

KEY CONCEPTS

■ Conflict of Interest ■ Confidentiality ■ Preconditions of accepting professional engagement ■ Audit Engagement ■ CSAS-1 ■ Appointing Authority ■ Auditing Standard

Learning Objectives

To understand:

- The meaning of audit engagement offer and acceptance of audit engagement.
- The procedures and authority for appointment of Auditors.
- Various requirement of laws and the point which should be considered while taking up the audit engagement by any professional.
- What are the factors to be considered while charging audit audit fees and expenses.
- What are the types of audits which may be undertaken by company secretaries under various statutes.
- The concept of conflict of interest and substantial conflict of interest.

Lesson Outline

- Meaning of Audit Engagement
- Appointing Authority
- Audit Fees and Expenses
- Independence and conflict of Interest
- Confidentiality
- Audit Engagement Letter
- Lesson Round-Up
- Glossary
- Test Yourself
- List of Further Readings
- Other References (Including Websites/Video Links)

REGULATORY FRAMEWORK

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

MEANING OF AUDIT ENGAGEMENT

An audit engagement is an arrangement wherein an auditor perform an audit of the transaction of the auditee for which he has been engaged by the auditee. The audit engagement is a contractual arrangement by way of the Audit Engagement letter between the auditee and the auditor.

ICSI issued CSAS-1 – Auditing Standard on Audit Engagement effective from 1st April, 2021, which defines:

“Audit Engagement” means detailed terms of reference of appointment including scope of audit, remuneration and limiting conditions, if any.“

Question: CSAS-1 is mandatory for audit engagements accepted on or after.....

Answer: April 01, 2021.

Question: What is the scope of CSAS-1 and what does it deal with?

Answer: CSAS-1 is applicable to the Auditor undertaking Audit Engagement under any statute. The Standard deals with the Auditor’s role and responsibilities with respect to an Audit Engagement and the process of entering into an understanding/agreement with the Appointing Authority for the purpose of audit.

Offer and acceptance of the Audit Engagement

The offer for the audit engagement may be initiated either by the Auditee or by the auditor. However it is necessary that the engagement are accepted by the auditors and the auditor fulfils the various criteria for acting as an auditor prescribed in the various applicable laws. For example in case of the statutory audit the auditor shall fulfil the eligibility criteria as prescribed under section 141 of the Companies Act, 2013.

An auditor may be appointed either as a result of one to one communication between the auditor and the Management or through a tendering process followed by the Management.

CASE STUDY

Offer:

PQS Company, a trading company, is looking to engage an internal auditor for the financial year 2022-2023. The company sends an email to ABC & Associates (Practicing Company Secretaries Firm), outlining the scope of the audit, the timeframe for completion, the audit fee, and any other terms and conditions that are relevant.

“We would like to engage your services to conduct an internal audit for the financial year 2022-2023. The audit should cover all aspects of our Internal control effectiveness; Statutory, procedures and control compliance; Implementation of recommendations; Corporate governance; Systems development; Process improvement; and Value for money and Best Value. The audit should be completed within four months of engagement. We are willing to pay a fee of INR 5,00,000 for this engagement. Please let us know if you are willing to accept this engagement, and if so, we can proceed with the necessary paperwork.”

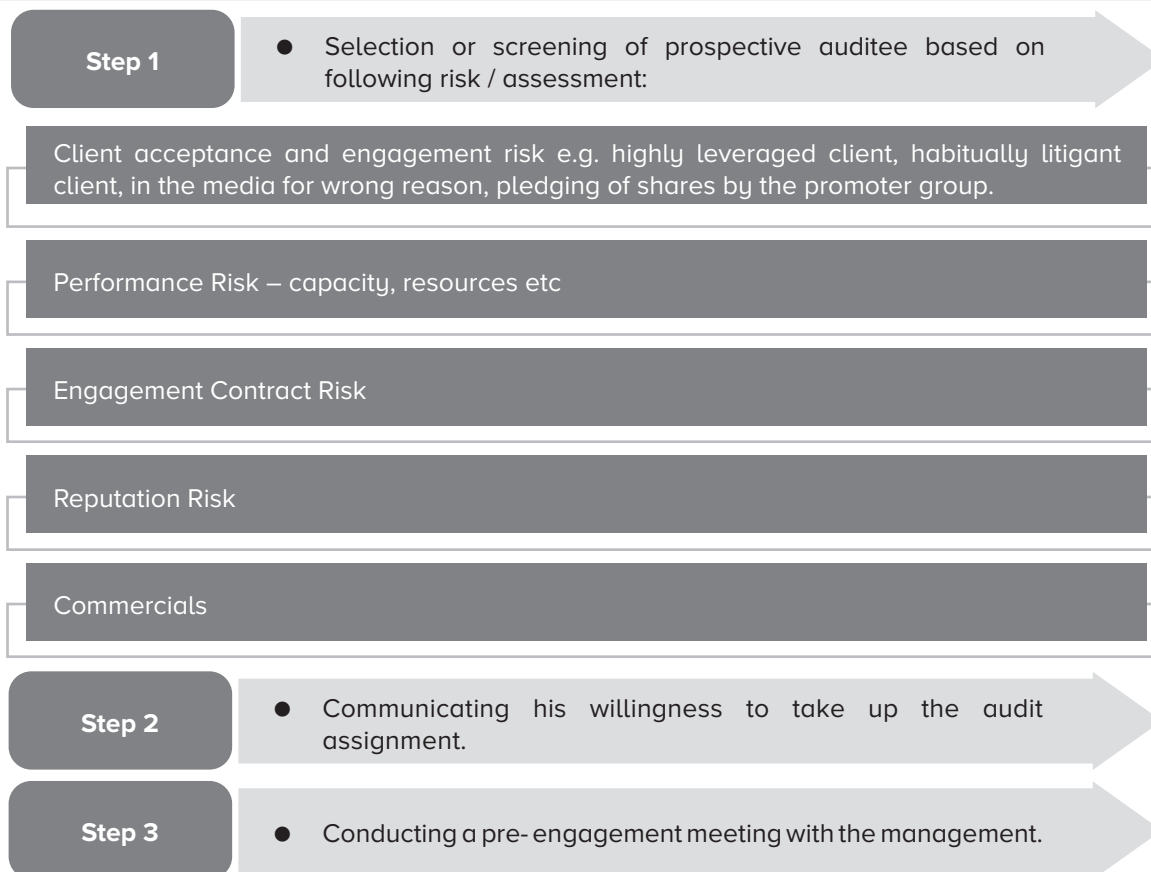
Acceptance:

ABC & Associates (Practicing Company Secretaries Firm) reviews the offer and responds with an acceptance that includes any additional terms or conditions they may have.

“Thank you for offering us this internal audit engagement. We are pleased to accept this engagement under the terms outlined in your email. In addition, we would like to include a clause that states that any findings from the audit will be presented before the audit committee. We will also require access to all financial records and documentation related to this engagement. If this is agreeable to you, we can proceed with the necessary paperwork.”

Once both parties have agreed to the terms of the engagement, they can proceed with the necessary paperwork, such as an engagement letter.

In case the auditor is to be appointed by the management on one to one basis, following steps should be taken care by the auditor:



The meeting may inter-alia include discussion about the terms of engagement, to discuss about the terms of engagement, prior year audit results, appropriateness of reporting framework, understanding business and environment including internal control system, design & operation, audit process, periodicity of audit, determining nature and conflict of interest, prior year audit findings and conclusions, appropriateness of reporting framework, understanding Auditee’s business operations and environment including internal control system, commercial terms of the audit and the timelines and milestones, if any, for conducting the Audit and submission of the Audit Report. Auditor shall disclose in the pre-engagement meeting conflict of interest, if any, with the Auditee. The Auditor shall be under Confidentiality obligation with respect to the information obtained during the pre-engagement meeting.

Step 4

- Signing the engagement letter with the Management and issuance of certificate by auditor before accepting an audit.

In case where the appointment of auditor is through a tendering process by the management:**Step 1**

Pre-bid meeting with the management to discuss upon various aspects of the tender, scope of work terms of engagement, prior year audit results, appropriateness of reporting framework, understanding business and environment including internal control system, design & operation, audit process, periodicity of audit determining nature and conflict of interest etc.

Step 2

Submission of technical bid as per the requirements of the tender document of the management.

Step 3

Signing the engagement letter with the management.

Step 4

Certificate by auditor before accepting an audit.

The Auditor shall furnish a certificate to the Appointing Authority that:

- The number of audits are within the ceiling prescribed by the ICSI as specified in para 2 of CSAS 1.
- No substantial conflict of interest as defined in para 3 of CSAS-1 exists with the Auditee.
- There is no restriction to render the professional services under ICSI Guidelines.
- He is not debarred to undertake such audit under any law or under the disciplinary mechanism of the ICSI.

