPP Pvt. Ltd suggested the Board of Directors to get the Secretarial Audit of this company. Whether the Secretarial Audit of a Private Limited Company is mandatory as per the provisions of the Companies Act, 2013.*

*By above mentioned definition, it can be inferred that Secretarial Audit would be applicable to a private company which is a subsidiary of a public company, and which falls under the prescribed class of companies.*

In view of this, it is clear that Section 204 is applicable to a private company which is a subsidiary of a public company, and which falls under the prescribed class of companies.

Although, the companies which are not covered under section 204 may opt for conducting Secretarial Audit voluntarily as it provides an independent assurance of the compliances of applicable laws by the company.

**Need of Secretarial Audit:**


The need for secretarial audit arises from several factors, all of which contribute to ensuring corporate transparency, compliance with laws and regulations, and the overall health of the organization. Here are some key reasons why secretarial audit is essential:

1. **Compliance Verification**: Secretarial audit helps verify compliance with various laws, regulations, and guidelines applicable to the company, such as the Companies Act, SEBI regulations, FEMA regulations, etc. It ensures that the company operates within the legal framework and fulfils its statutory obligations.

2. **Corporate Governance**: Secretarial audit plays a crucial role in promoting good corporate governance practices. By reviewing the company's governance structure, board procedures, disclosure practices, and adherence to ethical standards, it helps identify areas for improvement and ensures transparency and accountability.

3. **Risk Mitigation**: Conducting regular secretarial audits helps identify potential risks and deficiencies in internal controls, policies, and procedures. By identifying these risks early on, companies can take proactive measures to mitigate them and prevent potential legal, financial, or reputational damage.

4. **Stakeholder Confidence**: Secretarial audit enhances stakeholder confidence by demonstrating the company's commitment to transparency, compliance, and ethical business practices. It provides assurance to investors, lenders, regulators, and other stakeholders that the company's affairs are conducted in a responsible and lawful manner.

5. **Preventing Fraud and Mismanagement:** Secretarial audit helps detect instances of fraud, mismanagement, or irregularities within the organization. By examining the company's records, transactions, and governance practices, auditors can identify red flags and investigate further to prevent or mitigate potential fraud or misconduct.

6. **Legal Requirements**: In many jurisdictions, secretarial audit is a legal requirement for certain types of companies or for companies above a certain size threshold. Failure to conduct a secretarial audit or comply with its findings may lead to legal and regulatory consequences, including penalties, fines, or even legal action against the company and its officers.

7. **Improving Efficiency and Effectiveness**: Through the process of secretarial audit, companies can identify inefficiencies in their administrative and compliance processes and implement measures to improve efficiency and effectiveness. This can lead to cost savings, enhanced productivity, and better utilization of resources.

In conclusion, secretarial audit is indispensable for ensuring legal compliance, promoting good corporate governance, mitigating risks, enhancing stakeholder confidence, preventing fraud and mismanagement, complying with legal requirements, and improving overall organizational efficiency and effectiveness. It is a valuable tool for companies to maintain integrity, transparency, and accountability in their operations.

**Secretarial Audit as a Tool for Good Corporate Governance:**


Secretarial audit serves as a crucial corporate governance tool by ensuring transparency, compliance, and accountability within organizations. Here's how secretarial audit contributes to effective corporate governance:

1. **Ensuring Regulatory Compliance**: Secretarial audit verifies compliance with various laws, regulations, and guidelines applicable to the company. By reviewing corporate records, governance practices, and statutory filings, secretarial auditors ensure that the organization operates within the legal framework and fulfills its regulatory obligations.

2. **Monitoring Corporate Practices**: Secretarial audit monitors corporate practices to ensure they align with ethical standards and best practices. By assessing board procedures, decision-making processes, and governance structures, secretarial auditors help identify areas for improvement and ensure that the organization adheres to principles of good governance.

3. **Assessing Board Effectiveness**: Secretarial audit evaluates the composition, independence, and performance of the board of directors. By reviewing board meeting minutes, director appointments, and adherence to governance guidelines, secretarial auditors assess the effectiveness of the board in fulfilling its oversight responsibilities and promoting the interests of stakeholders.

4. **Enhancing Transparency and Disclosure:** Secretarial audit promotes transparency by ensuring accurate and timely disclosure of information to stakeholders. By reviewing disclosure practices, communication channels, and shareholder relations, secretarial auditors help maintain open and transparent communication with investors, regulators, and other stakeholders, building trust and confidence in the organization.

5. **Identifying Risks and Controls**: Secretarial audit helps identify risks and evaluate the effectiveness of internal controls within the organization. By assessing compliance mechanisms, risk management frameworks, and corporate policies, secretarial auditors assist in identifying potential risks, such as legal liabilities or reputational risks, and recommend measures to strengthen internal controls.

6. **Supporting Strategic Decision-Making**: Secretarial audit provides insights that support strategic decision-making processes. By identifying governance gaps, compliance issues, and opportunities for improvement, secretarial auditors help management and the board make informed decisions that promote the long-term success and sustainability of the organization.

Overall, secretarial audit plays a crucial role in promoting good corporate governance practices, fostering trust among stakeholders, and ensuring the integrity and credibility of the organization. By providing independent assurance on governance processes and compliance practices, secretarial audit helps organizations uphold their commitments to transparency, accountability, and ethical conduct.

**Objectives of a Secretarial Audit**

The objectives of a secretarial audit encompass various aspects of ensuring legal compliance, promoting good corporate governance, and enhancing transparency within an organization. Here are the key objectives of secretarial audit:

1. **Verification of Compliance:** To verify compliance with the provisions of applicable laws, regulations, and guidelines governing the company's operations, including the Companies Act, SEBI regulations, FEMA regulations, and other relevant statutes.

2. **Assessment of Governance Practices:** To assess the adequacy and effectiveness of corporate governance practices within the organization, including the composition and functioning of the board of directors, adherence to governance guidelines, and ethical standards.

3. **Identification of Legal and Regulatory Risks:** To identify potential legal and regulatory risks faced by the company and assess the adequacy of internal controls and compliance mechanisms in mitigating these risks.

4. **Evaluation of Board Procedures:** To evaluate the procedures and processes followed by the board of directors in discharging their duties and responsibilities, including decision-making processes, meeting protocols, and adherence to statutory requirements.

5. **Review of Statutory Registers and Records:** To review the maintenance and accuracy of statutory registers, records, and filings required under company law, ensuring that they are up-to-date and compliant with legal requirements.

6. **Examination of Disclosures and Reporting:** To examine the accuracy and completeness of disclosures made by the company to regulators, shareholders, and other stakeholders, ensuring transparency and accountability in reporting practices.

7. **Assessment of Related Party Transactions:** To assess the adequacy of controls and disclosures related to transactions with related parties, ensuring compliance with regulatory requirements and safeguarding against potential conflicts of interest.

8. **Detection of Fraud and Mismanagement:** To detect instances of fraud, mismanagement, or irregularities within the organization by conducting a comprehensive review of corporate records, transactions, and governance practices.

9. **Recommendation of Remedial Measures:** To recommend remedial measures to address any deficiencies or weaknesses identified during the audit, ensuring that the company takes corrective action to enhance compliance and governance practices.

10. **Enhancement of Stakeholder Confidence:** To enhance stakeholder confidence by providing independent assurance on the company's compliance and governance practices, fostering trust and credibility among investors, regulators, and other stakeholders.

**Test Yourself:**

**Question:** Is Secretarial Audit applicable on private limited companies, which is subsidiary of public company having turnover of more than Rupees 250 Crore?

**Answer:** Yes.

## SECRETARIAL AUDIT AND SECRETARIAL COMPLIANCE REPORT UNDER THE SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

In view of the criticality of secretarial functions for ensuring efficient functioning of the Board, the Kotak Committee on Corporate Governance, in its report dated October 05, 2017, recommended that-

(a) Secretarial Audit to be made compulsory for all listed entities under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, in line with the provisions of the Companies Act, 2013.

(b) Secretarial Audit to be extended to all material unlisted Indian subsidiaries in line with the recommendations of the Committee on strengthening group oversight and improving compliance at a group level for listed entities.

Accordingly, SEBI vide circular no. CIR/CFD/CMD1/27/2019 dated February 08, 2019 notified the following provisions to be included in the SEBI (LODR) Regulations, 2015:

- *Regulation 24A*: Secretarial Audit: Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake secretarial audit and shall annex with its annual report, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed with effect from the year ended March 31, 2019.

This will ensure the strengthening of the oversight of group companies of the listed entities. The term 'Material Subsidiary' means a subsidiary, whose Turnover or net worth exceeds ten per cent (10%) of the consolidated Turnover or net worth, respectively, of the listed entity and its subsidiaries in the immediately preceding accounting year.

The above provision has been substituted by the SEBI vide amendment dated 13.12.2024 which reads as under:

- **Regulation 24A (1) (a) Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake Secretarial Audit by a Secretarial Auditor who shall be a Peer Reviewed Company Secretary and shall annex a Secretarial Audit Report in such form as specified, with the annual report of the listed entity.**

Explanation:

(i) “Secretarial Auditor” means a Company Secretary in Practice or a firm of Company Secretary(ies) in practice appointed to conduct the Secretarial Audit.

(ii) “Peer Reviewed Company Secretary” means a Company Secretary in practice, who is either practicing individually or as a sole proprietor or as a partner of a Peer Reviewed Practice Unit, holding a valid certificate of peer review issued by the Institute of Company Secretaries of India.

(b) On the basis of recommendation of board of directors, a listed entity shall appoint or re-appoint:

(i) an individual as Secretarial Auditor for not more than one term of five consecutive years; or

(ii) a Secretarial Audit firm as Secretarial Auditor for not more than two terms of five consecutive years, with the approval of its shareholders in its Annual General Meeting:

Provided that-

(i) an individual Secretarial Auditor who has completed his or her term under sub-clause (i) of this clause shall not be eligible for re-appointment as Secretarial Auditor in the same entity for five years from the completion of his or her term;

(ii) a Secretarial Audit firm which has completed its term under sub-clause (ii) of this clause, shall not be eligible for re-appointment as Secretarial Auditor in the same entity for five years from the completion of such term:

Provided further that as on the date of appointment no Secretarial Audit firm having a common partner or partners to the other Secretarial Audit firm, whose tenure has expired in the listed entity immediately preceding the financial year, shall be appointed as Secretarial Auditor of the same listed entity for a period of five years:

Provided further that, nothing contained in these regulations shall prejudice the right of the entity to remove Secretarial Auditor with the approval of its shareholders in its Annual General Meeting or the right of the Secretarial Auditor to resign from such office of the listed entity.

(c) The casual vacancy arising out of resignation, death or disqualification of a Secretarial Auditor shall be filled by the board of directors of the listed entity within a period of three months and the secretarial auditor so appointed shall hold office till the conclusion of the next annual general meeting.

(1A) Eligibility, Qualifications and Disqualifications of Secretarial Auditor:

(a) A person shall be eligible for appointment as a Secretarial Auditor of the listed entity only if such person is a Peer Reviewed Company Secretary and has not incurred any of the disqualifications as specified by the Board:

Provided that a firm whereof majority of partners practicing in India are qualified for appointment as aforesaid may be appointed by its firm name to be Secretarial Auditor of the listed entity.

(b) Where a firm including a limited liability partnership is appointed as Secretarial Auditor of the listed entity, only the partners who are Peer Reviewed Company Secretaries shall be authorized to act and sign on behalf of the firm.

(c) Where a person appointed as Secretarial Auditor of the listed entity incurs any of the disqualifications as specified by the Board, after appointment, such person shall vacate the office as Secretarial Auditor and such vacation shall be deemed to be a casual vacancy in the office of the Secretarial Auditor.

(1B) Secretarial Auditor not to render certain services:

A Secretarial Auditor appointed under these regulations shall provide to the listed entity only such other services as are approved by the board of directors, but which shall not include any services as specified by the Board in this behalf.

(1C) With effect from April 1, 2025, every listed entity shall ensure compliance with sub-regulation (1), (1A) and (1B) for appointment, re-appointment or continuation of the Secretarial Auditor of the listed entity:

Provided that any association of the individual or the firm as the Secretarial Auditor of the listed entity before March 31, 2025 shall not be considered for the purpose of calculating the tenure under clause (b) of sub-regulation (1).

(2) Every listed entity shall submit a secretarial compliance report in such form as specified, to stock exchanges, within sixty days from end of each financial year:

Provided that the listed entity shall ensure that with effect from April 1, 2025, the Secretarial Compliance Report submitted to the stock exchange(s) on annual basis is signed only by the Secretarial Auditor or by a Peer Reviewed Company Secretary who satisfies the conditions mentioned in sub-regulations (1A) and (1B) of this regulation.

