

Auditing

Company Audit-1



Chapters Summary

All important points

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Audit of accounts is compulsory for all types of companies

All the companies registered under the Companies Act, 1956, whether public or private and whether having a share capital or not are required maintaining proper books of accounts under Section 209 of the Companies Act, 1956. Companies have also to get their Books of accounts audited as required under section 224 of the Act.

APPOINTMENT OF AUDITORS

Section 224 governs the appointment of auditors. The auditors are to be appointed by the shareholders of the company in an Annual General Meeting **by passing an ordinary resolution.** Kindly note appointment of Statutory under section 224(1) is an ordinary business read with Section 173 of the Companies Act, 1956. However, special resolution is required to be passed when section 224A comes into play.

Appointment of first auditors [Section 224(5)]

As per section 224(5), the first auditor or auditors of a company shall be appointed by the Board of directors within one month of the date of registration of the company; and the auditor or auditors so appointed shall hold office until the **conclusion** of the first annual general meeting. Please note the following important provisions related to the appointment of first auditors:

(i) Appointment of first auditors in general meeting.—A company in general meeting may appoint the first auditor or auditors if the Board of directors fails to exercise its power of appointment of first auditors within one month of the date of incorporation of the company.

(ii) Appointment of first auditors through Memorandum and Articles of Association.—The Institute of Chartered Accountants of India has expressed its opinion *vide* Compendium of Opinion Volume No. 1 that the appointment of first auditors through the Memorandum and Articles of Association of the newly floated private company **is not a valid appointment.**

(iii) Removal of first auditors.—The company may, at a general meeting, remove first auditor(s) or all or any of such auditors and appoint in his or their places any other person or persons who have been nominated for appointment by any member of the company and of whose nomination notice has been given to the members of the company not less than fourteen days before the date of the meeting.

(iv) Tenure of office of the first auditor.—The first auditor(s) shall hold office until the conclusion of the first annual general meeting of the company and then be eligible for re-appointment.

Appointment of Auditor other than first auditor

As per Section 224(1) every company shall, at each annual general meeting, appoint an auditor or auditors to hold office from the conclusion of that meeting until the conclusion of the next annual general meeting.

Appointment of auditor shall be an ordinary business

As per section 173(l)(a)(iv) of the Act, the appointment of, and the fixing of the remuneration of the auditors **shall be an ordinary business** to be transacted at an Annual General Meeting of a company. Only an ordinary resolution is to be passed for this purpose except, in the circumstances stated u/s 224A requiring the passing of a special resolution.

Re-appointment of the retiring auditor(s) [Section 224(2)]

As per section 224(2), a retiring auditor shall be re-appointed subject to the limit on maximum number of audits as stated u/s 224(1B). However, in the following cases, a retiring auditor shall not be reappointed:—

- (i) he is not qualified for re-appointment;
- (ii) he has given the company a notice in writing of his unwillingness to be re-appointed;
- (iii) a resolution has been passed at that meeting appointing somebody instead of him or providing expressly that he shall not be re-appointed; or
- (iv) where notice has been given of an intended resolution to appoint some other person or persons in the place of a retiring auditor, and by reason of the death, incapacity or disqualification of that person or of all those persons as the case may be, the resolution cannot be proceeded with.

Deemed re-appointment == Require some action on the part of the company

As per Department's Circular No. 5/72, dated 21-2-1972, the appointment or reappointment of auditors at the annual general meeting is one of the items of ordinary business to be transacted at such a meeting. As provided by section 224(2) of the Act at any annual general meeting, a retiring auditor shall be re-appointed except, in four types of cases referred to therein. The expression shall be re-appointed, postulates some action on the part of the company resulting in the auditor getting re-appointed or automatically re-appointed at the annual general meeting.

It has been clarified that passing of the resolution for that purpose at the annual general meeting is essential for the re-appointment of the retiring auditor who is still qualified and willing to act. Till this is done, a retiring auditor cannot be said to have been re-appointed as contemplated by the section. In this view, it is not correct to say that in the absence of the resolution to the effect that the retiring auditors shall not be re-appointed; the retiring auditors shall stand re-appointed as auditors of the company.

Appointment of auditor is mandatory at each annual general meeting

The auditor(s) appointed at the last annual general meeting ceases to hold office at the conclusion of the next annual general meeting. Therefore, the auditor(s) must be appointed at each annual general meeting to hold office till the conclusion of the next annual general meeting. It has been held in the case of the Institute of Chartered Accountants v Jnanendranath Saikia (1955) 25 Comp Cas 53, 55 (Assam) that the appointment of auditor is mandatory in the annual general meeting for the ensuing year.

Intimation as to appointment

A company is required to give intimation of appointment to every auditor(s) so appointed within seven days of the appointment as desired by section 224(1). The intimation may be given in form of a letter on the letter head of the company by a responsible officer of the company.

Written certificate from auditor regarding eligibility must be obtained

The company shall, before making any appointment or re-appointment of auditor(s) at any annual general meeting, obtain a written certificate to the effect that the appointment or re-appointment, if made, shall be in accordance with the limits specified in section 224(1B) of the Act.