Preconditions of accepting/continuing any professional engagement

Prior to acceptance of any Audit engagement, the auditor, in order to establish whether the preconditions for accepting professional assignment are present, the auditor should check that:

- Whether the reporting framework as required in the preparation, performance of audit, review of the secretarial/ non-financial statements is acceptable; and
- Whether the management is in agreement to acknowledge and understands its responsibility relating to:
 - Preparation of the secretarial/ non-financial statements in accordance with the applicable reporting framework, including their fair presentation;
 - Development of internal control/systems/procedure to enable the preparation of secretarial/ non-financial statements which are free from material misstatement, whether due to fraud or error; and
 - Providing:
 - Access to all information of which management is aware that is relevant to the preparation/ audit/ review etc. of the secretarial/ non-financial statements such as records, documentation and other matters;
 - Additional information that the auditor may request from management for the relevant purpose; and

- (c) Unrestricted access to persons within the company from whom the auditor determines it necessary to obtain audit evidence.

Limitation on scope prior to Engagement Acceptance

If management or appointing authority impose a limitation on the scope of the auditor's work in the terms of a proposed audit engagement such that the auditor believes the limitation will result in the auditor disclaiming an opinion on the Secretarial records/non-financial statements, the auditor shall not accept such a limited engagement as an audit engagement, unless required by law or regulation to do so.

Other factors affecting Engagement Acceptance

If the preconditions for an audit/professional assignment are not present, the auditor should discuss the matter with management. Unless required by law or regulation to do so, the auditor should not accept the proposed audit engagement:

- (a) If the auditor assesses that the reporting framework to be applied in the preparation of the secretarial records/ non-financial statements is unacceptable, or
- (b) If the agreement has not been concluded.
- (c) Reference to the expected form and content of any reports and a statement that there may be circumstances in which a report may differ from its expected form and content.

If any law or regulation prescribes sufficient detail of the terms of the engagement referred to above, there is no need to record them in a written agreement, except for the fact that such law or regulation applies and that management acknowledges and understands its responsibilities.

Criteria for declining and withdrawing from an Engagement

Based on the evaluation of client information and the following factors, the auditor should determine and document the conditions beyond which it would be prudent to decline, or withdraw from an engagement:

- (a) Client's status/information that is likely to impact adversely on the independence of the firm.
- (b) Ability of the firm to provide appropriate service to the client, considering needs for technical skills, knowledge of the industry and personnel.
- (c) Consider circumstances which would cause the firm to regard the engagement as one requiring special attention or presenting unusual risks.

APPOINTING AUTHORITY

The appointing authority means the person who is appointing the Auditors of the company. The Auditee under the Statute could be a company or any other form of entity. Appointing Authority will depend upon the type of the Auditee. In case the Auditee is a company, the Appointing Authority would be the Board of company or members of the company, as the case may be, and in other cases, it would be the persons who have been entrusted with the responsibility of governance and compliances of the Auditee. Further, the Appointing Authority may also include Court, Tribunal or Regulator or any officer thereof.

CASE LAW

In the matter of *Kingston Cotton Mill Co. (No. 2)* [1896] 2 Ch. 279, the case involved a dispute between the shareholders and the directors of a company over the appointment of an auditor. The shareholders had passed a resolution to appoint an auditor, but the directors refused to comply with the resolution. The honourable court held that the shareholders of a company have the right to appoint an auditor, and that the directors of the company cannot interfere with this right.

ICSI auditing standard CSAS-1 (Auditing Standard on Audit Engagement) effective from 1st April, 2021, defines: “Appointing Authority” means any person having authority to appoint the Auditor.

“Auditee” means a person subject to audit.

Under the provision of the Section 139 of the Companies Act, 2013, it has been specifically provided that the first statutory auditor shall be appointed by the Board of Directors of the company within 30 days of the incorporation of the company, however, subsequent auditors shall be appointed upon the recommendation of the board or the audit committee of the company, if any, by the members at the general meeting of the company.

For example, to conduct audit of the function and activities of the company in case of Secretarial Audit under Section 204 of Companies Act, 2013 or Clause 24A of the SEBI (LODR) Regulations, 2015 and Internal Audit under Section 138 of Companies Act, 2013, the Appointing Authority would be the Board of the Company. It may be noted that the internal auditor may or may not be the employee of the company. In case where the tribunal/ official liquidator by exercising his power, appointed the auditor, the tribunal/ official liquidator is considered as the appointing authority.

In case where the law specifically provides for the appointing authority and the appointing authority may authorize such person to sign the engagement letter, however instances where the law has not provided, the person who signs the engagement letter in official capacity can be considered as the appointing authority.

In case, the Auditee is under Corporate Insolvency Resolution Process, the Appointing Authority shall be the Resolution Professional.

In case of Audit of Depository Participants, the Appointing Authority may depend upon the type of Auditee, e.g. if the Depository Participant is a company then the Appointing Authority will be the Board or in case of an LLP it could be the designated partner or any other partner as may be authorised to appoint the Auditor.

Similarly, in case of Internal Audit of Stock Brokers, Internal Audit of Investment Advisors, Internal Audit of Portfolio Managers, Internal Audit of Credit Rating Agencies and Internal Audit of Research Analysts, the Appointing Authority would depend upon the type of Auditee.

Types of appointing authorities	
First statutory auditor of the Company	Board of Directors or members in EGM
Statutory Auditor	Members in AGM
Secretarial Auditor	Board of Directors/Members in AGM For Listed Companies (As per SEBI LODR amendment dated 13.12.2024)
Internal Auditors	Board of Directors
Auditee is under Corporate Insolvency Resolution Process	Resolution Professional
Tribunal/ official liquidator by exercising his power	Tribunal/Official Liquidator
Audit of Depository Participants	Director /Designated etc. partner depends on nature of Organisation
Internal Audit of Stock Brokers	Depends upon the type of auditee

CASE STUDY

Sun Moon Limited is a listed company and operates in the manufacturing sector. In January 2023, the company received a notice from the Securities and Exchange Board of India (SEBI) stating that Sun Moon Limited had failed to comply with several provisions of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. The SEBI notice also required the company to appoint a practicing company secretary to conduct a secretarial audit of its records and submit a report to SEBI.

The board of directors of Sun Moon Limited have decided to appoint a M/S RR & Associates (Practicing Company Secretaries Firm) to conduct the secretarial audit and passed the Board resolution in their meeting.

However, Mr. Abhinav (shareholder) of the company challenged the appointment of the secretarial auditor in court, stating that the board did not have the authority to appoint the auditor and that the appointment should have been made by SEBI. The matter was referred to court.

The court examined the provisions of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, and found that the regulations did not specify who had the authority to appoint a secretarial auditor. However, the court noted that the regulations required the secretarial auditor to be appointed by the company to conduct the audit.

Based on these findings, the court ruled that the board of directors of Sun Moon Limited had the authority to appoint the secretarial auditor, and that the appointment was valid. The secretarial audit was conducted, and the report was submitted to SEBI. Sun Moon Limited took corrective measures to rectify the non-compliances identified during the audit.

Terms and Conditions of Audit engagement

The objective and scope of every audit is dependent on the four corners of the terms and conditions which also include the scope of audit as agreed by and between the auditee and the auditors of the company. This requires the specific attention of the auditors and auditee on the following points:

- The objective and purpose of the audit;
- The responsibilities of the auditor;
- The responsibilities of management/ Auditee;
- The audit risk;
- The audit limitation;
- The audit plan.

This is essential that the auditor as well as the auditee should agree upon the terms of audit engagement and documented the same in the audit engagement letter or other suitable form of written agreement which can be referred on any conflict arising during the course of audit.

In case of instances where due to change in the governing laws the amended law should be considered in the performance on the audit, however, any request in the change of the terms of audit engagement should be considered by the auditor on its merit and shall be properly documented by the auditors.

AUDIT FEE & EXPENSES

Audit fee which is to be charge by the auditor depends on several factors, which includes:

- Size of the organization;
- Nature of business;
- Internal Controls systems & Technology adopted;
- Scope of audit;
- Frequency of audit etc.

Audit fees should be a fair reflection of the value of the work performed for the auditee, taking into account the above mentioned factors. However, the Audit services should not be offered or rendered under an arrangement whereby no fee will be charged unless specified findings or results are obtained, or where the fee is otherwise contingent upon the findings or results of such services, and fees should not be regarded as being contingent if fixed by a court or other public authority. Also the charge or accept a fee for professional work on a percentage basis is not advisable except where that course is authorized by statute or has been approved by a member body as generally accepted practice for certain work.

Auditors should not accept a very low level of fee as a result of competing for business. Also not to enter in to price competition and deplored in the profession, as it could impair the auditors' independence and deteriorate the quality of the auditing service. However, charging a lower fee than has previously been charged by another auditor for similar work is not restricted in any law.

In case of Statutory Auditors, Section 142 of the Companies Act, 2013 provides that the remuneration to the Auditors shall be fixed in the general meeting of the company, also the auditor can claim the expenses incurred by him in connection with the audit of the company.

Similarly, In case of the Secretarial Audit and the Internal Audit, the Audit fee shall be decided by the Audit committee or by the board of the company.