SEBI while reposing immense confidence in the members of ICSI has mandated the issuance of Annual Secretarial Compliance Report by a Company Secretary in Practice to the listed entities to enable them to undertake certifications in accordance with the Regulations and this circular in letter and in spirit. Annual Secretarial Audit shall cover a broad check on compliance with all laws applicable to the entity, listed entities shall additionally, on an annual basis, require a check by the Company Secretary in Practice on compliance of all applicable SEBI Regulations and circulars / guidelines issued thereunder, consequent to which, the Company Secretary in Practice shall submit a report to the listed entity in the manner specified in this circular.

The Annual Secretarial Compliance Report is applicable to all Listed Entities.

The Annual Secretarial Compliance Report postulates for an independent verification of the records, books, papers and documents by a Company Secretary in Practice to check the compliance status of the company with the provisions of all applicable SEBI laws, Regulations and circulars/ guidelines issued thereunder.

**Test Yourself:**

**Question:** Is it compulsory for a listed entity to annex Secretarial Audit Report to annual report?

**Answer:** Yes, as section 204 requires the Secretarial Audit Report with Board Report, but Regulation 24A of SEBI (LODR) Regulations, 2015 provides the requirement of annexing it with Annual Report.

**Exemptions:**

As per regulation 15 of the SEBI (LODR) Regulations, 2015 the compliance specified in regulations 24A, shall not apply, in respect of –

15(2)(a)Listed entity having paid up equity share capital not exceeding rupees ten crore and net worth not exceeding rupees twenty five crore, as on the last day of the previous financial year:

Provided that where the provisions of regulations 17 to 27, clauses (b) to (i) and (t) of sub-regulation (2) of regulation 46 and para C, D and E of Schedule V become applicable to a listed entity at a later date, it shall ensure compliance with the same within six months from such date.

Provided further that once the above regulations become applicable to a listed entity, they shall continue to remain applicable till such time the equity share capital or the net-worth of such entity reduces and remains below the specified threshold for a period of three consecutive financial years.

15(2)(b)listed entity which has listed its specified securities on the SME Exchange:

Provided that with effect from April 01, 2025, the provisions of regulation 23 (Related party transactions) shall be applicable in respect of a listed entity which has listed its specified securities on the SME Exchange and which has either paid up equity share capital exceeding Rupees ten crore or net worth exceeding Rupees twenty-five crore, as on the last day of the previous financial year.

Provided further that where the provisions of regulation 23 become applicable at a later date to a listed entity which has listed its specified securities on the SME Exchange, it shall ensure compliance with the same within six months from such date.

Provided further that once the provisions of regulation 23 become applicable to a listed entity which has listed its specified securities on the SME Exchange, they shall continue to remain applicable till such time the equity share capital and the net-worth of such entity reduces and remains below the specified threshold for a period of three consecutive financial years.

## AUDITING STANDARD ON SECRETARIAL AUDIT (CSAS-4)

The Auditing Standard on Secretarial Audit (CSAS-4) formulated by Auditing Standards Board (ASB) of the Institute of Company Secretaries of India (ICSI) and issued by the Council of ICSI, is effective from 1st July, 2019 on recommendatory basis and mandatory with effect from 1st April, 2021.

The Standard shall apply to Secretarial Audit undertaken under Section 204 of the Companies Act, 2013 and Regulation 24A of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. The Standard deals with basis and manner for carrying out the Secretarial Audit.

The objective of the Standard is to lay down the principles for evaluation of statutory compliances and corporate conduct in relation thereto.

The application of this Standard is not mandatory for:

- Annual Secretarial Compliance Report issued in terms of SEBI Circular No. CIR/CFD/CMD1/27/2019 dated 8th February, 2019; and
- Secretarial Audit entrusted on a voluntary basis by an Auditee to an Auditor. However, adherence to the Standard is recommended in respect of Audits entrusted on voluntary basis also.

***Note:*** *This Standard is not applicable in case the Secretarial Audit is mandated by any third party or regulatory authority.*

However, if the Auditor has followed the Auditing Standards issued by the ICSI while performing the Audit, he should state the fact that he has followed the Auditing Standards (CSAS 1 to CSAS 4) issued by the Institute of Company Secretaries of India.

**How adherence to other standards has to be ensured while complying with CSAS-4?**

An Auditor while accepting Secretarial Audit, shall also comply with the principles laid down in CSAS-1 to CSAS 3.

For example, M/s. ABC & Associates, a practicing company secretaries firm, accepts an audit assignment on 20th April, 2021 for the FY 2021-2022. The firm should adhere to the principles laid down in the CSAS-1 (Audit Engagement) while accepting the audit assignment, the Auditor should plan, proceed and perform the audit assignment as per the CSAS-2 (Audit Process and Documentation) and give his opinion based on the Audit Process performed by him in line with the principles given in CSAS-3 (Forming of Opinion).

## CONCEPT & ADVANTAGES

### CONCEPT

Secretarial audit can be an effective multi-pronged weapon to assure the regulators, generate confidence amongst the shareholders, the creditors and other stakeholders in companies, assure FIIs/FIs/SFCs/SIDCs/ Banks and instil self-regulation and professional discipline in companies. It is a tool of risk mitigation and will allow companies to effectively address compliance risk issues.

**Test Yourself:**

**Question:** What is periodicity of Secretarial Audit?

**Answer:** Proactive Secretarial Audit on a continuous basis would help the company in initiating corrective measures and strengthening its compliance mechanism and processes. It is therefore, advisable that the Secretarial Audit is carried out periodically (quarterly / half year / annually) and adverse finding if any, is reported on interim basis to the Board immediately. The Secretarial Audit Report to be annexed with Board's report is required to be submitted before the preparation of Board's Report.

Once the Secretarial Audit Report is submitted by the secretarial auditor, the Government as well as other stakeholders can gauge in first instance the level of compliances or non-compliances by the company concerned. It can then immediately take suitable corrective measures under the specific applicable legislations. The measures would act as a check on frauds as well as reduce the number of prosecutions by the Government and consequent litigation on account of non-compliance with the provisions of corporate and securities laws, thereby resulting in healthy and orderly development of the corporate sector. This would, in turn, lead to reduction of investor grievances and enhance various stakeholders' confidence.

In addition to the Government and shareholders, introduction of secretarial audit would be in the interest of companies themselves.

Secretarial audit besides ensuring due compliance of the statute, will act as an aid to the management by proving to be a strong internal control device. It can relieve the company and their directors from consequences of unintended non-compliance of law. Independent directors and nominee directors can be assured that the affairs of the company are being conducted as per law. Besides the Secretarial Auditor can act as a fearless adviser to the company so that the mistakes and lapses, if any, could be rectified well in time and management is reassured that internal systems are guarded.

Few risks of non-compliance with laws and regulations:

| | |
|---|---|
| Failure of legal compliance | Failure to keep proper books and records or non-compliance with the provisions of corporate laws and securities laws, executing certain unviable or undesirable corporate actions or transactions with related parties or loan to directors, issue, allotment and transfer of security or otherwise, without proper authority of the board of directors or the general meeting or the memorandum of association, etc., could lead to the ability by third parties to play with the stakeholder's limited liability protection. |
| Failure to obtain proper approvals/permissions/ Licenses | Failure to obtain proper approvals/permissions/licenses could lead to fines, penalties or/and imprisonment in some cases, even closure of the business by government or governmental agencies. |
| Regulatory actions | Failure to comply with certain laws and regulations may lead to initiation of action by the regulators like MCA, SEBI, RBI or others authorities, which may jeopardize the very stability of the financial and manufacturing operations. |
| Non-compliances of Environment Laws | Failure to adopt proper environment law compliance and policies which are reviewed periodically could give rise to governmental and civil liability, besides causing risk to the environmental sustainability. |
| Failure to keep accurate records | Failure to keep accurate records and minutes of its decision-making procedures, proves that directors are not exercising informed judgment, and may subject the company and its board to liability to its shareholders and investors. |

| | |
|---|---|
| Failure to monitor the company's reporting requirements | Failure to monitor the company's reporting requirements may put the company into a position of default with lenders or investors. |
| PCS as extended Arm | Company secretary in practice acts as an extended arm of the regulators in ensuring the compliances. Detecting and reporting any non-compliance before it takes seriously alarming shape. |

The inclusion of Secretarial Audit Report in the Directors' Report would go a long way in reassuring public, financial institutions and all others dealing with the company about the quality of corporate governance in the corporate entity concerned.

Companies entering into joint ventures and foreign collaborations will need such an audit to assure foreign partners that the laws of the land are duly complied with. A secretarial audit will serve as a first line due diligence. The secretarial audit will provide an in-built mechanism for enhancing corporate compliances generally and help restore the confidence of investors in the capital market through greater transparency in the corporate functioning.

## ADVANTAGES

Secretarial Audit provides an effective mechanism to ensure that compliance of various legislations and regulations including the Companies Act, SEBI Law, Secretarial Standards and other corporate and economic laws applicable to the company has been diligently done. This would give necessary comfort to the Investors, Management, Regulators and Other Stakeholders.

The periodical Secretarial Audit helps to detect the instances of non-compliances and facilitates taking corrective-measures well in time to avoid any further risk.

Secretarial Audit facilitates monitoring compliances with the requirements of law through a formal compliance management programme which can produce following positive results to the stakeholders of a company:

- Better compliance of laws leading to reduction in number of frauds and consequent prosecutions.
- Protecting the interest of stakeholders and strengthening their faith in the corporates.
- Protecting the company/directors from the consequences of unintended non-compliance of laws.
- Independent assurance and comfort to independent/non-executive/nominee directors that the affairs of the company have been conducted as per law.
- Instilling professional discipline and self-regulation.
- Reducing workload of regulators due to better and timely compliances.
- Enhancing quality of services to investors.
- Any qualification in the Report will immediately alert the investor.


(a) *Promoters*

Secretarial audit assures the promoters of a company that those in-charge of its management are conducting its affairs in accordance with the requirements of laws and the owner's stake is not being exposed to unintended risks.

(b) *Non-executive/Independent directors*

Secretarial audit provides comfort to the non-executive/independent directors that appropriate mechanisms and processes are in place to ensure compliance with laws applicable to the company, thus mitigating any risk from a regulatory or governance perspective.

(c) Government authorities/regulators

It also facilitates reducing the burden of the regulators in ensuring compliances and they can take timely actions against the offenders.

(d) *Investors*

Secretarial audit helps the investors in taking informed investment decision, as it evaluates the company in terms of compliance and governance norms being followed by the company.

(e) *Other Stakeholders*

It is an effective due diligence exercise for the prospective investors or joint venture partners. Further financial institutions, banks, creditors and consumers can measure the law abiding nature of company management.

## RISK OF SECRETARIAL AUDITOR

**Section 204(4) - Punishment for Contravention:**

If a company or any officer of the company or the company secretary in practice, contravenes the provisions of section 204, then the company, every officer of the company or the company secretary in practice, who is in default, shall be liable to a penalty of two lakh rupees.

In case the Practicing Company Secretary failed to comply with the provisions of section 143 is liable for a penalty:

(a) in case of a listed company, be liable to a penalty of five lakh rupees; and

(b) in case of any other company, be liable to a penalty of one lakh rupees.

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

**Section 448 - Punishment for false statement:** Save as otherwise provided in this Act, if in any return, report, certificate, financial statement, prospectus, statement or other document required by, or for, the purposes of any of the provisions of this Act or the rules made thereunder, any person makes a statement, (a) which is false in any material particulars, knowing it to be false; or (b) which omits any material fact, knowing it to be material, he shall be liable under section 447.

Also, as per section 451 of the Companies Act 2013, punishment is provided for repeated default :

If a company or an officer of a company commits an offence punishable either with fine or with imprisonment and where the same offence is committed for the second or subsequent occasions within a period of three years, then, that company and every officer thereof who is in default shall be punishable with twice the amount of fine for such offence in addition to any imprisonment provided for that offence.

**Professional misconduct as per Company Secretaries Act, 1980:**

Company Secretary in whole time employment and as well as Practicing Company Secretary both are liable for disciplinary action for professional misconduct under provisions of Company Secretaries Act, 1980.

In addition to the penal provisions contained in the Companies Act, 2013, the Institute of Company Secretaries of India (ICSI), has also made penal provision which are contained in Part I of First and Second Schedule of Company Secretaries Act, 1980 which provides the professional misconduct in relation to Company Secretaries in Practice.

Section 21C of the Act provides that where the Disciplinary Committee is of the opinion that a member is guilty of a professional or other misconduct mentioned in the Second Schedule or both the First Schedule and the Second Schedule, it shall afford to the member an opportunity of being heard before making any order against him and may thereafter take any one or more of the following actions, namely:

(a) Reprimand the member;

(b) Remover the name of the member from the Register permanently or for such period, as it thinks fit;

(c) impose such fine as it may think fit, which may extend to Rs 5 lacs.