CASE STUDY

In Re *R. Swarup Reddy Vs. M.N Pratap Reddy*, NCLAT New Delhi, Company Appeal (AT) Nos. 77 & 121 Of 2018, in this matter CLB appointed Independent auditors for auditing books of account the company. Auditors completed their work and claimed fees of Rs. 36.16 lakh. The director company stated that fees claimed by auditors was on higher side and at best they were entitled for a fees of Rs. 8 lakh.

The Court observed that said auditors had not only done audit but also did investigation, particularly with reference to related party transactions entered at instance of appellant with its two sister companies for period from 1-4-2007 to 31-3-2014. Further, amount claimed by said auditors was supported by number of days spent and composition of people working on assignment. It was also observed that appellant had paid nearly Rs. 62 lakh for auditing of sister concerns for same period. Therefore, fees claimed by auditors were reasonable. Court was justified in directing the company to remit to said auditors entire claimed amount.

The clause pertaining to Audit fees and expenses in the Audit Engagement Letter may be reflected as:

“V. Commercial Terms

Audit fees for the F.Y. 20XX-XX is fixed at Rs. XXXXXXXX plus applicable taxes. Fees will be billed as the work progresses.

Out-of-pocket expenses by the Auditor shall be reimbursed on actual basis”.

AUDITING STANDARD ON AUDIT ENGAGEMENT (CSAS-1)

ICSI Guidance Note on Audit Engagement

The Auditing Standard on Audit Engagement (CSAS-1) is applicable to the Practicing Company Secretaries (PCS) as defined in the Company Secretaries Act, 1980, who undertake the audit assignment envisaged under the Companies Act, 2013 or Securities and Exchange Board of India Act, 1992 or any other law prevailing in India.

CSAS-1 is not applicable for Audits entrusted on a voluntary basis by the Auditee to the Auditor. However, adherence to the Standard is recommended in respect of Audits entrusted on voluntary basis also.

In case of appointment by Court, Tribunal or Regulatory Authority, CSAS-1 shall apply to the extent possible, since the manner of appointment and terms of engagement in such cases shall be as per the directions of the Court, Tribunal or Regulatory Authority.

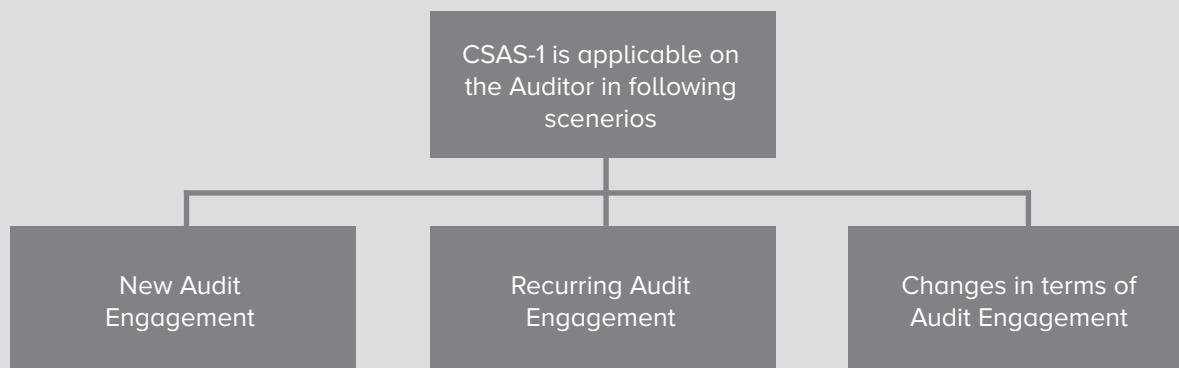
Following is an illustrative list of Audits which may be undertaken by a Company Secretary under various Statutes:

Type of Audit	Act/Regulation	Section/ Regulation	Auditee
Secretarial Audit	Companies Act, 2013	204	Company

Type of Audit	Act/Regulation	Section/ Regulation	Auditee
Secretarial Audit	SEBI (LODR) Regulations, 2015	24A	Listed Entities
Internal Audit	Companies Act, 2013	138	Company
Audit of Depository Participants	SEBI (Depositories and Participants) Regulations 2018	76	Sole Proprietorship, Partnership Firm, LLP, Company
Internal Audit of Stock Brokers	SEBI (Stock Brokers) Regulations, 1992	SEBI Master Circular for Stock Brokers dated 09.08.2024	Sole Proprietorship, Partnership Firm, LLP, Company
Internal Audit of Investment Advisors	SEBI (Investment Advisors) Regulations, 2013	19(3)	Sole Proprietorship, Partnership Firm, LLP, Company
Internal Audit of Portfolio Managers	SEBI (Portfolio Managers) Regulations, 2020	SEBI Master Circular for portfolio managers dated 20.03.2023	Body Corporate
Internal Audit of Credit Rating Agencies	SEBI (Credit Rating Agencies) Regulations 1999	SEBI Master Circular for Credit Rating Agencies dated 16.05.2024	Public Financial Institution, Scheduled Commercial Bank, Foreign Bank operating in India with RBI approval, Foreign Credit Rating Agency recognised by or under any law, Company, Body Corporate
Internal Audit of Research Analysts	SEBI (Research Analysts) Regulation, 2014	25(3)	Sole, Partnership Firm, LLP, Company

While auditing under any of the statutes, the Auditors are required to examine the Records, documents and information from the Auditee to express an independent opinion. Therefore, it becomes very important to understand the scope of audit.

The CSAS-1 deals with the Auditor's responsibilities while agreeing to the terms of Audit Engagement and entering into an agreement with the Management or those charged with governance. This includes principal contents of an Audit Engagement Letter and also the duties and responsibilities of the Auditor and the Auditee in case of a change in terms of engagement, if any.



New Audit Engagement – Covers an audit being conducted first time and therefore the appointment of the Auditor is an initial appointment. It will also cover the situations where the audit for the previous period was conducted by another Auditor.

Recurring Audit Engagement – Covers the situation where the Auditor had conducted the audit for the previous period and is requested to conduct the audit for the subsequent period as well. In such a case, the Auditor should obtain fresh Audit Engagement Letter if the period of engagement has expired, including revised terms if the circumstances so require Auditor shall adhere to the Standard even if the Audit Engagement is a continuing one.

Changes in terms of Audit Engagement – Whenever there is a change in the terms of Audit Engagement in the middle of an ongoing audit, the Auditor shall adhere to the Standard and initiate a revised Engagement Letter in terms of this Standard.

Definitions:

“Auditor” means a member of the ICSI who holds a valid Certificate of Practice under Section 2(2) of the Company Secretaries Act, 1980. It includes a firm or Limited Liability Partnership (LLP) registered with ICSI and whose partners are members of the ICSI.

The term “Management” includes Board of Directors and persons who have been entrusted with the responsibility of governance and compliances of the Auditee like In case of Companies.

The term “persons who have been entrusted with the responsibility of governance and compliances of the Auditee” include the Key Managerial Personnel as defined under Section 2(51) of the Companies Act, 2013 and senior

As per Section 2(51) of Companies Act, 2013: “Key Managerial Personnel”, in relation to a company, means –

- (i) the Chief Executive Officer or the Managing Director or the Manager;
- (ii) the Company Secretary;
- (iii) the whole-time Director;
- (iv) the Chief Financial Officer;
- (v) such other officer, not more than one level below the directors who is in whole-time employment, designated as Key Managerial Personnel by the Board; and
- (vi) such other officer as may be prescribed.

As per regulation 16(1)(d) of the SEBI (LODR) Regulations, 2015: “Senior Management” shall mean the officer sand personnel of the listed entity whoare members of it score managemen team, excluding the Board of Directors, and shall also comprise all the members of the management one level below the Chief Executive Officer or Managing Director or Whole Time Director or Manager (including Chief Executive Officer and Manager, in case they are not part of the Board of Directors) and shall specifically include the functional heads, by whatever name called and the persons identified and+ designated as key managerial personnel, other than the board of directors, by the listed entity.

Explanation to Section 178 of the Companies Act, 2013, describes that “Senior Management” means personnel of the company who are members of its core Management team excluding Board of Directors comprising all members of Management one level below the Executive Directors, including the functional heads.

In case of Auditee other than companies, the term “persons who have been entrusted with the responsibility of governance and compliances of the Auditee” shall include any person or employee of the Auditee as may be authorised. For example, in case of an LLP, Management includes the partners or designated partners or any officer of the LLP entrusted with such responsibility.

In case of a Proprietorship, Management means the proprietor or any officer authorised by him.

“Predecessor or Previous Auditor” means an Auditor who has conducted the most recent audit assignment of the Auditee and submitted report thereon prior to the incumbent Auditor or was engaged but did not complete the audit assignment due to his resignation, termination or otherwise. An Auditor who has completed the assignment and has not been reappointed or an Auditor who had been appointed but has not completed the assignment due to resignation, termination or otherwise, shall be deemed to be a “Predecessor or Previous Auditor” for the same assignment.

AUDIT ENGAGEMENT PROCESS

Pre-Engagement Meeting

Before accepting the Audit Engagement, the Auditor should have a pre-engagement meeting with the Auditee. The meeting may inter-alia include discussion about the terms of engagement, prior year audit findings and conclusions, appropriateness of reporting framework, understanding Auditee's business operations and environment including internal control system, commercial terms of the audit and the timelines and milestones, if any, for conducting the Audit and submission of the Audit Report. Auditor shall disclose in the pre-engagement meeting conflict of interest, if any, with the Auditee.

The Auditor shall be under Confidentiality obligation with respect to the information obtained during the pre-engagement meeting.

Appointment

The appointment of Auditor shall be made in the manner prescribed in the applicable laws, act, rules, regulations, standards and guidelines and in case no such manner has been prescribed, such appointment shall be made in the manner determined by the Appointing Authority.

Before accepting an audit, the Auditor shall furnish a certificate to the Appointing Authority that:

- (a) The number of audits are within the ceiling prescribed by the ICSI as specified in para 2 of CSAS 1.
- (b) No substantial conflict of interest as defined in para 3 of CSAS-1 exists with the Auditee.
- (c) There is no restriction to render the professional services under ICSI Guidelines.
- (d) He is not debarred to undertake such audit under any law or under the disciplinary mechanism of the ICSI.

Illustration:

Section 179(3)(k) of Companies Act, 2013 read with Rule 8(4) of Companies (Meeting of Board and its Powers) Rules, 2014 requires that the Internal Auditor and Secretarial Auditor of the company shall be appointed by passing a resolution at a duly convened meeting of the Board.

Therefore, the appointment of Internal Auditor/Secretarial Auditor cannot be made by passing a resolution by circulation.

Further, the said appointment cannot be made by Key Managerial Personnel or Senior Management, even if authorised by the Board in this regard.

A Specimen Eligibility Certificate is placed at Annexure A.

The Auditor shall obtain an Audit Engagement Letter along with a copy of the resolution, if any, passed by the Appointing Authority and shall provide acceptance to the Appointing Authority.

The Auditor may give his acceptance to undertake the audit either on the copy of the Audit Engagement letter or through a separate letter. The acceptance may also be communicated through an email.

Audit engagement letter

The engagement letter provides the opportunity to detail the scope of the Audit Engagement and to define the responsibilities between the Auditor and the Auditee.

It is in interest of both the management and the auditor that the auditor should get an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the terms of engagement. In some entities, however, the objective and scope of an audit and the responsibilities of management and of the auditor may be sufficiently established by law, in that case, the engagement letter may

give a reference to the fact that relevant law or regulation applies and that management acknowledges and understands its responsibilities for preparation and maintenance of records and for devising proper systems to ensure compliance with the provisions of applicable laws and regulations.

It should be reviewed every year to ensure that it is up to date but does not need to be reissued every year unless there are changes to the terms of the engagement. The auditor shall obtain a new engagement letter if the scope or context of the assignment changes after initial appointment.

It documents the terms of Audit Engagement agreed between the Auditor and the Appointing Authority with reference to scope of audit, responsibilities of Auditor and Auditee, remuneration and limiting conditions, if any.

The Audit Engagement Letter shall *inter alia* include:

- a. The objective and scope of the audit;
- b. The responsibilities of the Auditor and the Auditee;
- c. Written representations provided and/or to be provided by the Management to the Auditor, including particulars of the Predecessor or Previous Auditor;
- d. The period within which the audit report shall be submitted by the Auditor, along with milestones, if any;
- e. The commercial terms regarding audit fees and reimbursement of out of pocket expenses in connection with the audit; and
- f. Limitations of audit, if any.

Where the objective and scope of the audit and responsibilities of the Management and of the Auditor have been established by law, the Audit Engagement Letter shall give a reference to the provisions of the relevant law along with a statement that the Management acknowledges and understands its responsibilities for preparation and maintenance of records and for devising proper systems to ensure compliance with the provisions of applicable laws, act, rules, regulations and standards for the time being in force.

The Auditor shall agree upon the terms of Audit Engagement with the Appointing Authority which shall be documented in an Audit Engagement letter.

The Responsibilities of Auditor *inter alia* include the following:

- To take up the audit as per the terms of the engagement.
- To depute personnel who have the knowledge of the laws under which the audit is being carried out, subject to his overall supervision.
- To observe and ensure observance of highest standards of ethics and maintain utmost professionalism at all times by the employees, staff and other team members involved in the Audit and persons engaged by him to provide advice or assistance for the conduct of audit.
- To maintain and ensure confidentiality by the employees, staff and other team members involved in the audit and persons engaged by him to provide advice or assistance for the conduct of audit.
- To not trade in securities relating to which unpublished price sensitive information has come to his/her knowledge during the course of audit, which responsibility shall extend to the employees, staff and other team members involved in the audit and persons engaged by him to provide advice or assistance for the conduct of audit also.

Responsibilities of Auditee *inter alia* include:

- To provide access to premises of the Auditee and timely access to Records, documents, legal opinions, show cause notices, inspection reports and other information, explanations and reports as may be necessary in connection with the audit.

- To identify and depute a responsible official to timely provide relevant documents, information and explanations required by the Auditor.
- To provide written Management representations, if any, to the Auditor during the course of audit, which shall provide the Auditor a substantive evidence of important assertions and the Management's primary responsibility for the assertions and its accuracy.
- To provide details of the Predecessor or Previous Auditor, so as to enable proposed Auditor to communicate with the Predecessor or Previous Auditor.

Audit remuneration and expenses may depend on several factors including:

- Size of the organisation;
- Location of business and its branches;
- Type of company (Listed/Unlisted);
- Sector to which company belongs;
- Nature of business;
- Internal control mechanism;
- Scope of Audit Engagement;
- Frequency of audit, whether monthly, quarterly, yearly;
- Type of audit, whether sole, joint or concurrent audit;
- The experience of the Auditor in conducting audits;
- Estimated man-hours required to complete the assignment;
- Guidance/Advisory issued by the ICSI, if any;
- Any other term or a combination of any of the above.

Audit fees should be a fair reflection of the value of the work performed for the Auditee, considering the above factors. Quantum of fees, billing arrangement and terms of payment shall be mentioned in the Audit Engagement letter.

The Audit fee shall not be contingent upon findings or results of the audit. However, fees shall not be regarded as being contingent if fixed by a court or other public authority.

The Auditor is not permitted to pay a commission to obtain an audit nor shall he accept a commission for referral of an Auditee to a third party. He shall not accept a commission for the referral of the products or services of others.

As per Clause 2 of Schedule I of the Company Secretaries Act, 1980: A Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he pays or allows or agrees to pay or allow, directly or indirectly, any share, commission or brokerage in the fees or profits of his professional work to any person, other than a member of the Institute or a partner or a retired partner or the legal representative of a deceased partner.

As per Clause 9 of Schedule I of the Company Secretaries Act, 1980: A Company Secretary in Practice shall be deemed to be guilty of professional misconduct, if he charges or offers to charge, accepts or offers to accept, in respect of any professional employment, fees which are based on a percentage of profits or which are contingent upon the findings, or result of such employment, except as permitted under any regulation made under this Act.

Auditor should include a statement in the Audit Engagement Letter that because of inherent limitations of an audit, inherent limitations of internal control, an unavoidable risk exists that some material non-compliance may

not be detected, even though the audit is properly planned and performed in accordance with the applicable Auditing Standards.

Audit Engagement Letter should also specify that arrangements concerning the involvement of third party and experts in some aspects of the Audit.

If the Appointing Authority has imposed a limitation on the scope of the Auditor's work in the terms of engagement and the Auditor believes that such limitation will result in lower level of assurance than what is required under law, the Auditor shall not accept such an engagement, unless required by law or regulation to do so.

Specimen Audit Engagement Letter is placed at Annexure B.

Communication to Previous Auditor

As a measure of the professional etiquettes, while taking up the any audit engagement, the auditors shall give intimation to the previous auditor, intimating his engagement as auditors of the company. The term predecessor or previous auditor can be defined as an auditor who has conducted the most recent audit assignment of the Auditee of the same nature and submitted report thereon prior to the incumbent auditor or was engaged but did not complete the audit assignment due to his resignation, termination or otherwise.

CASE LAW

In *Re, Ssay & Associates v. Institute of Chartered Accountants of India, HC of Delhi W.P. NO. 7674*, it was held that there is no requirement for an auditor to secure a no objection certificate from previous auditor as only requirement is that auditor, who accepts position as an auditor, must communicate with previous auditor about same.

In case whenever a practicing company secretary is appointed as secretarial auditor in place of the existing secretarial auditor, he should communicate the appointment to the earlier incumbent in writing.

Illustration

Mr. P was appointed as the Secretarial Auditor of ABC Ltd. for the F.Y. 2019-20. However, during the course of audit, he intimated the Appointing Authority his inability to complete the audit of ABC Ltd. and therefore cannot give audit report thereon. ABC Ltd. accepted the request of Mr. P and approached Mr. Q to become the secretarial Auditor for F.Y. 2019-20.

In such case, Mr. Q has to first communicate to the Predecessor Auditor i.e. Mr. P of his intention to accept the secretarial audit assignment of ABC Ltd. and wait for 7 days from the date of intimation to Mr. P, before accepting the secretarial audit of ABC Ltd. for F.Y. 2019-20.