**CASE LAW**

**Non-Reporting of related party transaction led Secretarial Auditor to pay penalty**

*In the matter of Sun Pharmaceutical Industries Ltd, Adjudication Order passed by RoC Gujarat, Dadra & Nagar Haveli dated 28.04.2023*

**Facts of the case:**

On receipt of whistle blower compliant in respect of Related Party Transaction, money diversion from Sun Pharmaceutical Ltd to Aditya Medisales Ltd and other group companies, the Inquiry of M/s Sun Pharmaceutical Industries Ltd under section 206(4) of the Companies Act, 2013 was ordered by Ministry of Corporate Affairs for FYs 2014 to 2018. During the inquiry it was observed by the inquiry officer that Secretarial Auditor of the company has not reported "Aditya Medisales Ltd.' as related party.

As per section 204 of the Companies Act, 2013 the Secretarial Auditor plays a crucial role in laws for effective compliances. The object of Secretarial Audit is evaluation and form an opinion and to report to the shareholders as to whether, the company has complied with the applicable laws comprising various statutes, rules, regulations, guidelines, followed by board processes also to report on existence of compliance management system.

The Practicing Company Secretary has to examine the transactions during the period of audit to identify whether any fraud element is present in the transaction. Also that, the ICSI has issued Guidance Note for Secretarial Audit. As per the Guidance Note the Secretarial Auditor is need to adhere the checklist to review the related party transaction.

In this matter, the instead of complying his duty as per the Guidance Note in respect of related party transaction u/s 188, the Secretarial Auditor has merely relied on the statutory Auditors' report, which led to non-compliance on his part pertaining to non-reporting of related party transaction.

**Decision:**

After considering the facts and submissions, the adjudicating officer had reasonable cause to believe that the Secretarial Auditor of the company has failed to discharge their duty as per provisions of section 143(14) read with section 188 and 204 of the Companies Act, 2013 read with ICSI Guidance Note on Secretarial Audit issued by ICSI and imposed a penalty on Secretarial Auditor.

## CODE OF CONDUCT

A Code of Conduct is a necessary component of any profession to maintain standards for the individuals within that profession to adhere. It brings about accountability, responsibility and trust to the individuals that the profession serves. A professional needs to constantly live up to its values so that the clients, stakeholders, regulators, fellow professionals and the public at large repose full trust in the profession. The corporate world in which the professionals operate today has become quite demanding and competitive with new regulatory prescriptions each passing day and added emphasis on self-regulation.

Code of Conduct is a set of Principles outlining the responsibilities of, or proper practices with values for, an individual, party or organization.

***"People forget how fast you did a job – but they remember how well you did it"***

***-Howard Newton***

World over, the professions have accorded highest priority to professional ethical standards in the dealings and relationship of professionals with their employers, employees, Government, fellow professionals and the public at large. The fundamental principles which should govern the conduct of a professional with others have been broadly identified as to encompass;

— Integrity;

— Independence;

— Competence;

— Objectivity;

— Ethical behaviour;

— Conformance to the prescribed technical standards; and

— Confidentiality of information acquired in the course of professional work.

Adherence to the Code of Conduct coupled with high level of integrity and ethical behaviour are the hallmark of quality of professional services. Company Secretaries being Secretarial Auditors under the Companies Act, 2013 hold huge responsibilities they serve and influence the investors, employees, customers, suppliers, lenders, government and the society at large.

In order to evoke the necessary interest and awareness among the members and to create the necessary climate for laying down the right type of conduct which should govern the profession, the ICSI organised in February 1976, a National Convention, primarily to evolve the necessary framework for a code of conduct. After the conclusion of that Convention, the Council of the Institute appointed a Code of Conduct Committee with the task of formulating a model code of conduct. The Council of the Institute accepted the recommendations of the Code of Conduct Committee which inter alia prescribed:

(a) rules applicable to all members; and

(b) rules applicable to members in service or in practice.

In formulating the code of conduct, the Committee and the Council adopted a certain normative approach or value judgment. The codes evolved were rooted in the principles of Dharma stating positively what the profession stands for, what it expects from the members and what it cherishes as valued ideals of the society. The code also negatively laid down what constitutes a breach of the code in any given situation and the penal consequences for any violation or misconduct.

The code of conduct acquired statutory status with the conversion of the Institute into a statutory body under the Company Secretaries Act, 1980 ('the Act'), with effect from 1st January, 1981. In the year 2006 substantial amendments were made to Act and also to the First and the Second Schedules to the Act which encompass in detail, various instances of professional misconduct on the part of the members of the Institute in practice as well as in service.

## SCOPE OF SECRETARIAL AUDIT

| ***Examination & Specific Reporting on Compliance under:*** | ***Examination & Specific reporting on Compliance of other laws as may be Applicable specifically to the Company*** | ***Further Reporting*** | ***Further Reporting*** |
|---|---|---|---|
| The Companies Act, 2013 and the Rules made thereunder | E.g. Banks-all laws applicable to banking Industry | Whether there are Adequate systems and processes in the Company commensurate with its size & operation to monitor and ensure compliance with applicable laws including general laws like labour law, environmental laws. | Constitution of Board of Directors |
| Securities Contracts (Regulation) Act, 1956 ('SCRA') and the rules made thereunder | Companies in petroleum sector- All laws applicable to petroleum Industry | | Notices, Agenda and Minutes of Board Meetings etc. |
| Depositories Act, 1996 and the Regulations framed thereunder | | | Board processes |
| Foreign Exchange Management Act, 1999 | | | |
| Regulations and Guidelines under the SEBI Act, 1992 as enlisted in Form MR-3 | | | |
| Secretarial Standards issued by ICSI | | | |
| Listing Agreement entered into by the company with Stock Exchange(s) if any | | | |

The scope of Secretarial Audit comprises verification of the compliances according to the provisions of following enactments, rules, regulations, notifications and guidelines:

(i) The Companies Act, 2013 (the Act) and the Rules made thereunder:

The Act is divided into 29 chapters, 470 sections and VII Schedules. On various matters, Central Government has been empowered to make rules. A perusal of the scheme of the Act makes it clear that compliances under the Act may be divided into two categories. Compliances of the first type are annual and non-event based such as filing of the annual return, annual report including secretarial audit report, wherever applicable, etc. The compliances of second category are event based i.e. on happening of certain event. Secretarial audit envisages the verification of all secretarial records of a company.

(ii) The Securities Contracts (Regulation) Act, 1956 ('SCRA') and the rules made there-under;

(iii) The Depositories Act, 1996 and the Regulations and Bye-laws framed there-under;

(iv) Foreign Exchange Management Act, 1999 and the rules and regulations made there-under to the extent of Foreign Direct Investment, Overseas Direct Investment and External Commercial Borrowings;

(v) The following Regulations and guidelines as prescribed under the Securities Board of India Act, 1992 (SEBI Act):

(a) The Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;

(b) The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015;

(c) The Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018;

(d) The Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014

(e) The Securities and Exchange Board of India (Issue and Listing of Debt Securities) Regulations, 2008;

(f) The Securities and Exchange Board of India (Registrars to an Issue and Share Transfer Agents) Regulations, 1993

(g) The Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2021;

(h) The Securities and Exchange Board of India (Buyback of Securities) Regulations, 2018;

(i) The Securities and Exchange Board of India (Listing Obligations and Disclosures Requirements), Regulations, 2015.

(vi) Mention the other laws as may be applicable specifically to the company Other Applicable Laws include:

Reporting on compliance of 'Other laws as may be applicable specifically to the company' shall mean all the laws which are applicable to specific industry for example for Banks- all laws applicable to Banking Industry; for insurance company-all laws applicable to insurance industry; likewise for a company in petroleum sector; all laws applicable to petroleum industry; similarly for companies in pharmaceutical sector, cement industry etc.

### 'Other areas' which need to be checked

Secretarial Auditor needs to examine and report on the compliance with the applicable clauses of the following:

(i) Secretarial Standards issued by the Institute of Company Secretaries of India.

(ii) The Listing Agreements entered into by the Company with the respective Stock Exchange(s), if applicable;

Secretarial Audit report also requires reporting on whether –

- The Board of Directors of the Company is duly constituted with proper balance of Executive Directors, Non-Executive Directors, Independent Directors, and Women Director.
- The changes in the composition of the Board of Directors that took place during the period under review were carried out in compliance with the provisions of the Act.
- Adequate notice is given to all directors to schedule the Board Meetings, agenda and detailed notes on agenda were sent at least 07 days in advance, and a system exists for seeking and obtaining further information and clarifications on the agenda items before the meeting and for meaningful participation at the meeting.
- Majority decisions are carried through while the dissenting members' views are captured and recorded as part of the minutes.
- There are adequate systems and processes in the company commensurate with the size and operations of the company to monitor and ensure compliance with all applicable laws including general rules like labour laws, competition law, environmental laws, regulations and guidelines.

Secretarial Auditor is required to report and provide details of specific events and actions that occurred during the reporting period having major bearing on the affairs of the company in pursuance of above referred laws/ rules & regulations.

## SECRETARIAL AUDIT – THE PROCESS

Secretarial Audit is a process to check compliance with the provisions of all applicable laws and rules/ regulations/ procedures; adherence to good governance practices with regard to the systems and processes of seeking and obtaining approvals of the Board and/or shareholders, as may be necessary, for the business and activities of the company, carrying out activities in a lawful manner and the maintenance of minutes and records relating to such approvals or decisions and implementation. The secretarial auditor is also expected to express an opinion, after satisfying himself, that there exist adequate systems and processes in the company commensurate with the size and operations of the company to monitor and ensure compliance with applicable laws, rules, regulations and guidelines. The secretarial auditor has to verify whether diverse requirements under applicable laws have been complied with.

### Appointment of Secretarial Auditor

As per Rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014, read with Section 179 of the Companies Act, 2013, secretarial auditor is required to be appointed by means of resolution passed at a duly convened board meeting. Further the appointment shall also be in compliance with the Auditing Standards prescribed by the Institute of Company Secretaries of India.

### Communication to earlier Incumbent

Whenever a company secretary in practice is engaged as a secretarial auditor in place of an earlier incumbent, he shall communicate to the earlier incumbent about the proposed engagement in writing to be sent by registered/ speed post or any other mode of delivery, as may be recognized by the Institute of Company Secretaries of India.

The Council of ICSI at its meeting held on 16th March, 2019 has made amendments in Guidelines wherein for Practice Company Secretaries, communication to previous incumbent would be mandatory before accepting the assignment, in terms of Clause (8) of Part i of the First Schedule to the Company Secretaries Act, 1980. The Council has approved some services in respect of which it shall be mandatory to communicate to the previous incumbent (Company Secretary) before accepting the assignment in terms of terms of clause (8) of part I of the First Schedule to the Company Secretaries Act, 1980, which includes the Issuance of Secretarial Audit Report in terms of Section 204 of the Companies Act, 2013 and Issue of Secretarial Audit Report to material unlisted subsidiaries of Listed entities (whose equity shares are listed) under Regulation 24A of SEBI (LODR) Regulations, 2015.

### Acceptance of Appointment

A formal letter for appointment should be issued by the company to the secretarial auditor along with the copy of the board resolution for appointment. The secretarial auditor should confirm acceptance of appointment in writing.

### Preliminary Discussions/Surveys

It is important to have relevant information about the company. The secretarial auditor is expected to take general overview of the obtain of the company and interact with the personnel involved to know about the nature of the business. He may opt for surveys for generating information about the company.

### Preliminary Meeting

The preliminary meeting with the senior management and the administrative staff involved in the audit will give a fair idea of what is expected and the manner in which audit activities are to be undertaken. At this stage, a time frame of the secretarial audit should be determined and finalized. The secretarial auditor shall discuss the scope and objectives of the audit, gather information on important Board processes, evaluate existing control systems and prepare the audit plan.

### Finalization of Audit Plan and Briefing the Staff

It is important to work out an audit plan. The plan involves briefing the audit staff as to allotment of work, fieldwork responsibilities and other roles. The audit plan should comprehensively outline the fieldwork and usage of auditing tools. The review of controls helps the auditor determine the areas of highest risk and design tests to be performed in the fieldwork section. It is essential that the audit plan adheres to the timelines. Detailed checklist for each aspect of secretarial audit should be prepared and audit staff should be properly sensitized before commencement of audit.

### Testing, Interviews and Analysis

The secretarial auditor may use a variety of tools and technology to gather information about the company's operations. The secretarial auditor should determine whether the controls identified during the preliminary review are operating properly, and in the manner described by the Company.

Fieldwork typically consists of interviewing with staff of the company whether formally or informally, reviewing procedure manuals and processes, testing and analysing compliance with applicable policies and procedures and laws, rules, regulations and assessing the adequacy of controls. This exercise may result in significant findings which the secretarial auditor may bear in mind while preparing the secretarial audit report.

### Working Papers

Working papers are a vital tool of the audit process. They form the basis for expression of the audit opinion. They connect the management's records and information to the auditor's opinion. They are comprehensive and serve many purposes for the company as well as for the Auditor.

### Audit Summary for Discussions

It is recommended that the findings during the course of audit are summarized and presented for initial discussions with the management for their views/ clarifications/replies.