There should be an effective communication with the Predecessor or Previous Auditor, if any. Auditor should communicate with the Predecessor or Previous Auditor in such manner as to retain positive evidence of the delivery of the communication. Communication by a letter sent by Registered Acknowledgement Due or by courier or by hand against the written Acknowledgement or through an email would be in the normal course provide such evidence. The Auditor shall wait for a period of 7 days from the date of communication before accepting the audit.

In case any information is provided by the Predecessor Auditor, the Successor Auditor shall take cognizance of the same. The information obtained from the Predecessor may be useful in undertaking the audit. Such information shall remain confidential.

CASE STUDY

XYZ Limited is a listed company and recently hired a new secretarial auditor firm (M/s AA & Associates) to replace the previous auditor firm (M/s BB & Associates), who had been serving the company for two years. The M/s AA & Associates was made responsible for ensuring compliance with various regulations and guidelines and preparing audit report.

Challenge:

The primary challenge faced by XYZ Limited was to smoothly execute the transition of responsibilities between new and old auditors to communicate effectively with the M/s BB & Associates. This was crucial, as the new auditor would need access to all previous records, reports, and other information related to the company's secretarial audit.

Solution:

To address this challenge, the company's management decided to set up a meeting between the M/s AA & Associates and the M/s BB & Associates. During the meeting, the new auditor would have the opportunity to ask any questions, clarify any doubts, and obtain access to all relevant records and reports.

Results:

The communication between the previous secretarial auditor and the new auditor was successful as a written communication in form of email has been made by M/s AA & Associates to previous auditor, and the M/s AA & Associates was able to obtain all necessary information to perform their duties effectively. The information provided by the previous auditor was extremely useful, as it helped the new auditor to identify any areas of concern and address them promptly.

The Council of the Institute of Company Secretaries of India has resolved that it shall be mandatory for every Company Secretary in Practice, before accepting any of the following assignments, to communicate to the previous incumbent, in terms of terms of clause (8) of part I of the First Schedule to the Company Secretaries Act, 1980:

- (i) Signing of Annual Return in Form MGT-7 under Section 92(1) of the Companies Act, 2013 and rule 11(1) of the Companies (Management and Administration) Rules, 2014.
- (ii) Certification of Annual Return in Form MGT-8 under Section 92(2) of the Companies Act, 2013 and rule 11(2) of the Companies (Management and Administration) Rules, 2014.
- (iii) Issuance of Secretarial Audit Report in terms of Section 204 of the Companies Act, 2013.
- (iv) Issue of Secretarial Audit Report to material unlisted subsidiaries of Listed entities (whose equity shares are listed) under Regulation 24A (1) of SEBI (LODR) Regulations, 2015.
- (v) Issue of Annual Secretarial Compliance Report to Listed entities (whose equity shares are listed) under Regulations 24A (2) of SEBI (LODR) Regulations, 2015.
- (vi) Certification under SEBI (Listing Obligations & Disclosure Requirements) Regulations, 2015 that none of the directors on the board of the company have been debarred or disqualified from being appointed or continuing as directors of companies by the Board/ Ministry of Corporate Affairs or any such statutory authority under Schedule V, Part C, Clause (10)(i).
- (vii) Certification under Regulation 40(9) of SEBI (LODR) Regulations, 2015 certifying that all certificates have been issued within thirty days of the date of lodgement for transfer, sub-division, consolidation, renewal, exchange or endorsement of calls/ allotment monies.
- (viii) Acting as Compliance Auditor under Third Party Certification/ Audit Scheme (Amendment), 2018 in the State of Haryana and similar recognition in other states.

Question: *Is communication to previous auditor required?*

Answer: *Yes, the Auditor shall communicate in writing to the predecessor or previous auditor, if any before accepting the audit engagement.*

Further, Council of ICSI has prescribed the following format to be issued by Company Secretaries under Clause 8 of the First Schedule of the Company Secretaries Act, 1980:

CS.....
 Address

Dear Sir / Madam,

Sub.: Intimation in terms of Clause 8 of the First Schedule to the Company Secretaries Act, 1980.

I, CS /We, M/s....., Company Secretary in Practice / Firm of Company Secretaries have been approached by the Management of M/s..... Limited to..... (list of professional services) for the FY vide their letter No. dated

We understand that earlier the abovementioned professional services were being rendered by your goodself/ firm to M/s. Limited during the Financial Year

I / We request you to kindly take this communication as an intimation to be given to the previous incumbent in terms of Clause 8 of the First Schedule to the Company Secretaries Act, 1980.

Regards, CS

Membership No.ACS / FCS

CoP No.....

For & Co./ & Associates,
 Company Secretaries

Unique Code

Date:

Place:

Limits on Audit Engagements

An auditor shall not accept audit engagement beyond the limits of number of audits, if any, as may be specified under applicable laws or any other body governing such profession. Violation of the limits by the auditor may attract disciplinary actions against the auditor.

The fact that because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements or material non-compliances may not be detected, even though the audit is properly planned and performed in accordance with the applicable auditing standard.

To uphold the quality of services rendered by members of the Institute, the Institute has issued the following guidelines:

Guidelines	Guidelines Issued at
Limits for the issue of Secretarial Audit Reports: <ul style="list-style-type: none"> ● 10 Secretarial Audits per partner/ PCS, and ● an additional limit of 5 Secretarial Audits per partner/PCS in case the unit is peer reviewed. The limits will be applicable for the Secretarial Audit Reports issued for the FY2016-17 onwards)	235th meeting of the Council held on 11th February, 2016

Guidelines	Guidelines Issued at
Number of Annual Secretarial Compliance Reports to be issued by PCS are 5 (five) reports individually / per partner in each financial year w.e.f. 1st April, 2020 and an additional limit of 5 (five) ASCR individually/ per partner in case the unit has been Peer Reviewed.	260th meeting of the Council held on 4-5 May, 2019
In case of the following, Secretarial Audit/ Secretarial Compliance Report to be done by Peer Reviewed Units only: <ul style="list-style-type: none"> ● Top 100 companies as per market capitalization w.e.f April 1, 2020 ● Top 500 companies as per market capitalization w.e.f April 1, 2021 ● All listed companies w.e.f April 1, 2022 ● All companies w.e.f April 1, 2023 	259th meeting of the Council held on 16th March, 2019

Issue of Diligence Report for Banks in case of consortium lending/ Multiple Banking Arrangements to be undertaken only by peer Reviewed Practicing Unit w.e.f 1st April, 2020.

Question: Can an Auditor accept any number of audits?

Answer: The Auditors shall accept audit engagements within the limits of number of audits, if any, as may be under any law or by ICSI from time to time.

CONFLICT OF INTEREST

CSAS-1 (Auditing Standard on Audit Engagement) effective from 1st April, 2021, defines: "Conflict of Interest" as: The Auditor shall not have any substantial conflict of interest with the Auditee. Any conflict of interest, other than substantial conflict of interest, must be disclosed by the Auditor before accepting the Audit Engagement or as soon as the Auditor becomes aware of the same, as the case may be.

The term conflict of interest term is defined below. It is expected that the Auditor shall not have any conflict of interest with the Auditee. If the Auditor has any such interest, it is the duty of the Auditor to disclose such interest/ conflict of interest to the Auditee before accepting the Audit Engagement.

The conflict of interest with the Auditee explained below shall not be construed as a substantial conflict of interest:

- Auditor holding not more than 2% paid up share capital or shares of nominal value of Rs. 50,000, which ever is lower or more than 2% voting power.
- Auditor indebted to the Auditee for an amount not exceeding Rs. 5,00,000.
- Auditor was in employment of the Auditee more than 2 year ago

In above cases, the Auditor shall be eligible for undertaking the Audit Engagement only if he discloses such fact in writing before accepting the Audit Engagement or as soon as he becomes aware of the same, as the case may be.

In following cases, it shall be construed that the Auditor has a substantial conflict of interest with that of the Auditee and he shall not accept any Audit Engagement from the Auditee.

- Auditor holding not more than 2% paid up share capital or shares of nominal value of Rs. 50,000 or holding not more than 2% voting power.
- Auditor indebted to the Auditee for an amount not exceeding or equal to Rs. 5,00,000 indebtedness that may seriously impair the independence of the Auditor, irrespective of the amount.
- Auditor was in employment of the Auditee more than 2 year ago.

In above mentioned cases, the Auditor is debarred from accepting such Audit Engagement.

Test Yourself

Question: Can an auditor accept Audit engagement even if there is conflict of interest?

Answer: Yes. The Auditor can accept audit engagement where there is conflict of interest with the Auditee by making disclosure before accepting audit engagement or on becoming aware of such conflict. However in case of substantial conflict of interest Auditor cannot accept Audit engagement.

Explanation

Substantial Conflict of Interest means:

Holding of more than 2% in the paid up share capital or shares of nominal value of rupees fifty thousand, whichever is lower or more than 2% voting power, as the case may be, by the Auditor singly or along with partners, spouse, parent, sibling, and child of such person or of the spouse, any of whom is dependent financially on such person.