### Submission of Secretarial Audit Report

After considering the clarifications/replies of the management, the secretarial auditor shall prepare the secretarial audit report in Form MR - 3. The report is addressed to the members but is to be submitted to the Board. The report shall contain the opinion on the statutory compliances examined by the auditor and shall state whether in his opinion the Company is carrying out/not carrying out due compliances of the applicable provisions of the various laws. The report shall be provided with or without qualifications.

### Auditing Standards

Secretarial Audit should be conducted in accordance with the Auditing Standard issued by the Institute of Company Secretaries of India.

## IDENTIFICATION AND SEGREGATION OF APPLICABLE LAWS

**SECRETARIAL AUDIT – TO ENSURE COMPLIANCE OF SPECIFIC LAWS AND GENERAL LAWS**

The Auditor shall take note of the industry specific laws and other laws as may be applicable to the auditee based on the identification/ segregation by the Management and his own verification.

### Industry specific laws

Identification of all laws applicable to the auditee, as well as industry specific laws and the segregation thereof, is the primary responsibility of the auditee. Auditor's role is to verify that the laws identified and segregated by the management are appropriate and sufficient having regard to the business of the auditee and the auditee should communicate the same to the secretarial auditor. The Auditor shall exercise his professional judgment to verify that the identification and segregation of the laws made by the Management, as may be applicable specifically to the auditee, is correct. In case, the Auditor is not satisfied by the identification and segregation made by the Management, or no such identification and segregation has been made, he should seek explanation from the management to form the opinion and report accordingly.

The Institute of Company Secretaries of India vide communication dated 22nd December, 2014 and 15th May, 2015 has clarified regarding the scope of Secretarial Audit with regard to industry specific and other laws as under:

(1) Reporting on the compliance of 'other laws as may be applicable specifically to the company' include all the laws which are applicable to specific industry, For example, for Banks - all laws applicable to Banking Industry; for insurance companies - all laws applicable to Insurance industry; likewise, for a company in Petroleum sector - all laws applicable to petroleum industry; similarly, for companies in pharmaceutical sector, cement industry, etc. - all laws specifically applicable to them;

(2) Examining and reporting whether the adequate systems and processes are in place to monitor and ensure compliance with general laws like labour laws, competition laws, and environmental laws.

(3) The provisions relating to audit of accounts and financial statement of a company are dealt in the Statutory Audit, and that relating to taxation is dealt in Tax Audit. Hence, the Secretarial Auditor may rely on the reports given by statutory auditors or other designated professionals.

### Applicable Laws

"Other laws as may be applicable specifically to the company" shall mean all the laws, rules and regulations that are applicable specifically to the company. The Secretarial Auditor may take note of all such laws, rules and regulations identified by the management of the company;

For example for Banks - all laws applicable to Banking Industry; for insurance company - all laws applicable to insurance industry; likewise, for a company in petroleum sector - all laws applicable to petroleum industry; similarly, for companies in pharmaceutical sector, cement industry, etc.

### Principles for making such segregation

Segregation of laws applicable on the Company into the industry specific and general is essential for Secretarial Audit. Based on the following factors auditor should verify the correctness of the segregation of the laws:

- Registration with various authorities such as SEZ, Sectoral Regulators, etc.
- Segments such as Manufacturing/ Trading/ Service/ E-commerce and Industry classification thereof
- Status of company such as listed/ unlisted
- Geographic location of registered office, units/ divisions/ plants/ branches, etc.

However, for identification of laws applicable on the company, in addition to above following factors shall also be considered:

- Key financial parameters such as Turnover, Paid-up Share Capital, Net Worth, Borrowings, etc.
- Type/Class of company such as Private, Public, Holding, Subsidiary, Foreign, Nidhi, Producer, Section 8, etc.
- Agreements governing rights, obligations of shareholders such as Joint venture agreements, shareholders agreements etc.
- Number, class and category of employees/ workers such as women, contractual employees, etc.

It is important to note that certain laws which may fall in the category of General Laws may also become specific laws for particular industries.

***Illustrations for various Industries Specific Laws***

*Illustration 1: For a food & beverages manufacturing & processing unit, industry specific laws includes National Food Security Act, 2013, Food Safety and Standard Act, 2006 and State specific laws, if any.*

*Illustration 2: For a Coal Mining company, industry specific laws includes Mines Act, 1952, Indian Explosives Act, 1884, Colliery Control Order, 2000 and rules & regulations made thereunder, Coal Mines Pension Scheme, 1998, Coal Mines Conservation & Development Act, 1974, The Mines Vocational Training Rules, 1966, The Mines Creche Rules, 1961, The Mines Rescue Rules, 1985 etc.*

The Form MR-3 as notified by the MCA under section 204 of the Companies Act, 2013 has provided that the Secretarial Auditor shall report on the status of the compliance of other laws as may be applicable specifically to the company as specified in point No. (vi) of MR-3.

Further the Form MR-3 also provides for further reporting on the status of the compliance along with the comments on the adequacy of the systems and procedures in the company to manage the compliance of the laws, rules, regulations and guidelines applicable to the company under the following paragraph of the report.

*"I/we further report that there are adequate systems and processes in the company commensurate with the size and operations of the company to monitor and ensure compliance with applicable laws, rules, regulations and guidelines."*

This part of the Secretarial Audit report specifically refers to the compliance of the other applicable laws apart from the Laws covered in the Form MR- 3 and Laws specifically applicable to the company.

**Test Yourself:**

**Question:** What is the format of Secretarial Audit Report?

**Answer:** Secretarial Audit Report is required to be provided in the format prescribed in Form MR-3. (Rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014).

**Question:** To Whom Secretarial Audit Report is addressed?

**Answer:** Secretarial Auditor is appointed by the Board of Directors of the Company. However Secretarial Audit Report is addressed to the members of the Company.

## REPORTING OF GENERAL LAWS

As stated above, the Secretarial Auditor should verify and report that adequate system and processes are in place to monitor and ensure compliance with general laws like labour laws, competition law, and environmental laws.

## VERIFICATION OF CORPORATE CONDUCT AND COMPLIANCE OF LAWS

### Identification of Events/ Corporate Actions

The Auditor shall identify events/ corporate actions that took place during the audit period. The identification shall be made by reviewing the website of the regulators, website of the Auditee, statutory records including books and papers, interaction with the Management and in any other appropriate manner.

### Events/ corporate action

A corporate action is an event initiated by a company that brings or could bring an actual change to the working of the company, such as the investment made during the period under audit, change in the borrowing limits, issuance of the securities-equity or debt, appointment of the KMPs, etc., as approved by its board of directors and/or shareholders.

An action based event may be defined as any activity that amends the functioning of an organization and impacts its stakeholders, including Shareholders, both common and preferred, as well as Lenders. These events are generally approved by the company's board of directors or shareholders of the company, some of the examples are given below for reference:

- Events/ actions altering the Charter documents of the company;
- Changes in the Capital structure of the company;
- Change in the Affairs/ Management of the company;
- Change in the Licensing or permission for the business operation of the company;
- Casual Vacancy of statutory auditor/ director/ KMP;
- Borrowing in excess of limits specified in Section 180 of the Companies Act, 2013.

### Identification of Events/Coprorate Events

The Auditor is expected to identify the Corporate Actions from which a compliance requirement may arise. Corporate actions may primarily be identified from the following:-

- Financial statements;
- Agenda and Notes on Agenda of Board/ Committee/ Members' Meetings;
- Minutes of the Board/ Committees/ Members' Meetings;
- Reporting and Filing to the regulators;
- Annual Report;
- Statutory Disclosures on website of the company, website of the Ministry of Corporate Affairs and on any other platform such as Stock Exchange;
- Third party sources which may include registrar and transfer agents, banks, financial auditor, stakeholders etc.

### Verification of Compliance

The Auditor shall verify all event and calendar-based compliances from the Records of the Auditee, database or website of the regulators and other relevant sources.

The Auditor shall use systematic and comprehensive audit checklists for carrying out the audit and verifying the compliance requirements. The Auditor shall compile and validate the checklists for use in the audit process on the basis of information gathered about the Auditee and scope of the audit. It is a useful tool to ensure that no compliance point is missed or omitted while conducting the audit. The audit checklist should provide structure and continuity to an audit. Audit checklists should be reviewed and updated from time to time to meet the scope of audit and its effectiveness.

The Auditor should verify the compliances of applicable laws and rules based on the information gathered by the Auditor.

## BOARD COMPOSITIONS

The Auditor shall verify compliance of the Companies Act, 2013, SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015, Agreement with Lenders/ Investors, Articles of Association and provisions of other Acts/ Rules/ Regulations specific to the industry, Guidelines and Policies of the Government for promotion of particular industry or location-specific industry, board decisions, shareholders decisions, as may be applicable to the Auditee with regard to:

1. **The overall composition of the Board including the minimum and maximum strength of the Board.**

   **Various provisions mandating the Board Composition**

   There are certain companies which are governed by the Specific Acts and legislations, as applicable in addition to the Companies Act, 2013 with certain exemptions, for example., Banking Companies, Insurance Companies, State Financial Corporations, Public Sector Undertakings, in such cases the Auditor shall ensure the Board Composition is as per the requirements of the applicable laws and acts to the Auditee. A few examples of special situations are given below for reference:

   **Illustration 1:** *In case the Auditee is a non-scheduled flight operator, then it will require prior approval from the Ministry of Civil Aviation for the appointment of a new member on its Board.*

   **Illustration 2:** *The board composition in the State Bank of India (SBI) is regulated by the State Bank of India Act, 1955.*

   **Role of Auditor in the verification of Board Composition**

   The Auditor should identify the laws and rules that govern the company and check the compliances of the Board Composition in accordance with those applicable laws and rules. For example, a Banking Company is regulated by the Banking Regulation Act, 1949, therefore, the Auditor should ensure that the Board Composition is in compliance of the Banking Regulation Act, 1949 or any other law specifically applicable to the Auditee in addition to the basic governing laws enumerated under the Companies Act, 2013 or SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

   In case of audit of any nationalized bank, the Auditor should check the Board Composition in line with Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 and Nationalised Bank (Management & Miscellaneous Provisions) Scheme, 1980.

   The Auditor should examine the applicability of the various laws and regulations applicable to the Auditee to verify the requirement of a minimum and maximum number of directors on the Board of the Auditee. In the case of specific categories of companies to which special Acts apply such as the Insurance Act, 1938, the Banking Regulation Act, 1949 and the Electricity Act, 2003, different rules are prescribed w.r.t a minimum and maximum number of the Board of Directors and accordingly the auditor should consider the compliances envisaged under those laws, Articles of Association and arrangements as may be appropriate in the context.

2. **Optimum Combination of the Board include a proportion of executive, non-executive, independent, non-independent, retiring, non-retiring, women and nominee directors.**

   **Various provisions mandating optimum combination**

The optimum combination of the Board should be as per the provisions laid down in various Statutes such as the Companies Act, 2013, the SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015, the Banking Regulation Act, 1949, the Insurance Act, 1938, etc., as may be applicable to the company.

For example, provisions of the Companies Act, 2013 w.r.t. the Board Composition is given as under:

- As per section 149(2), Every Company shall have at least 01 director who stays in India for a total period of not less than 182 days during the financial year.

  Provided that in the case of a newly incorporated company the requirement under this sub-section shall apply proportionately at the end of the financial year in which it is incorporated.

- As per section 149(3), Every Listed Public Company shall have at least one-third of the total number of directors as independent directors and the Central Government may prescribe the minimum number of independent directors in case of any class or classes of public companies.

*Explanation* – for the purposes of this sub-section, any fraction contained in such one-third numbers shall be rounded off as one.

An independent director in relation to a company, means a director other than a managing director or a whole-time director or a nominee director.

As per second Proviso to Section 149(1) read with Rule 3 of The Companies (Appointment and Qualification of Directors) Rules, 2014 of the Companies Act, 2013, the following classes of companies are required to appoint at least 01 Woman Director:

(i) Every Listed Company;

(ii) Every Other Public Company having –

  (a) paid–up share capital of 100 crore Rupees or more; or

  (b) turnover of 300 crore Rupees or more.

For the appointment of Woman Director, paid up share capital or turnover, as the case may be, as on the last date of latest audited financial statements has to be taken into account.

Similarly, Regulation 17 of SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 provides Board Composition as under:

(1) The composition of the Board of Directors of the listed entity shall be as follows:

  (a) Board of Directors shall have an optimum combination of executive and non-executive directors with at least 01-woman director and not less than 50% of the Board of Directors shall comprise of non-executive directors.

  Provided that the Board of Directors of the top 1000 listed entities shall have at least 01 independent woman director.

  (b) Where the Chairperson of the Board of Directors is a non-executive director, at least one-third of the Board of Directors shall comprise independent directors and where the listed entity does not have a regular non-executive Chairperson, at least half of the Board of Directors shall comprise independent directors.

  Provided that where the regular non-executive chairperson is a promoter of the listed entity or is related to any promoter or person occupying management positions at the level of the Board of Directors or at one level below the Board of Directors, at least half of the Board of Directors of the listed entity shall consist of independent directors.