Before accepting the audit, the Auditor shall disclose that there is no conflict of interest of ownership as specified in this Standard or prescribed in any law, act, rules and regulations under which the audit is being carried on.

Where there exists a substantial conflict of interest in the Auditee organisation, the Auditor cannot accept the Audit Engagement.

The limit of holding of more than 2% in the paid-up share capital or shares of nominal value of rupees fifty thousand, whichever is lower or more than 2% voting power shall be applied based on combined holding of the Auditor along with partners, spouse, parent, sibling, and child of such person or of the spouse, any of whom is dependent financially on such person.

Illustration 1

Mr. A, Mr. B and Mr. C are partners in ABC, LLP, a firm of Practising Company Secretaries. Mr. B holds 1% paid-up share capital in a company XYZ Ltd. Wife and daughter of Mr. A, who are financially dependent on him hold 1% paid-up share capital in XYZ Ltd. each.

Mr. A has been offered the Secretarial Audit of XYZ Ltd.

In this case, Mr. A is not directly holding any interest in XYZ Ltd. However according to para 3.1 of CSAS-1, Mr. A is having a substantial conflict of interest in XYZ Ltd. as the aggregate value of paid-up share capital held by his wife, daughter and partner in XYZ Ltd. is 3%. Hence, he is not eligible to become Secretarial Auditor of XYZ Ltd.

Illustration 2

Mr. A, Mr. B and Mr. C are partners in ABC, LLP, a firm of Practicing Company Secretaries. Mr. A holds 1% paid-up share capital in a company XYZ Ltd. and Mr. B holds shares of nominal value of Rs. 60,000 in XYZ Ltd.

Mr. A has been offered the Secretarial Audit of XYZ Ltd.

In this case, though Mr. A holds only 1% of the paid up share capital in XYZ Ltd. But according to para 3.1 of CSAS-1, he is having a substantial conflict of interest in XYZ Ltd. as his partner Mr. B is having a share capital of nominal value of more than Rs.50,000 in XYZ Ltd. and therefore Mr. A is not eligible to become Secretarial Auditor of XYZ Ltd

Illustration 3

Mr. A, Mr. B and Mr. C are partners in ABC, LLP, a firm of Practicing Company Secretaries. Mr. A & Mr. B each holds 0.5% paid-up share capital in a company XYZ Ltd. Nominal value of such shares held by each of them is Rs. 20,000. Mr. A has been offered the Secretarial Audit of XYZ Ltd.

In this case, though Mr. A is having a conflict of interest in XYZ Ltd. The same will not be considered as a substantial conflict of interest. Therefore, Mr. A can accept the Secretarial Audit of XYZ Ltd. In this case he shall disclose to the Appointing Authority the fact that he has a conflict of interest with the company, but the same is not substantial conflict of interest in accordance with CSAS-1.

Illustration 4

Mr. A, Mr. B and Mr. C are partners in ABC, LLP, a firm of Practicing Company Secretaries. Mr. A holds 1% of the paid-up share capital in company XYZ Ltd. Nominal value of such shares is Rs. 60,000. The market value of the shares held by Mr. A is Rs. 40,000. Mr. A has been offered the Secretarial Audit of XYZ Ltd.

In this case, there will be a substantial conflict of interest between Mr. A and the company XYZ Ltd. as the nominal value of shares held by Mr. A is more than Rs. 50,000, therefore he cannot accept the Secretarial Audit of XYZ Ltd. The market value of the shares is irrelevant while deciding the conflict of interest based on ownership in accordance with CSAS-1.

Illustration 5

Mr. A, Mr. B and Mr. C are partners in ABC, LLP, a firm of Practicing Company Secretaries. Mr. A holds 1% of the paid-up share capital in company XYZ Ltd. Nominal value of such shares is Rs. 60,000. XYZ Ltd. wants to give its Internal Audit assignment to ABC, LLP.

In this case, there exists a substantial conflict of interest of ABC, LLP with the company XYZ Ltd. due to the fact that one of the partners of the LLP is holding shares of a nominal value of more than Rs. 50,000 in XYZ Ltd. Therefore, it will not be eligible to undertake the internal audit assignment of XYZ Ltd. as per CSAS-1.

Indebtedness of the Auditor for an amount exceeding rupees five lakh other than that arising out of ordinary course of business of the Auditee:

Provided that any indebtedness that may seriously impair his independence shall also be considered as substantial conflict of interest.

Before accepting the audit the Auditor shall disclose that there is no conflict of financial interest as specified in this standard or prescribed law under which the audit is carried on.

The limit of rupees five lakh as specified shall be applicable to the combined indebtedness of the audit firm including indebtedness by the partners in their individual capacity.

The term “ordinary course of business” has not been defined. An assessment of whether a transaction is in “ordinary course of business” can be subjective and may vary on case-to- case basis.

For example, a banking company which in ordinary course of business provides loan or gives guarantees/ securities for the due repayment of any loan and in respect of such loans an interest is charged at a rate not less than the prevailing lending rate , may extend loan to its Auditor as per the terms and conditions of the company and such loan shall not be treated as conflict of financial interest.

Illustration 1

Mr. A is a Practicing Company Secretary. He has taken a personal loan of Rs. 5,00,000 from a XYZ LLP wherein Mr. B, who is the designated partner is friend of Mr. A. The payment of such loan is still outstanding in full. Mr. A has been offered to undertake the Internal Audit of XYZ, LLP.

In the given case, Mr. A has a conflict of interest in XYZ LLP, but it doesn't debar Mr. A from undertaking the Internal Audit of XYZ LLP. Mr. A shall disclose the fact to the Appointing Authority before accepting such Audit.

Illustration 2

Mr. A is a Practicing Company Secretary. He had taken a personal loan of Rs. 5,00,000 from XYZ Ltd. wherein his uncle is Managing Director. Mr. A has been offered to undertake the Secretarial Audit of XYZ Ltd.

In the given case, Mr. A has conflict of interest with the Auditee, as the amount of indebtedness is Rs. 5,00,000, but the same is not considered as substantial conflict of interest. In this case, he is required to make disclosure of the fact to Appointing Authority.

Illustration 3

Mr. P is a Practicing Company Secretary and is offered to conduct the Secretarial Audit of ABC Ltd. Mr. P is indebted to the Director of the company for an amount Rs. 6,00,000. Whether he can accept the Secretarial Audit Engagement of ABC Ltd.

In the given case, Mr. P has a substantial conflict of interest in ABC Ltd. And therefore he can't accept the secretarial audit assignment.

Illustration 4

Mr. A is a Practicing Company Secretary. He had taken a personal loan of Rs. 25,00,000 from XYZ Ltd.. He has used such loan towards purchase of his house which has been mortgaged with XYZ Ltd. Due to some financial crisis, Mr. A has not been able to repay any amount towards the loan since past 2 years. Mr. A has been offered to undertake the Secretarial Audit of XYZ Ltd.

The circumstances of the case suggest that indebtedness of Mr. A towards XYZ Ltd. is such that , if he accepts the Audit of XYZ Ltd., it may substantially impair the independence of Mr. A while forming an opinion on the basis of his audit findings and therefore considered as substantial conflict of interest . Therefore in this case, Mr. A shall be debarred from accepting the Secretarial Audit assignment of XYZ Ltd.

Where an Auditor was in employment of the Auditee, its holding or subsidiary company and 2 (two) years have not lapsed from the date of cessation of employment, the same shall be considered as substantial conflict of interest.

A PCS or member/partner of a PCS firm cannot undertake the audit of that undertaking where the member was in employment prior to holding the Certificate of Practice, unless two years have lapsed from the date

of cessation of employment. The PCS shall disclose the fact that two years have not lapsed from the date of cessation of his employment to the Auditee.

Holding and Subsidiary company shall have the same meaning as defined under section 2 (46) and 2(87) of the Companies Act, 2013.

Illustration 1

Mr. A was the Company Secretary of PQR Ltd. from 1st October, 2015 till 31st May, 2018. He left the job w.e.f. 31st May, 2018 and joined in ABC and Associates (CS Firm) as a partner. On 1st January 2020, ABC and Associates has been offered to conduct Secretarial Audit of ST Ltd. for the F.Y. 2020-21. ST Ltd. is the wholly owned subsidiary of PQR Ltd.

According to para 3 of CSAS-1, Mr. A or ABC and Associates, in which he is a partner cannot undertake any audit assignment in PQR Ltd. and/or its holding or subsidiary companies till 31st may, 2020, i.e. two years from the date of cessation of his employment in PQR Ltd. Therefore, ABC and associates cannot undertake the Secretarial Audit assignment of ST Ltd. for the F.Y. 2020-21.

Illustration 2

Mr. A was the Company Secretary of PQR Ltd. from 1st October, 2015 till 31st May, 2018. He left the job w.e.f. 31st May, 2018 and joined ABC and Associates (CS Firm) as an employee. On 1st January 2020, ABC and Associates has been offered to conduct Secretarial Audit of ST Ltd. for the F.Y. 2020 -21. ST Ltd. is the wholly owned subsidiary of PQR Ltd.

Since Mr. A has joined ABC and Associates in the capacity of an employee, ABC and associates can undertake the Secretarial Audit assignment of ST. Ltd. for the F.Y. 2020-21.

Effect of Substantial Interest

The Company Secretaries Act, 1980 (the Second Schedule, Part I, paragraph 4) makes it an act of misconduct for a Company Secretary to express an opinion on any report or statement of a business or enterprise in which he or his firm or a partner of his firm has a substantial interest, unless he discloses the interest also in his report. Such restriction will put the stakeholders on guard against any possibility of an impairment of the independence of the professional signing the report.

The Companies Act, 2013 does not define the phrase “substantial interest”. This should be left to the judgment and discretion of the professional to determine the extent of interest which would affect his independence. He would be well advised to satisfy himself that the decision in this regard is such as would be taken as reasonable by an objective third party in the circumstances of the case. The professional must take care to see that he does not get into situations where there could be a conflict of interest and duty.

A practicing professional in practice may face a conflict of interest situation while performing a professional service. A conflict of interest creates a threat to objectivity and may create threats to the other fundamental principles. Such threats may be created when:

- The professional provides a professional service related to a particular matter for two or more clients whose interests with respect to that matter are in conflict; or
- The interests of the professional with respect to a particular matter and the interests of the client for whom the professional provides a professional service related to that matter are in conflict.

An auditor shall not allow a conflict of interest to compromise professional judgment. Examples of situations in which conflicts of interest may arise include:

Transaction advisory service	Providing a transaction advisory service to a client seeking to acquire an audit client of the firm, where the firm has obtained confidential information during the course of the audit that may be relevant to the transaction.
Auditing competitive clients	Auditing two clients at the same time who are competing to acquire the same company where the audit report might be relevant to the parties' competitive positions.
Auditing clients in legal dispute	Taking audit assignment of two clients regarding the same matter, who are in a legal dispute with each other.
Audit report for Licensor and Licensee	Providing an audit report for a licensor on royalties due under a license agreement when at the same time advising the licensee of the correctness of the amounts payable.

When identifying and evaluating the interests and relationships that might create a conflict of interest and implementing safeguards, when necessary, to eliminate or reduce any threat to compliance with the fundamental principles to an acceptable level, the auditor shall exercise professional judgment and take into account whether a reasonable and informed third party, weighing all the specific facts and circumstances available to the auditor at the time, would be likely to conclude that compliance with the fundamental principles is not compromised.

When addressing conflicts of interest, including making disclosures or sharing information within the firm or network and seeking guidance of third parties, the auditor shall remain alert to the fundamental principle of confidentiality.

If the threat created by a conflict of interest is not at an acceptable level, the auditor shall apply safeguards to eliminate the threat or reduce it to an acceptable level. If safeguards cannot reduce the threat to an acceptable level, the auditor shall decline to perform the audit; or shall terminate relevant relationships or dispose of relevant interests to eliminate the threat or reduce it to an acceptable level.

Before accepting a new client relationship, engagement, or business relationship, an auditor shall take reasonable steps to identify circumstances that might create a conflict of interest, including identification of:

1. The nature of the relevant interests and relationships between the parties involved; and
2. The nature of the service and its implication for relevant parties.

It is expected that the Auditor shall not have any conflict of interest with the Auditee. If the Auditor has any such interest, it is the duty of the Auditor to disclose such interest/ conflict of interest to the Auditee before accepting the Audit Engagement.

CONFIDENTIALITY

The Auditors of a company while performing the audit assignment access the various confidential information of the company and it is most required for the auditors to maintain the confidentiality of the auditee information. The principle of confidentiality imposes an obligation on the auditor to refrain from:

Disclosing information	Disclosing information acquired as a result of professional relationships without proper and specific authority or unless there is a legal or professional right or duty to disclose; and
Using information for personal advantage	Using information acquired as a result of professional relationships to their personal advantage or the advantage of third parties.
Inadvertent disclosures	An auditor should maintain confidentiality even in a social environment. The auditor should be alert to the possibility of inadvertent disclosure, particularly in circumstances involving long association with a business associate or a relative.
Information disclosed by a Prospective client	An auditor should also maintain confidentiality of information disclosed by a prospective client or employer.
Confidentiality within the firm	An auditor should also consider the need to maintain confidentiality of information within the firm or employing organization.
Control of Staff	An auditor should take all reasonable steps to ensure that staff under the auditor's control and persons from whom advice and assistance is obtained respect the auditor's duty of confidentiality.

Clause (1) of Part I of the Second Schedule to the Company Secretaries Act, 1980 provides that a Company Secretary in practice shall be deemed to be guilty of professional misconduct, if the member – “discloses information acquired in the course of professional engagement to any person other than the Auditee so engaging him, without the consent of the Auditee, or otherwise than as required by any law for the time being in force.”

The word ‘information’ here implies any information which is not available in public domain.

During the course of audit, Auditor receives, verifies and inspects various audit documents, evidence, representation etc. to form an opinion or to give a report. These may be confidential and privileged information that remain in possession of the Auditor and shall not be disclosed without the express authority of the Auditee.

Herein the term proper and specific authority implies the Appointing Authority or any other person or committee as may be entrusted by the Appointing Authority to look after the conduct of Audit. It is the inherent duty of the Auditor to maintain the confidentiality of any information about the Auditee or his business that came to his knowledge as a result of performing the audit work. However, if permitted by the Auditee, Auditor may disclose or share such information with any other person as may be specifically allowed by Auditee. Since there may be different types of Auditee, the authority to give such permission to the Auditor may be different in each case. For example, in case of a company, the Secretarial Auditor is appointed by the Board and therefore it may be authorised by the Board whether the Auditor can disclose any confidential information to anyone. In another case, it may be possible that the Board has authorised a director in this regard to give such authorities and permissions to the Auditor and therefore that director will become the specific authority. Likewise in case of an LLP, it may be a designated partner or any other person as may be authorised by the LLP in this regard.

An Auditor shall maintain confidentiality even in a social environment. The Auditor shall be alert to the possibility of inadvertent disclosure, particularly in circumstances involving long association with a business associate or a relative or friends etc.

However, if the Auditor gives any reference of the audit evidence or documents while forming the opinion in the audit report, it will be deemed to be the disclosure of information under the legal obligation or in the performance of the duty.

If during the course of audit and forming opinion, the Auditor uses the decisions of the judicial authority, it will not be treated as use or sharing of confidential information.

The Auditor shall educate his employees, staff and other team members about the importance of the confidentiality of the information available to them during the course of audit. The Auditor shall ensure that reasonable procedures have been followed to maintain the confidentiality of the information. The Auditor shall also take a duly signed Non Disclosure Agreement (NDA) from such personnel who may have access to such confidential information.

The Auditor shall also ensure that reasonable procedures and safeguards are being followed to prevent unauthorised access to such confidential information.

CHANGES IN TERMS OF ENGAGEMENT

The Auditor shall not agree to a change in the terms of the Audit Engagement where there is no reasonable justification for doing so.

If the terms of the Audit Engagement are changed, the Auditor and the Appointing Authority shall agree on the new terms of the engagement by way of a supplementary/revised engagement letter or any other suitable form in writing.

A request from the Appointing Authority to change the terms of Audit Engagement may result from a change in circumstances affecting the need for the service or a restriction on the scope of Audit Engagement, whether imposed by Management or caused by other circumstances. The Auditor shall consider the justification given for the request, particularly the implication of a restriction on the scope of the Audit Engagement.

A change in circumstances that affects the Auditee's requirements may be considered a reasonable basis for requesting a change in the Audit Engagement.

A change may not be considered reasonable if it appears that the change relates to information that is incorrect, incomplete or otherwise unsatisfactory. For example, where the Auditor is unable to obtain sufficient appropriate audit evidence regarding labour law compliance by the company and the Appointing Authority asks for the Audit Engagement to be changed to a review engagement to avoid a modified opinion or a disclaimer of opinion.

With mutual consent the terms of the Audit Engagement may be changed. When such changes are there, the Auditor shall obtain the supplementary/revised engagement letter with a justification for the change and it shall be duly signed by the Appointing Authority. The impact of such change on the level of assurance shall be ascertained before accepting the same. If such change is likely to result in a lower level of assurance, then the Auditor may accept such change only if such change can adequately be covered by way of modified report.

However, the Auditor should take the following precautions while accepting the change:

- (1) The Auditor should not agree to a change in the terms of the Audit Engagement which restricts the scope of audit provided under any statutes.
- (2) If the term of the Audit Engagement is changed when it is expected that Auditor may have to issue a modified report, such type of changes should be resisted.
- (3) Any request to change to avoid or circumvent unfavorable Auditor's report is also unjustified and should not be accepted.
- (4) If the terms of the Audit Engagement are changed before the completion of the audit, the Auditor should not disregard the evidences obtained prior to the change in scope of audit.

Test Yourself

Question: Can terms of audit engagement be changed?