  (c) The Board of Directors of the top 2000 listed entities shall comprise of not less than six directors.

  (d) Where the listed company has outstanding Superior Voting Rights (SR) equity shares, at least half of the Board of Directors shall comprise of independent directors.

**Additional Requirements for NSE Prime Companies**

The National Stock Exchange (NSE) launched 'NSE Prime' in December 2021-a framework that allows listed companied to sign up voluntarily for higher governance standards than what is required under the law.

**Composition:**

- The Board of Directors shall consist of a minimum of 8 directors.
- The Chairperson of the Board of Directors shall not be a relative of the Managing Director or Chief Executive Officer of the NSE Prime Company.
- Where the public shareholding is in excess of 50%, more than half of the Board of Directors shall comprise Independent Directors; and in case of any fractions, the same shall be rounded to the higher number.
- Where the public shareholding is 50% or less, at least half of the Board of Directors shall comprise Independent Directors; and in case of any fractions, the same shall be rounded to the higher number.
- With effect from July 01, 2025, at least 2 directors shall be women, with at least one such Woman Director also being an Independent Director.

**Role of Auditor in the verification of optimum combination**

Laws specifically applicable to the company may also mandate to have optimum combination of directors. The Auditor should also verify the compliance thereof and report deviations, if any.

3. **Eligibility criteria including disqualifications of directors**

**Various provisions mandating qualifications/ disqualification**

The conditions for qualifications/ disqualification of a director prescribed in the Companies Act, 2013 or any other industry specific Act or law, need to be checked while verifying the Board Composition of the company. For example, Section 164 of the Companies Act, 2013 lays down the provisions for disqualifications for the appointment as Director on the board of the company. Further, the Auditor also needs to check the eligibility criteria including disqualifications of the directors as may be prescribed in any other industry specific Act or laws applicable to the company.

4. **Constitution and Composition of Committees of the Board**

**Various provisions mandating Board Committees**

The constitution of various Committees and the terms of reference of the Committees can be as per various regulatory requirements. For example, for banking companies, stipulated Committees shall mean committees constituted in compliance with the Banking Regulation Act, 1949, Circulars issued by the Reserve Bank of India (RBI) and the Government of India (GOI) from time to time.

Other than Banking companies or other specific companies to which special Acts apply, there are certain mandatory committees that are required to be constituted by certain class or classes of companies as per the Companies Act, 2013, SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015 and certain industry/ sector specific laws. Such mandatory committees include:

- Audit Committee
- Nomination and Remuneration Committee
- Stakeholders Relationship Committee
- CSR Committee
- Risk Management Committee (Note: Secretarial Standard - 1 is not applicable as it is not a Board's Committee under the Companies Act, 2013)
- Internal Committee constituted under the POSH Act

### Role of Auditor in verification of Board Committees

The Auditor needs to check whether the constitution of committees, as constituted by the auditee, is as per the laws, act, rules, regulations and standards applicable to the Auditee.

**Preferable Board size as per Proxy Advisors Guidelines**

**Iias**

Iias prefers a Board size of 6-15 members. Board size should be commensurate with the size and operations of the company. Iias believes that, given the nature and quantum of work involved, three directors may not be optimal. Their guidelines are therefore aligned with the Kotak Committee threshold of at least 6 directors. On the other hand, consensus on many critical issues may be difficult to achieve if Board size exceeds 15 members.

Key risks of big Board size highlighted by them include:

- Board size may be increased to accommodate family members.
- Large Board size may make consensus building difficult.

**InGovern**

InGovern prefers a Board size of 7-15 members. A Board size outside of this range is considered less effective either due to low diversity of expertise and opinion, and low representation of Independent Directors on Kay Committees or a big Board size of greater than 15 members present the disadvantages of delayed decision making that come along an uncontrollable size and risk of having majority of promoters and related parties on board, InGovern too is not in favour of huge Board size.

**SES**

SES prefers a Board size of 6-15 members. If the proposed Board size is outside this range, SES expects that the company must provide a rationale for the same.

## BOARD PROCESSES

The Board of directors as an institution plays a prominent role in Corporate Governance. It is responsible for directing and overseeing the business and management of the Company. Given this pivotal role of the board, directors are considered as fiduciaries in that they are required to act in the interest of various constituencies in a Company such as shareholders and other stakeholders. Accordingly, the law foists on the directors duties and liabilities as instruments that modulate their conduct.

Directors are, however, entitled to various protective measures in the form of mitigating factors either conferred upon them by law or through practical mechanisms they may establish. The Section 118(10) mandates on every company to observe the Secretarial Standards on the meeting of the Board of Directors (SS-1) as specified by the Institute of Company Secretaries of India (ICSI).

The SS-1 helps in providing clarity in certain areas where the law is either silent or ambiguous. Wherever the law is silent, certain good governance practices have been recommended and where it is ambiguous, the standards try to bring in more clarity and adhere the common board processes across country.

### CASE LAW

**RoC imposes penalty on company, directors and company secretary for Non-compliance of SS-1**

In the matter of M/s Polaris India Private Limited (ROC /D/ADJ Order /118(10)/ Polaris/ 328 to 333) adjudication order by the Registrar of Companies, NCT of Delhi & Haryana on 19th January 2022. The company was under obligation to comply with the Secretarial Standard -1 relating to meetings of the board of directors issued by the Institute of Company Secretaries of India which inter alia requires that the company shall hold at least four meetings of its board in each calendar year with a maximum interval of one and hundred and twenty days.

The company has failed to comply with Secretarial Standard – 1 in respect of holding at least four meetings of its board as well as the gap between board meetings. Upon realizing the default / non-compliance committed by the company, the company has *suo-moto filed an application via e-form GNL-1 for adjudication of penalty.*

Accordingly, Registrar of Companies, upon receipt of the application for adjudication received from the company, in the interest of natural justice, before imposing the penalty on the company, its directors who is in default, or any other person, as the case may be, a reasonable opportunity of being heard was given to them by issuing a notice for personal hearing. On the day of the personal hearing, the Company secretary of the company appeared before the authorities on behalf of the company and its directors / officers and explained that the defaults are of technical nature, which were committed inadvertently and without any mala-fide intentions.

The Registrar of Companies / Adjudicating Officer, in the exercise of the powers conferred on him and having considered the facts and circumstances of the case besides written and oral submissions, imposed penalty on the company and its officers including the Company Secretary amounting to Rs. 1.60 Lacs in total.

To ensure the effective board processes, the auditors shall verify that the decisions of the Board and its Committees are taken and recorded in compliance with applicable laws, rules, regulations, guidelines, standards and defined internal processes, if any.

### Various provisions mandating Board Processes

Provisions w.r.t Board processes may include:

- Meetings of Board and Committees
- Meetings of Committees that exercise powers of the Board under Section 179 of Companies Act, 2013
- Meeting of Members
- Board's performance evaluation and training
- Appointment and Resignation of the members of the Board.

### Role of Auditor in the verification of Board Processes

The Auditor shall verify notice of the meetings, minutes, and supporting records, including the agenda, to satisfy himself whether the Auditee has complied with the applicable laws, rules, regulations, guidelines, standards and defined internal processes (defined internal processes to be explained). Many corporates have manuals for Board Processes, in such cases, the Auditor should verify whether the Auditee has complied with the policy and processes laid down in the manual of the Auditee.

Deviations, if any, observed during the course of audit from the policies and processes laid down in the manual adopted by the Board.

Directors, collectively called Board of Directors, in fulfilling the fiduciary objectives need to ensure that the company adheres to transparent, ethical and responsible governance of the company. It is, therefore, important that the Board processes of the company are robust. The board process refers to the processes followed for decision making by the Board and its committees. They can be broadly divided into two parts namely: -

1. Part A – Board Structure
2. Part B – Board Systems and Procedures

### CASE STUDY

Mr. CS is appointed as a Company Secretary of Flowers Pvt Ltd. Mr. CS have to conduct the audit for the financial year 2022-23. Mr. CS is required to draft the guidelines for verification of Board Composition & Board Process as per the CSAS-4 (Auditing Standard on Secretarial Audit).

**Board Composition the auditor shall verify:**

1. Overall composition of the Board including the minimum and maximum strength of the Board as per provisions of the Companies Act, 2013, SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015, Articles of Association and provisions of other Acts/rules/regulations as may be applicable to the Company.
2. Optimum combination of Executive, Non-executive, Independent, Non-independent, retiring, non-retiring, woman, nominee in the Board as per provisions of the Companies Act, 2013, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, Articles of Association, agreement with Lenders/Investors and provisions of other Acts/rules/regulations as may be applicable to the company.
3. Eligibility criteria including qualifications of Directors in accordance with the provisions/principles laid down in the Companies Act, 2013, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, Articles of Association and provisions of other Acts/rules/regulations as may be applicable on the Company.
4. The constitution and composition of Committees of the Board.

**Board Processes:**

The Auditor shall verify that the decisions of the Board and its Committees are taken and recorded in compliance with applicable laws, rules, regulations, guidelines, standards and defined internal processes, if any. In case of conflict between various provisions the stricter compliance to be verified.

## SYSTEM AND PROCESS

System and process broadly refer to the framework of legal and procedural compliances of the Auditee including but not limited to internal regulations, control, guidance and governance.

**Meaning of systems and processes**

A system is the core element, that company management has and/or implements in its business. It's something that helps the business run. The processes are all the things that company management do in order to make any given system work most efficiently. In other words, systems are designed to connect all of an organization's intricate parts and interrelated steps to work together for the achievement of the business strategy. System and process in the context of Secretarial Audit includes internal policies, decisions or procedures, etc. laid down by the Auditee for ensuring the compliance of the various laws, rules, standards and guidelines as may be applicable to the company. The Auditor should verify those policies, decisions, procedures, etc. of the Auditee to verify the adherence thereof and ascertain that the systems and processes are adequate and commensurate to its size and operations to ensure compliance with applicable laws, rules, regulations, standards, guidelines and defined internal processes.

The Auditor shall assess the efficacy and adequacy of the system and processes of the Auditee commensurate with its size and operation for verifying compliance of applicable laws, rules, regulations, standards, guidelines, and defined internal processes, if any by:

- Reviewing records maintained by the Auditee.
- Understanding compliance responsibility centers, control points, matrix, the flow of information, escalation of non-compliances to different levels, reporting of any non-compliance.
- Assessing compliance mechanism and understanding its extent, coverage and severity mapping. The Auditor shall also assess compliance manual/ standard operating procedures, if any, available with the Auditee.
- Analysing instances of show cause notices received, prosecution initiated, fine or penalties levied, imprisonment ordered, qualification, adverse remark or observations in the statutory, internal or industry specific audit, orders passed by regulatory bodies or judicial/ quasi-judicial authorities.

***Illustrations:***

*Below mentioned companies are observing certain best practices for Board Processes (2022):*

1. **Bharti Airtel Limited**

   *- The company submits audited quarterly results to the Stock Exchange.*

   *- Separate meeting of Independent Directors on a quarterly basis.*

   *- The evaluation of the Board of Directors is done by an external agency*

   *- Linkage of remuneration of MD & CEO and Senior Management with ESG/sustainability targets.*

2. **Hindustan Unilever Limited**

   *The Board of directors has adopted 'Corporate Governance Code' a statement of practices and procedures to be followed by the company and its officers and employees.*

3. **Mahindra Logistics Limited**

   *- The company has voluntarily adopted the practice of scheduling its AGM within 5 month of end of financial year as a god governance measure.*

   *- The company, voluntarily as a good governance practice, observes a 'silent/quiet period' for 15 days prior to the announcement of quarterly and annual financial results.*

   *- The company has structured system-based PAN India compliance mechanism, with process management and end-to-end visibility for its compliance process.*

4. **AU Small Finance Bank Limited**

   *The Executive Directors are duty bond with Malus and Claw back clause, which activates in the event of subdues or negative financial performance of the Bank.*

**Companies in India that have historically been recognized for good corporate governance practices:**

**Tata Group:** Tata Group is known for its strong corporate governance practices. It has a diverse board, with independent directors playing a significant role in decision-making processes.

**Infosys:** Infosys has been recognized for its transparent board processes and proactive engagement with shareholders. The company regularly updates stakeholders on its performance and strategic initiatives.

**Reliance Industries Limited:** Reliance has made efforts to enhance its corporate governance framework in recent years. The company has a well-structured board and has implemented several best practices recommended by regulatory authorities.

**HDFC Bank:** HDFC Bank has been praised for its robust risk management practices and transparent communication with stakeholders. The bank's board comprises experienced professionals with diverse backgrounds.

**Wipro:** Wipro has focused on strengthening its corporate governance practices to align with global standards. The company has a comprehensive code of conduct and ethics and emphasizes accountability at all levels.