Answer: As per Para 5.1 of CSAS-1, unless there is reasonable justification for doing so, the auditor shall not agree to change the terms of Audit Engagement. Further, if before completion of the assignment, the Auditor is requested by the Appointing Authority to change the scope of engagement, resulting in a lower level of assurance, the Auditor shall consider the appropriateness of carrying out the same.

Annexure A**Specimen Certificate of Eligibility as Secretarial Auditor**

Date:

To

The Board of Directors, Dear Sir,

Sub: Proposed Appointment as Secretarial Auditor

I/We thank you for your communication dated 2019 seeking my/our consent to act as the Secretarial Auditor of your company for the financial year I/We give my/ our consent for being appointed as Secretarial Auditor of the company.

I/we hereby confirm that:

1. I am/we are eligible for appointment and not disqualified for appointment as per the Companies Secretaries Act, 1980 and rules and regulations made thereunder and ICSI Auditing Standards;
2. The proposed appointment is within the limits, if any laid down by ICSI;
3. I/We do not have any substantial conflict of interest in terms of ICSI Auditing Standard on Audit Engagement (CSAS 1);
4. I/We do not have any conflict of interest in terms of ICSI Auditing Standard on Audit Engagement (CSAS 1)

Or

I/We do have conflict of interest other than substantial conflict of interest which are as below :

Thanking you,

Yours sincerely,

Annexure B**Specimen Audit Engagement Letter**

To,

ABC & Associates (name of Audit firm)

Company Secretaries (Address)

Dear Sir,

This engagement letter is provided in connection with (type of audit) of XYZ Ltd.

I. Scope of work

The scope of the Audit shall include (For example, in case of Secretarial Audit , the scope of audit shall be as specified in Section 204 of the Companies Act, 2013)

II. Responsibilities of Auditor

The Auditor shall carry out the audit with utmost integrity in terms of this Audit Engagement Letter adhering to the highest level of ethics and standards. The Audit shall be conducted in accordance of the requirements of the Act.

III. Duties of Auditee

Auditee acknowledges its responsibility for maintenance of Records and compliances under the applicable laws, acts, rules and regulations.

Auditee acknowledges its responsibility to provide the Auditor access to Records and documents of the Auditee, reports of third party and information as may be sought by the Auditor. The Auditee shall be responsible for the correctness and appropriateness of the Records, documents and information of the Auditee.

IV. Timeline

The Auditor shall submit the Audit Report for the F.Y. 20XX-XX within days of the end of the financial year.

Auditor may also submit a quarterly/half-yearly review report in which the audit observations of the Auditor made during the quarter for timely redressal.

V. Commercial Terms

Audit fees for the F.Y. 20XX-XX is fixed at Rs. XXXXXXX plus applicable taxes. Fees will be billed as the work progresses.

Out-of-pocket expenses by the Auditor shall be reimbursed on actual basis.

VI. Confidentiality

The Auditor shall not disclose the information obtained during the course of Audit without proper and specific authority or unless there is a legal obligation or duty to disclose.

VII. Indemnity

During and after the term of this Engagement, both Parties agree to protect, indemnify, defend and hold harmless other Party, and to extent required from time to time non defaulting party, its officers, agents, and employees, from and against any and all expenses, damages, claims, suits, losses, actions, judgments, liabilities, and costs whatsoever (including legal fees on a full indemnity basis) arising out of, connected with, or resulting from, defaulting Party's negligence, misrepresentation or the breach of any obligations to be performed by the other party and/or its representatives under this Engagement. In no event will either party's liability towards otherparty arising from the terms of this Engagement exceed the total sum of fees paid under this Engagement.

VIII. Any other term as may be agreed between the Auditor and the Auditee, if any

For XYZ Limited

Date

Place

Director

Director

LESSON ROUND-UP

- The audit engagement may be initiated either by the Auditee or by the auditor. However it is necessary that the engagement is accepted by the auditors.
- The auditor may be appointed by the management on one to one basis, or through a tendering process by the management.

- In case where the practicing company secretary is appointed as Secretarial Auditor in place of the existing Secretarial Auditor, he should communicate the appointment to the earlier incumbent in writing, in view of the provisions of clause (8) of Part I of the First Schedule to the Company Secretaries Act, 1980.
- A conflict of interest creates a threat to objectivity of the audit and may create threats to the other fundamental principles, hence the auditor should maintain his Independence or avoid such situation of conflict of Interest.
- The principle of confidentiality imposes an obligation on the auditors to maintain confidentiality of the auditee information.
- It is in interest of both the management and the auditor that the auditor should get an audit engagement letter before the commencement of the audit to help avoid misunderstandings with respect to the terms of engagement.
- The CSAS-1 deals with the Auditor's responsibilities while agreeing to the terms of Audit Engagement and entering into an agreement with the Management or those charged with governance. This includes principal contents of an Audit Engagement Letter and also the duties and responsibilities of the Auditor and the Auditee in case of a change in terms of engagement, if any.
- Before accepting the Audit Engagement, the Auditor should have a pre-engagement meeting with the Auditee. The meeting may inter-alia include discussion about the terms of engagement, prior year audit findings and conclusions, appropriateness of reporting framework, understanding Auditee's business operations and environment including internal control system, commercial terms of the audit and the timelines and milestones, if any, for conducting the Audit and submission of the Audit Report.
- As a measure of the professional etiquettes, while taking up the any audit engagement, the auditors shall give intimation to the previous auditor, intimating his engagement as auditors of the company.
- A request from the Appointing Authority to change the terms of Audit Engagement may result from a change in circumstances affecting the need for the service or a restriction on the scope of Audit Engagement, whether imposed by Management or caused by other circumstances.

GLOSSARY

Document : It includes summons, notice, requisition, order, declaration, form and register, whether issued, sent or kept in pursuance of this Act or under any other law for the time being in force or otherwise, maintained on paper or in electronic form;

Expert : It includes an engineer, a valuer, a chartered accountant, a company secretary, a cost accountant and any other person who has the power or authority to issue a certificate in pursuance of any law for the time being in force.

Officer : It includes any director, manager or key managerial personnel or any person in accordance with whose directions or instructions the Board of Directors or any one or more of the directors is or are accustomed to act.

Total voting power : It is in relation to any matter, means the total number of votes which may be cast in regard to that matter on a poll at a meeting of a company if all the members thereof or their proxies having a right to vote on that matter are present at the meeting and cast their votes.

Professional and Other Misconduct : For the purpose of Company Secretaries Act, 1980 "Professional or other misconduct" shall be deemed to include any act or omission provided in any of the schedules.

Appointing Authority under CSAS : It means any person having authority to appoint the Auditor.

Auditing Engagement : It means detailed terms of reference of appointment including scope of audit, remuneration and limiting conditions, if any.

Auditee : It means a person subject to audit.

Auditor under CSAS : It means a Company Secretary who is deemed to be in practice under sub-section (2) of Section 2 of the Company Secretaries Act, 1980 and includes a firm or Limited Liability Partnership (LLP) registered with ICSI, undertaking the Audit.

Management : It includes Board of Directors and persons who have been entrusted with the responsibility of governance and compliances of the Auditee.

TEST YOURSELF

(These are meant for recapitulation only, Answer to these questions are not to be submitted for evaluation)

1. In the Audit engagement process the acceptance of the Audit Engagement by the professional is mandatory, Comment.
2. What is the scope of CSAS-1 and what does it deal with?
3. Write the examples where an auditor is assumed to have interested in the auditee's business or enterprise.
4. Draft an Audit engagement letter for the Secretarial Auditor.
5. What is the meaning of Confidentiality, Why it is necessary for the auditor to maintain confidentiality.
6. What documents are required at the time of audit engagement?
7. What is substantial conflict of interest?
8. The Board of Directors of ATP Ltd. authorized its one of the Directors X to appoint Secretarial Auditor of the Company. Can X do so as per the provisions of the Companies Act, 2013 ? Also explain pre-engagement meeting in the Audit Engagement Process.
9. X, Y and Z are three partners in JK LLP, a firm of Practicing Company Secretaries. X holds 1% paid-up share capital in ABC Ltd. Y holds shares of nominal value of Rs. 70,000/- in ABC Ltd. Referring the provisions relating to ICSI Auditing Standards, advise whether JK LLP can be engaged for the Secretarial Audit of ABC Ltd.

LIST OF FURTHER READINGS

- Companies Act, 2013 alongwith rules made thereunder
- SEBI (LODR) Regulations, 2015
- Company Secretaries Auditing Standards
- Guidance Note on ICSI CSAS
- Articles published by Professionals
- ICSI FAQs on CSAS-1

OTHER REFERENCES (Including Websites / Video Links)

- <https://www.icsi.edu/auditing-standard/>
- https://www.icsi.edu/media/webmodules/Guidance_Notes_on_ICSI%20AS_Book_05-6-2021.pdf
- [https://en.wikisource.org/wiki/Re_Kingston_Cotton_Mill_Company_\(No.2\)_1896](https://en.wikisource.org/wiki/Re_Kingston_Cotton_Mill_Company_(No.2)_1896)