## DETECTION OF FRAUD

The Auditor shall exercise professional judgment and maintain professional scepticism throughout the planning and performance of the audit to detect and report the fraud envisaged under the provisions of Section 143(12) of the Companies Act, 2013 read with Companies (Audit and Auditors) Rules, 2014. A fraud may impact the organization adversely in monetary or other terms. The Auditor shall report the fraud, if the same has been observed by him during the course of audit.

Here, *professional scepticism* means, an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence.

Professional scepticism includes being alert to, for example:

- Audit evidence that contradicts other audit evidence obtained.
- Information that brings into question the reliability of documents and inquiries to be used as audit evidence.

*Professional Judgement* means, the application of the accumulated knowledge and experience gained through a relevant accounting or auditing training, by making use of the ethical standards, resulting in making informed decisions about the courses of action that are appropriate in specific circumstances.

The Auditor shall check whether the company has any anti-corruption and/or anti-bribery policy, ethics policy which may be in place at the Company. During the course of the audit, if the Auditor suspects commission of any fraud, he shall endeavour to collect further evidence for the same. The suspicion may arise on perusal of internal control systems, complaint under whistle blower mechanism and reports of the other auditors, etc.

'*Suspicion*' is a state of mind more definite than speculation, but falls short of knowledge based on evidence. It must be based on some evidence, even if that evidence is tentative – simple speculation that a person may be engaged in fraud is not sufficient grounds to form a suspicion. Suspicion is a slight opinion but without sufficient evidence.

- Examples of information which could be classified as suspicion are provided below: Recurring negative cash flows from operations or an inability to generate cash flows from operations while reporting earnings and earnings growth.
- The practice by management in maintaining or increasing the entity's stock price or earnings trend.

The Auditor may communicate directly with the internal auditors and statutory auditors to verify whether they have suspected/identified any fraud during the course of their audit. The Auditor shall ensure to collect sufficient evidence which substantiates his suspicion of the commission of the fraud against the Auditee by its employees and officers.

During the course of the audit, if the auditor suspects any commission of fraud, he shall endeavour to collect further evidence for the same. The suspicion may arise on perusal of internal control systems, perusal of any complaints under whistle blower mechanism, reports of the other auditors, etc.

The auditor shall ensure to collect sufficient evidence which substantiates his suspicion of the commission of the fraud against the Company by the employees and officers of the company. The auditor shall ensure that he has sufficient reason to believe that there is commission of fraud and should have justifiable grounds for the same.

## Transaction which may involve the fraud

In the past, "Fraud" has been noticed in many cases of scams in the following kinds of transactions:-

- **Related Party Transactions**

**CASE STUDY**

1. Poly Pack - British Textile company – diverted funds to related companies through 88 separate deals, mostly companies owned by his son and relatives - led to enactment of the Code of Corporate Governance in UK.
2. Lehman Brothers – One of the largest global financial services company in USA – Attempted to show rosy financial statements through a series of re-purchase contracts with related parties at artificial prize.

3. Satyam computer services –MD and CEO Mr. Ramalinga Raju put through RPT transactions to the tune of $ 1.6 billion to Maytas Properties and Maytas Infrastructure, companies predominantly owned and managed by his sons.

4. **Sun Pharmaceutical Industries Limited (2019):** Sun Pharma, India's largest pharmaceutical company, came under investigation by SEBI for alleged corporate governance lapses, including related party transactions. SEBI examined transactions involving Sun Pharma's co-promoter, Sudhir Valia, and his brother-in-law, Dilip Shanghvi (founder of Sun Pharma), related to certain real estate deals.

5. **Infrastructure Leasing & Financial Services (IL&FS) (2018):** IL&FS, a major infrastructure financing and development company, collapsed due to a liquidity crisis and allegations of mismanagement. The company's board was accused of approving numerous related party transactions without adequate disclosure or scrutiny. The IL&FS case led to significant regulatory reforms in India's corporate governance framework.

6. **Kingfisher Airlines (2012):** Vijay Mallya, the chairman of Kingfisher Airlines, faced allegations of financial irregularities, including questionable related party transactions. The airline, which eventually collapsed under a mountain of debt, was accused of providing loans and guarantees to companies associated with Mallya and his family.

- **Excessive Managerial Remuneration**

**CASE STUDY**

1. Tyco – (USA) – CEO Dennis drew $600 million excess compensation and spent $2 million on his wife's birthday party at company's expense.

2. Global Crossings - Four CEO's drew $23 million each from the company and later removed such liabilities through write of driving the company to bankruptcy.

3. **Infosys (2017):** Infosys, one of India's leading IT services companies, faced shareholder criticism over the high severance pay awarded to its former CFO, Rajiv Bansal, in 2015. The severance package amounted to approximately ₹17.38 crore (around $2.5 million USD), raising concerns about governance and transparency.

4. **Tata Motors (2016): In 2016,** Tata Motors faced shareholder dissent over the compensation package of its former CEO and Managing Director, Cyrus Mistry. Mistry's remuneration, which included a significant severance payout upon his removal from the position, drew scrutiny from investors and governance experts.

5. **Wipro (2019):** Wipro, another major Indian IT services company, faced shareholder dissent over the proposed remuneration package of its CEO, Abidali Neemuchwala, in 2019. Shareholders raised concerns about the size of Neemuchwala's compensation and its alignment with company performance.

- **Insider Trading**

**CASE STUDY**

1. ENRON – Largest American energy company. Fortune-100 named ENRON "America's Most Innovative Company" for six consecutive years. Kenneth Lay CEO and his wife Linda sold all the shares held by them in the company worth $ 90 million @ $ 90 per share. After CEO's wife completed sale of all shares between 10 am and 10.20 am, share price crashed less than a dollar around 10.30 am due to announcement of filing under chapter 11 for bankruptcy.

2. Galleon – Raj Rajarathnam obtained inside information from Rajath Gupta, a member of the Board of Goldman Sachs that Warren Buffet's Berkshire Hathaway was going to make a crucial investment in Goldman Sachs. Raj Rajarathnam was convicted to pay fine $ 92.8 million and sentenced to 11 years imprisonment.

3. **Martha Stewart (2001):** The lifestyle guru was convicted in 2004 for insider trading related to the sale of ImClone Systems shares. Stewart sold her shares after receiving insider information from her broker about the FDA's rejection of ImClone's cancer drug.

4. **SAC Capital Advisors (2013):** SAC Capital, a hedge fund founded by Steven Cohen, pleaded guilty to insider trading charges in 2013. The firm agreed to pay $1.8 billion in penalties.

- Inter Company transactions
- Mergers/demergers/acquisitions
- IPO frauds

Other means of Corporate fraud are the inadequate disclosures, false or misleading information, theft of assets, false expenses, corruption, theft in formation, fraudulent applications, misuse of assets, dishonest business partners, fraudulent billing.

*These areas are not exhaustive but only some examples are given so as to guide fraud detection.*

## REPORTING OF FRAUD

Secretarial Auditor in the course of performance of his duties as auditor it has reason to believe that an offence involving fraud is being committed or has been committed against the Company by its officers/employees needs to report the fraud. A very significant duty has been cast on the Company Secretary in Practice under section 143 (12) of the Companies Act, 2013. It provides that if the Company Secretary in Practice, in the course of the performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government. As per section 143(12):

***"Notwithstanding anything contained in this section, if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amounts as may be prescribed, is being or has been committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as may be prescribed:***

***Provided that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under section 177 or to the Board in other cases within such time and in such manner as may be prescribed:***

***Provided further that the companies, whose auditors have reported frauds under this sub-section to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed."***

A very significant duty has been cast on the Company Secretary in Practice under section 143 (12) of the Companies Act, 2013. It provides that if the Company Secretary in Practice, in the course of the performance of his duties as auditor, has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government, or to the Audit Committee or the Board.

### Duty of Report Fraud to Central Government

The section 143(12) read with the Companies (Audit and Auditors) Rules, 2014 provides that if an auditor of a company in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employee, the auditor shall report the matter to the Central Government.

## Duty of Report Fraud to Audit Committee/ Board

In case of a fraud involving lesser than rupees one crore, the auditor shall report the matter to audit committee or to the board 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.

## Disclosures in the Board's Report

The following details of each of the fraud reported to the Audit Committee or the Board during the year to be disclosed 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.

## Consequence on failure in Reporting of fraud

In case, Company Secretary in Practice does not comply with the provisions of section 143(12), he shall be punishable with fine which shall be liable to a penalty of five lakh rupees in case of a listed company, and one lakh rupees in case of any other company [section 143(15)]. Further, section 143(13) provides that no duty to which an auditor of a company is subject to shall be regarded as having been contravened by reason of his reporting the matter (fraud) if it is done in good faith.

**Who is considered as an Auditor for Fraud Reporting?**

The auditor includes the-

- Statutory Auditors of the company appointed under section 139 of the Companies Act, 2013;
- Company Secretary in Practice conducting Secretarial Audit under section 204 of the Companies Act, 2013;
- Cost Accountant in practice conducting Cost Audit under section 148 of the Companies Act, 2013 and the Branch Auditors referred to in section 143(8) of the Companies Act, 2013.

However, the Internal Auditor or such other professionals appointed under any other statutes rendering other services to the company such as a tax auditor appointed under Income Tax Act, GST auditors appointed under the respective GST legislations are not covered under section 143 of the Companies Act, 2013.

**CASE STUDY**

M/s ABC & Co., Practicing Company Secretaries were the Secretarial Auditors of Opoco Ltd. During the secretarial audit, the Secretarial Auditor was verifying the board approvals and other documentation for the loan taken by the Company and they found that a fraud of Rs. 3.5 crores was committed against the Company, by its officers which was not observed by the Statutory Auditors of the Company. In this background, below mentioned are the duties and responsibilities of Secretarial Auditors under the Companies Act, 2013.

The obligations and duties of the Secretarial Auditors in the mentioned case under Companies Act, 2013 are as provided under rule 13 of the Companies (Audit and Auditors) Rules, 2014:

If an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government as under:

- the auditor shall report the matter to the Board of Directors or the Audit Committee, as the case may be, immediately but not later than two days of his knowledge of the fraud, seeking their reply or observations within forty-five days.
- on receipt of such reply or observations, the auditor shall forward his report and the reply or observations of the Board of Directors 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 fifteen days from the date of receipt of such reply or observations;
- in case the auditor fails to get any reply or observations from the Board or the Audit Committee within the stipulated period of forty-five 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;
- the report shall be sent to the Secretary, Ministry of Corporate Affairs in a sealed cover by Registered Post with Acknowledgement Due or by Speed Post followed by an e-mail in confirmation of the same;
- the report shall be in the form of a statement as specified in Form ADT-4;
- as per Sec 143(15), any non-compliance of this duty by any auditor, cost accountant, or company secretary in practice, attracts penalty, which shall be-
  (a) in case of a listed company five lakh rupees; and
  (b) in case of any other company one lakh rupees.

**Difficulties in estimating the quantum of fraud**

By and large the Auditor including the Secretarial Auditor goes by the estimates or reasonable range provided by the management for the purpose of estimating the quantum of the fraud amount and reporting. Depending upon the complexity and duration of the fraud, at times it could be difficult for the auditing personnel to determine the quantum of fraud and loss suffered. In the event, after some time, it is discovered that the quantum of fraud has exceeded the threshold limit of one crore, then subsequent reporting may be required and thus the Secretarial Auditor may have to report to the Central Government within 45 days of the determination of the revised fraud estimate or loss which crossed one crore limit. In view of the above, the estimation of the amount of fraud is very critical and if the estimation goes wrong even after taking reasonable care, then it will impact the decision whether to report to the concerned Authorities or otherwise. Since the provision says that in case of fraud exceeding one crore is only required to be reported to Central Government and fraud involving less than a crore is required to be reported only to Audit Committee / Board. Hence, the secretarial auditor is required take extreme care in estimating the quantum of fraud.

**Very interesting question at this juncture**

One question arises in the mind as to whether regulatory non-compliance would come under the purview of fraud reporting. It may be noted that as per Ministry of Corporate Affairs notification there is no distinction between fraud and regulatory non-compliance as long as the quantum of fraud loss can be reasonably quantified due to regulatory non-compliance. Again, there would be difficulty for the Secretarial Auditor to determine the quantum of fraud if the fraud is arising under regulatory non-compliance. Where the secretarial auditor discovers instances involving bribery, money laundering, corruption or other regulatory non-compliance committed by either by the company or its employees or its management, then the secretarial auditor is duty bound to communicate the same to the Audit Committee / Board and depending upon the quantum he is also required to report to the Central Government if the determination of fraud exceeds the threshold limit of one crore.

## PROCEDURE FOR REPORTING OF FRAUD

**(i) Reporting of frauds by auditor involving amount more than Rs. 1 crore**

If an auditor of a company, in the course of the performance of his duties as statutory auditor, has reason to believe that an offence of fraud, which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employees, the auditor shall report the matter to the Central Government. Auditor should report such frauds as soon as possible but not later than 60 days of his knowledge about the frauds:

**STEP-I - Report to Board & Audit Committee**

Auditor shall forward his report to the board of directors or the audit committee, as the case maybe, within 2 days of his knowledge of the fraud, seeking their reply or observations within 45 (forty-five) days;

**STEP-II - Report to Central Government after reply of board**

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 fifteen days of receipt of such reply or observations;

**STEP-IIA - Report to Central Government if no reply received**

In case the auditor fails to get any reply or observations from the board or the audit committee within the stipulated period of forty-five 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 failed to receive any reply or observations within the stipulated time.

**(ii) Reporting of frauds by auditor involving amount less than Rs. 1 crore**

As per the Sub-rule (3) of Rule 13 of the Companies (Audit and Auditors) Rules, 2014 in case of fraud involving an amount less than Rs. 1 Crore, the auditor shall report the matter of fraud to the audit committee or to the board within 2 days of his knowledge of the fraud.

The report should specify the nature of the fraud with description, approximate amount of the fraud and parties involved in the fraud.

In such case, as per sub-rule (4), the Board shall disclose in its report (Board's Report) the nature of fraud with description, approximate amount of the fraud, parties involved in the fraud and remedial action taken. Name of parties should be disclosed only when the board or audit committee has not taken any remedial action against the fraud.

### CASE LAW

Fraud detection and reporting requires the practicing company secretary to focus beyond compliance

In the matter of *Globe Motors Limited v. Mehta Teja Singh & Company,* the Delhi High court observed that although an agreement in which a director was interested could not said to be invalid in view of compliance with the requirements of the Act, yet it is only a formal aspect of compliance with the statutory provisions; the basic question is as to the conduct of the director and whether it satisfies the test considering their fiduciary relationship to the company. Justice Sachar further observed that the directors are expected to display utmost good faith towards the company in their dealings with the company or on behalf of the company; they should not use the company's money or other property or information or other matters in their possession in order to gain any advantage to themselves. Therefore, a practicing company secretary should not be satisfied only with compliance during secretarial audit. He needs to look beyond and satisfy himself that the transactions which have taken place during audit period do not contain any fraud element.

## FRAUD V/S NON-COMPLIANCE

The term fraud can be defined as act or course of deception, an intentional concealment, omission, or perversion of truth, to-

1. gain unlawful or unfair advantage,
2. induce another to part with some valuable item or surrender a legal right, or
3. inflict injury in some manner.

Wilful fraud is a criminal offense which calls for severe penalties, and its prosecution and punishment. However, incompetence or negligence in managing a business or even a reckless waste of firm's assets (for example by speculating on the stock market) does not normally constitute a fraud.

**Non-Compliance:**

The term non-compliance refers to failure to comply with the laws, rules regulations etc., the term non-compliance is commonly used in regard to a failure to meet the compliance requirements or failure to doing compliance be it the failure in following procedures, filing of information, eligibility conditions, reporting etc.

The relationship between Fraud and non-compliance can be constructed as the non-compliance in the company may lead to a fraud, however it may also be noted that the fraud can also be made in the compliant company.

## IDENTIFICATION AND REPORTING OF THE EVENTS/ACTIONS HAVING MAJOR BEARING ON AUDITEE'S AFFAIRS

The Secretarial Auditor shall identify and report all events/actions having major bearing on the Company's affairs/ Governance in pursuance of the applicable laws, rules, regulations, guidelines, standards, etc. It shall be the duty of the Auditor to identify and report all events/actions having major bearing on the Company's affairs. An event/action may be considered as having major bearing on Company's affairs includes the following situations:

**Events having a major bearing on Auditee's Affairs**

1. The Auditor shall assess and identify the material action or events having bearing on the Auditee's affairs in pursuance of the applicable laws, act, rules, regulations, guidelines, standards, etc. and report accordingly.
2. The identification of the corporate actions or events having bearing on the Auditee's affairs in terms of applicable laws, act, rules, regulations, guidelines, standards, etc. is a subjective matter and needs to be concluded keeping in mind various parameters. Such parameters may include the following:
    a. The consideration involved in the transaction as a percentage of the consolidated turnover, net worth or profit;
    b. The transaction whether or not in the ordinary course of business;
    c. The transaction representing a significant shift from the company's strategy;
    d. The omission of an event or information is likely to result in significant market reaction if the said omission came to light at a later date.
3. Further, following are indicative actions and/or events may be considered to have a bearing on the Auditee's affairs:
    a. Future plans of Merger or Amalgamation.
    b. Revision in Rating(s).

c. Fraud/ defaults by promoter or key managerial personnel or by listed entity or arrest of key managerial personnel or promoter.

d. Agreements [viz. shareholder agreement(s), joint venture agreement(s), family settlement agreement(s) (to the extent that it impacts management and control of the listed entity), agreement(s)/ contract(s) with media companies)], which are binding and not in normal course of business, revision(s) or amendment(s) and termination(s) thereof.

e. Corporate Debt Restructuring.

4. The Auditor shall disclose the material non-compliances and transactions as observed during the course of Audit.

**Further, the SEBI (LODR) Regulations, 2015 include the following events which are considered as having bearing on affairs of the company:**

1. default in timely payment of interests/preference dividend or redemption or repayment amount or both in respect of the non-convertible debt securities and non-convertible redeemable preference shares and also default in creation of security for debentures as soon as the same becomes apparent;
2. any attachment or prohibitory orders restraining the company from transferring non-convertible securities from the account of the registered holders along-with the particulars of the numbers of securities so affected, the names of the registered holders and their demat account details;
3. any action which shall result in the redemption, conversion, cancellation, retirement in whole or in part of any non-convertible securities;
4. any action that shall affect adversely payment of interest on non-convertible debt securities or payment of dividend on non-convertible redeemable preference shares including default by issuer to pay interest on non-convertible debt securities or redemption amount and failure to create a charge on the assets;
5. any change in the form or nature of any of its non-convertible debt securities or non-convertible securities that are listed on the stock exchange(s) or in the rights or privileges of the holders thereof and make an application for listing of the securities as changed, if the stock exchange(s) so require;
6. any changes in the general character or nature of business/activities, disruption of operation due to natural calamity, and commencement of commercial production/commercial operations;
7. any events such as strikes and lock outs which have a bearing on the interest payment/dividend payment/ principal repayment capacity;
8. details of any letter or comments made by debenture trustees regarding payment/non-payment of interest on due dates, payment/non-payment of principal on the due dates or any other matter concerning the security, listed entity and/or the assets along with its comments thereon, if any;
9. delay/default in payment of interest or dividend/principal amount/redemption for a period of more than three months from the due date;
10. failure to create charge on the assets within the stipulated time period;
11. any instance(s) of default/delay in timely repayment of interests or principal obligations or both in respect of the debt securities including, any proposal for re-scheduling or postponement of the repayment programmes of the dues/debts of the Company with any investor(s)/lender(s). Explanation. - For the purpose of this sub-para, 'default' shall mean non-payment of interest or principal amount in full on the pre-agreed date and shall be recognized at the first instance of delay in servicing of any interest or principal on debt.

12. any major change in composition of its board of directors, which may amount to change in control as defined in Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;

13. any revision in the rating;

14. the following approvals by board of directors in their meeting:-

    (a) the decision to pass any interest payment;

    (b) short particulars of any increase of capital whether by issue of bonus securities through capitalization, or by way of right securities to be offered to the debt security holders, or in any other way;

15. all the information, report, notices, call letters, circulars, proceedings, etc. concerning non-convertible debt securities;

16. fraud/defaults by promoter or key managerial personnel or director or employees of listed entity or by listed entity or arrest of key managerial personnel or promoter.

## IMPACT OF AUDIT REPORT

Secretarial Audit helps the investors in taking informed investment decision, as it evaluates the company in terms of compliance and governance norms being followed by the company. It is an effective due diligence exercise for the prospective investors or joint venture partners.

Secretarial Audit facilitates monitoring compliances with the requirements of law through a formal compliance management programme which can produce positive results to the stakeholders of a company.

The Secretarial Audit Report should be prepared in accordance with the Auditing Standards issued by the Institute of Company Secretaries of India and be signed by the Secretarial Auditor who has been engaged by the company to conduct the Secretarial Audit and in case of a firm of Company Secretaries, by the partner under whose supervision the Secretarial Audit was conducted.

- An effective mechanism to make sure of the compliance with the legal and procedural Requirements.
- Provides a level of confidence to the directors & Key Managerial Personnel etc.
- Secretarial Audit ensures legal and procedural requirements so directors can concentrate on important business matters.
- Strengthen the goodwill of a company for their regulators and stakeholders.
- Secretarial Audit is an effective governance and compliance risk management tool.
- It helps the investor in analysing the compliance level of companies, thereby increases the reputation.

## Annexure -A

**FORM NO. MR-3**

**SECRETARIAL AUDIT REPORT**

**FOR THE FINANCIAL YEAR ENDED __________**

[Pursuant to section 204(1) of the Companies Act, 2013 and rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014]

To,

The Members,

............. Limited

I/We have conducted the secretarial audit of the compliance of applicable statutory provisions and the adherence to good corporate practices by....... (name of the company).(hereinafter called the company). Secretarial Audit was conducted in a manner that provided me/us a reasonable basis for evaluating the corporate conducts/ statutory compliances and expressing my opinion thereon.

Based on my/our verification of the .................................... (name of the company's) books, papers, minute books, forms and returns filed and other records maintained by the company and also the information provided by the Company, its officers, agents and authorized representatives during the conduct of secretarial audit, I/We hereby report that in my/our opinion, the company has, during the audit period covering the financial year ended on, complied with the statutory provisions listed hereunder and also that the Company has proper Board-processes and compliance mechanism in place to the extent, in the manner and subject to the reporting made hereinafter:

I/we have examined the books, papers, minute books, forms and returns filed and other records maintained by .............. ("the Company") for the financial year ended on, according to the provisions of:

(i) The Companies Act, 2013 (the Act) and the rules made thereunder;

(ii) The Securities Contracts (Regulation) Act, 1956 ('SCRA') and the rules made thereunder;

(iii) The Depositories Act, 1996 and the Regulations and Bye-laws framed thereunder;

(iv) The Foreign Exchange Management Act, 1999 and the rules and regulations made thereunder to the extent of Foreign Direct Investment, Overseas Direct Investment and External Commercial Borrowings;

(v) The following Regulations and Guidelines prescribed under the Securities and Exchange Board of India Act, 1992 ('SEBI Act'):

   (a) The Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;

   (b) The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992;

   (c) The Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;

   (d) The Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999;

   (e) The Securities and Exchange Board of India (Issue and Listing of Debt Securities) Regulations, 2008;

   (f) The Securities and Exchange Board of India (Registrars to an Issue and Share Transfer Agents) Regulations, 1993 regarding the Companies Act and dealing with client;

   (g) The Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009; and

   (h) The Securities and Exchange Board of India (Buyback of Securities) Regulations, 1998.

(vi) ............................................ (Mention the other laws as may be applicable specifically to the company)

I/we have also examined compliance with the applicable clauses of the following:

(i) Secretarial Standards issued by The Institute of Company Secretaries of India.

(ii) The Listing Agreements entered into by the Company with ..... Stock Exchange(s), if applicable;

During the period under review the Company has complied with the provisions of the Act, Rules, Regulations, Guidelines, Standards, etc. mentioned above subject to the following observations:

*Note*: Please report specific non-compliances / observations / audit qualification, reservation or adverse remarks in respect of the above para wise.

I/we further report that :

The Board of Directors of the Company is duly constituted with proper balance of Executive Directors, Non-Executive Directors and Independent Directors. The changes in the composition of the Board of Directors that took place during the period under review were carried out in compliance with the provisions of the Act.

Adequate notice is given to all directors to schedule the Board Meetings, agenda and detailed notes on agenda were sent at least seven days in advance, and a system exists for seeking and obtaining further information and clarifications on the agenda items before the meeting and for meaningful participation at the meeting.

Majority decision is carried through while the dissenting members' views are captured and recorded as part of the minutes.

I/we further report that there are adequate systems and processes in the company commensurate with the size and operations of the company to monitor and ensure compliance with applicable laws, rules, regulations and guidelines.

**Note:** Please report specific observations / qualification, reservation or adverse remarks in respect of the Board Structures/system and processes relating to the Audit period.

I/we further report that during the audit period the company has................................

(Give details of specific events / actions having a major bearing on the company's affairs in pursuance of the above referred laws, rules, regulations, guidelines, standards, etc. referred to above)

For example:

(i) Public/Right/Preferential issue of shares / debentures/sweat equity, etc.

(ii) Redemption / buy-back of securities.

(iii) Major decisions taken by the members in pursuance to section 180 of the Companies Act, 2013.

(iv) Merger / amalgamation / reconstruction, etc.

(iv) Foreign technical collaborations.

Place: Signature:

Date: Name of Company Secretary in Practice/Firm:

ACS/FCS No.

C P No.:

*(Note: Parawise details of the Audit finding, if necessary, may be placed as annexure to the report.)*

## Annexure -B

**Format of Annual Secretarial Compliance Report**

**(On the letter head of the Practicing Company Secretary)**

**Secretarial Compliance Report of [•] [Name of the listed entity] for the financial year ended**

I/We have examined:

(a) all the documents and records made available to us and explanation provided by [●] [Name of the listed entity] ("the listed entity"),

(b) the filings/ submissions made by the listed entity to the Stock Exchanges,

(c) website of the listed entity,

(d) any other document/ filing, as may be relevant, which has been relied upon to make this Report.

for the financial year ended [ ● ] ("Review Period") in respect of compliance with the provisions of :

(a) the Securities and Exchange Board of India Act, 1992 ("SEBI Act") and the regulations, circulars, guidelines issued thereunder; and

(b) the Securities Contracts (Regulation) Act, 1956 ("SCRA"), rules made thereunder and the regulations, circulars, guidelines issued thereunder by the SEBI;

The specific Regulations, whose provisions and the circulars/ guidelines issued thereunder, have been examined, include:-

(a) Securities and Exchange Board of India (LODR) Regulations, 2015;

(b) Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018;

(c) Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;

(d) Securities and Exchange Board of India (Buyback of Securities) Regulations, 2018;

(e) Securities and Exchange Board of India (Share Based Employee Benefits and Sweat Equity) Regulations, 2021;

(f) Securities and Exchange Board of India (Issue and Listing of Non Convertible Securities) Regulations, 2021;

(g) Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015;

(h) other regulations as applicable. and circulars/ guidelines issued thereunder;

(Note: The aforesaid list of Regulations is only illustrative. The list of such SEBI Regulations, as may be relevant and applicable to the listed entity for the review period, shall be added.) and based on the above examination, I/We hereby report that, during the Review Period:

(a) (**) The listed entity has complied with the provisions of the above Regulations and circulars/ guidelines issued thereunder, except in respect of matters specified below:

| **S.N.** | **Compliance Requirement (Regulations / circulars/ guidelines including specific clause)** | **Regulation/ Circular No.** | **Deviations** | **Action Taken by** | **Type of Action** | **Details of Violation** | **Fine Amount** | **Observations / Remarks of the Practicing Company Secretary (PCS)** | **Management Response** | **Remarks** |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Advisory/ Clarification/ Fine/ Show Cause Notice/ Warning etc. | | | | | |

(b) The listed entity has taken the following actions to comply with the observations made in previous reports:

| S.N. | Observations/ Remarks Of the Practicing Company Secretary in the previous reports) (PCS) | Observations made in the secretarial compliance report for the year ended ….. (the years are to be mentioned) | Compliance Requirement (Regulations/ circulars/ guidelines including specific clause) | Details of violation / deviations and actions taken / penalty imposed, if any, on the listed entity | Remedial actions, if any, taken by the listed entity | Comments of the PCS on the actions taken by the listed entity |
|---|---|---|---|---|---|---|

***(Note:***

1. *Provide the list of all the observations in the report for the previous year along with the actions taken by the listed entity on those observations.*
2. *Add the list of all observations in the reports pertaining to the periods prior to the previous year in case the entity has not taken sufficient steps to address the concerns raised/ observations*

   *E.g. In the report for the year ended 31st Mar, 2023, the PCS shall provide a list of:*

- *all the observations in the report for the year ended 31st March, 2022 along with the actions.*
- *taken by the listed entity on those observations.*
- *the observations in the reports pertaining to the year ended 31st March,2022 and earlier, in case the entity has not taken sufficient steps to address the concerns raised/ observations in those reports.)*

I. I/we hereby report that, during the review period the compliance status of the listed entity with the following requirements:

| Sr. No. | Particulars | Compliance Status (Yes/ No/NA) | Observations/ Remarks by PCS* |
|---|---|---|---|
| 1. | **Secretarial Standards:**<br>The compliances of the listed entity are in accordance with the applicable Secretarial Standards (SS) issued by the Institute of Company Secretaries of India (ICSI). | | |
| 2. | **Adoption and timely updation of the Policies:**<br>● All applicable policies under SEBI Regulations are adopted with the approval of board of directors of the listed entities.<br>● All the policies are in conformity with SEBI Regulations and have been reviewed & updated on time, as per the regulations/ circulars/guidelines issued by SEBI. | | |
| 3. | **Maintenance and disclosures on Website:**<br>● The listed entity is maintaining a functional website.<br>● Timely dissemination of the documents/ information under a separate section on the website.<br>● Web-links provided in annual corporate governance reports under Regulation 27(2) are accurate and specific which redirects to the relevant document(s)/section of the website | | |
| 4. | **Disqualification of Director(s):**<br>None of the director(s) of the listed entity is/ are disqualified under Section 164 of Companies Act, 2013 as confirmed by the listed entity | | |

| Sr. No. | Particulars | Compliance Status (Yes/ No/NA) | Observations/ Remarks by PCS* |
|---|---|---|---|
| 5. | **Details related to subsidiaries of listed entities have been examined w.r.t.:**<br>(a) Identification of material subsidiary companies.<br>(b) Disclosure requirement of material as well as other subsidiaries | | |
| 6. | **Preservation of Documents:**<br>The listed entity is preserving and maintaining records as prescribed under SEBI Regulations and disposal of records as per policy of preservation of documents and archival policy prescribed under SEBI LODR Regulations, 2015. | | |
| 7. | **Performance Evaluation:**<br>The listed entity has conducted performance evaluation of the board, independent directors and the committees at the start of every financial year/during the financial year as prescribed in SEBI Regulations. | | |
| 8. | **Related Party Transactions:**<br>(a) The listed entity has obtained prior approval of audit committee for all related party transactions;<br>(b) In case no prior approval obtained, the listed entity shall provide detailed reasons along with confirmation whether the transactions were subsequently approved/ratified/ rejected by the audit committee. | | |
| 9. | **Disclosure of events or information:**<br>The listed entity has provided all the required disclosure(s) under Regulation 30 along with Schedule III of SEBI LODR Regulations, 2015 within the time limits prescribed thereunder. | | |
| 10. | **Prohibition of Insider Trading:**<br>The listed entity is in compliance with Regulation 3(5) & 3(6) SEBI (Prohibition of Insider Trading) Regulations, 2015. | | |
| 11. | **Actions taken by SEBI or Stock Exchange(s), if any:**<br>No action(s) has been taken against the listed entity/ its promoters/ directors/ subsidiaries either by SEBI or by Stock Exchanges (including under the Standard Operating Procedures issued by SEBI through various circulars) under SEBI Regulations and circulars/ guidelines issued thereunder (or)<br>The actions taken against the listed entity/ its promoters/ directors/ subsidiaries either by SEBI or by Stock Exchanges are specified in the last column. | | |

| Sr. No. | Particulars | Compliance Status (Yes/ No/NA) | Observations/ Remarks by PCS* |
|---|---|---|---|
| 12. | **Resignation of statutory auditors from the listed entity or its material subsidiaries:**<br>In case of resignation of statutory auditor from the listed entity or any of its material subsidiaries during the financial year, the listed entity and / or its material subsidiary(ies) has / have complied with paragraph 6.1 and 6.2 of section V-D of chapter V of the Master Circular on compliance with the provisions of the LODR Regulations by listed entities. | | |
| 13 | **Additional Non-compliances, if any:**<br>No additional non-compliances observed for any SEBI regulation/ circular/guidance note etc. except as reported above. | | |

*Observations/Remarks by PCS are mandatory if the compliance statusis provided as 'No' or 'NA'*

**Assumptions & limitation of scope and review:**

1. Compliance of the applicable laws and ensuring the authenticity of documents and information furnished, are the responsibilities of the management of the listed entity.
2. Our responsibility is to report based upon our examination of relevant documents and information. This is neither an audit nor an expression of opinion.
3. We have not verified the correctness and appropriateness of financial records and books of account of the listed entity.
4. This report is solely for the intended purpose of compliance in terms of Regulation 24A (2) of the SEBI (LODR) Regulations, 2015 and is neither an assurance as to the future viability of the listed entity nor of the efficacy or effectiveness with which the management has conducted the affairs of the listed entity.

**Place:** **Signature:**

**Date:** **Name of the PCS**

**ACS/ FCS No.:**

**CP No.**

**UDIN : ....**

**PR No. ...**

## LESSON ROUND-UP

- Secretarial Audit is an independent and objective assurance intended to add value and improve operations of a company.
- Only a member of the Institute of Company Secretaries of India holding certificate of practice can conduct Secretarial Audit and furnish the Secretarial Audit Report to the company.
- Secretarial Audit is an audit to check compliance of various legislations including the Companies Act and other corporate and economic laws applicable to the company, so as to allow the Auditor to make an opinion as to whether there exist adequate systems and processes in the company to monitor and ensure compliance with applicable laws, rules, regulations etc.
- The Secretarial Audit Report should be prepared in accordance with the Auditing Standards issued by the Institute of Company Secretaries of India and be signed by the Secretarial Auditor who has been engaged by the company to conduct the Secretarial Audit and in case of a firm of Company Secretaries, by the partner under whose supervision the Secretarial Audit was conducted.

- Proactive Secretarial Audit on a continuous basis would help the company in initiating corrective measures and strengthening its compliance mechanism and processes. It is therefore, advisable that the Secretarial Audit is carried out periodically (quarterly / half year / annually) and adverse finding if any, is reported on interim basis to the Board immediately.
- The Accounting/ Financial related fraud shall be reported by the statutory auditors, whereas in case of nonfinancial fraud by the Secretarial Auditor and in case of the fraud relating to the costing Fraud it needs to be reported by the Cost Accountant in practice.

## GLOSSARY

**Listed Entity :** The terms listed entity means an entity which has listed, on a recognised stock exchange(s), the designated securities issued by it or designated securities issued under schemes managed by it, in accordance with the listing agreement entered into between the entity and the recognised stock exchange(s).

**MR-3 :** The form prescribed for Secretarial Audit Report.

**Secretarial Standards :** It means the Secretarial Standard Issued by The Institute of Company Secretaries of India and approved by the Central Government under Section 118(10) of the Companies Act, 2013

**Auditing Standard :** It means “Auditing Standard” issued by the Institute of Company Secretaries of India.

**Public Company :** It is a Company as defined under section 2 (71) of the Companies Act, 2013.

## TEST YOURSELF

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation).*

1. Indicate the scope of secretarial audit, which should be taken into consideration by a Practicing Company Secretary, to examine and report the compliance of various laws/regulations as specified in the form MR-3, for submission in Secretarial Audit Report.
2. Elucidate the Importance of Auditing Standard on Secretarial Audit.
3. Define the risk of Secretarial Auditor & code of conduct.
4. Explain reporting of specific event under Secretarial Audit Report.
5. Mehar, a Chartered Accountant was working as a Manager in Finance team of Sita Mining Ltd. Mehar was curious to know about the Secretarial Auditor comments on compliance with applicable laws and regulations. In the preliminary meeting, he asked Rohan, the Secretarial Auditor about the process of identification of applicable laws to the Company. Explain the process.
6. Explain compliances specified in the Regulation 24A regarding applicability of secretarial audit under the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015. Also state the exemptions provided from this Regulation.
7. You are appointed as a Company Secretary of Aparana Pvt Ltd. You have to conduct the audit for the financial year 2019-20. Draft the guidelines for verification of Board Composition & Board Process as per the CSAS-4 (Auditing Standard on Secretarial Audit).
8. Z, one of the director of Shyam International Ltd. leaked an insider information in the market for personal benefit. Ram, Secretarial auditor of the company, in the course of performance of his duties find out this offence which involved the amount of Rs. 2.40 crore. As a Secretarial Auditor of the company how would Ram report about this ? Also state the consequences of non-compliance by the Auditor under the Companies Act, 2013.

## LIST OF FURTHER READINGS

- Companies Act, 2013 and Rules made thereunder
- SEBI Act, 1992 and Regulations made thereunder
- The Secretarial Standards issued by ICSI.
- The Auditing Standards issued by ICSI
- ICSI Manual on Secretarial Audit
- Guidance Note on ICSI Auditing Standards (CSAS-1 to CSAS-4)
- Secretarial Audit under SEBI LODR Regulations
- ICSI FAQs on Secretarial Audit
- ICSI Guidance note on Code of Conduct for Company Secretaries

## OTHER REFERENCES (Including Websites/ Video Links)

- https://www.mca.gov.in/content/mca/global/en/acts-rules/ebooks/acts.html?act=NTk2MQ==
- https://www.sebi.gov.in/
- https://www.icsi.edu/media/webmodules/publications/A1_Guidance_Note_on_Secretarial_Audit_(Release1.4).pdf
- https://www.icsi.edu/media/webmodules/09092022_ManualonSecretarialAudit_Complete.pdf
- https://www.icsi.edu/media/webmodules/Guidance_Notes_on_ICSI%20AS_Book_05-6-2021.pdf
- https://www.indiacode.nic.in
- https://www.icsi.edu/auditing-standard/
- https://www.icsi.edu/ssb/home/
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