LIMIT ON NUMBER OF AUDITS

The expression 'specified number' means—

- (i) in the case of a person or firm holding appointment as auditor of a number of companies each of which has a paid-up share capital of less than rupees twenty-five lakhs, **twenty such companies**;
- (ii) in any other case, twenty companies, out of which not more than ten shall be companies each of which has a paid-up share capital of rupees twenty-five lakhs or more.

In computing the specified number of companies in respect of which or any part of which any person or firm has been appointed as an auditor, whether singly or in combination with any other person or firm, shall be taken into account in computing the specified number as defined in *Explanation I* of section 224(1C).

COMPANES NOT COUNTED IN THE LIMIT ON NUMBER OF AUDITS

The following types of **companies shall be excluded** from reckoning specified limits, in terms of share capital:—

- (a) Guarantee companies (Department's Letter No. 8/12/(224)/74-CL-V, dated 28-9-74)
- (b) Foreign companies (Circular No. 21 of TSF No. 35/3/75-CL-III, dated 24-9-1975)

As mentioned above, as per the Companies (Amendment) Act, 2000 private companies will not be taken into account for counting the 20 number of companies audit as specified as per sub-section (1B) of section 224.

- (c) Branch audit of the Indian Companies not counted for calculating the specified number.
- (d) Foreign Company

Obligation of the auditor to give intimation to the Registrar

Every auditor appointed under section 224(1) by a company in annual general meeting shall inform the Registrar in writing that he has accepted, or refused to accept the appointment [Section 224(1B)]. The information shall be given in e-Form 23B within a period of thirty days from the date of appointment.

However, first auditors appointed by the Board of directors of a company pursuant to section 224(5) are under no obligations to give notice of their appointment to the Registrar.

Appointment of auditor by the Central Government (Regional Director) [Section 224(3)]

Section 224(3) provides that if no auditors are appointed or re-appointed at an annual general meeting of a company, the Central Government may appoint a person to fill the vacancy. Therefore, the power of the Central Government to appoint auditors becomes exercisable when no auditors are appointed or reappointed at an annual general meeting of a company.

The Company is required to give intimation electronically to the Regional Director (Powers of the Central Government were delegated to the Regional Director) *vide* Notification No. GSR 288(E) dated 31st May, 1991) in new e-Form 24A prescribed by Notification No. GSR 56(E) dated 10th Feb., 2006.

Obligation has been cast on the company that within seven days of the Central Government's power u/s 224(3) becoming exercisable, it shall give a notice of that fact to that Government; and if a company fails to give such notice, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to five thousand rupees.

Consequences of failure to pass a special resolution at an AGM for appointment of an auditor under section 224A:—

- (a) it shall be deemed that no auditor or auditors had been appointed by the company at its annual general meeting; and
- (b) the power of the Central Government under section 224(3), to appoint auditors becomes exercisable.

CASUAL VACANCY [Section 224(6)]

Meaning of casual vacancy in the office of auditor(s)

The expression 'casual vacancy' has not been defined in the Companies Act, 1956. Simply stated, a casual vacancy in the office of an auditor means a vacancy caused in the office of an auditor by his death, disqualification, resignation, etc.

Section 224(6) governs this aspect and relevant provisions are stated hereunder:—

- (a) The Board may fill any casual vacancy in the office of an auditor, but while any such vacancy continues, the remaining auditor or auditors, if any, may act.
- (b) Any auditor appointed in a casual vacancy shall hold office until the conclusion of the next annual general meeting.

Powers of the Board to fill up the casual vacancy only in case of death or disqualification of auditors

In terms of section 224(6)(a) where a casual vacancy arises in the auditors appointed by a company due to death or disqualification, the Board of directors may appoint another auditor.

Only members in general meeting may fill up the casual vacancy caused by resignation of auditors

If any casual vacancy in the office of an auditor is caused by the resignation of an auditor, such vacancy shall only be filled by the company in general meeting and the Board has no power to fill up the casual vacancy in this case.

The auditor appointed in a casual vacancy shall hold office till the conclusion of the next annual general meeting. If a casual vacancy arises, the remaining auditors if any, will continue to Act.

REMOVAL OF AUDITORS [Section 224(7)]

Board of directors has no power to remove an auditor

The Board of directors of a company has no powers to remove an auditor appointed by the company in general meeting. Accordingly, the said auditor can be removed only by the company in general meeting after receiving the previous approval of the Central Government under section 224(7). Powers has been delegated to the Regional Director vide Notification No. GSR 288(E), dated 31-5-1991.

Removal of auditor(s) with the prior approval of the Central Government

As per Section 224(7) an auditor can be removed before expiry of his term only by the company in general meeting after obtaining the previous approval of the Central Government (Power has been delegated to the Regional Director).

PROCEDURE for removal of auditors

The company shall take further action as prescribed in section 225 and make an application to the concerned Regional Director in e-Form 24A.

Time limit

The application has to be filed for appointment within seven days of the annual general meeting and for removal before general meeting.

REMUNERATION OF AUDITORS [Section 224(8)]

Section 224(8) discusses the manner of fixation of remuneration of auditors. Following are the provisions in this regard:

☐☐☐☐☐☐**Remuneration of first auditors**

Fixed by the Board, if the Board does not fix such remuneration then remuneration of auditors shall be fixed by the company in general meeting or in such manner as the company in general meeting may determine.

☐☐☐☐☐☐**Remuneration of other than first auditors**

The remuneration of auditors other than first auditors shall be fixed by the company in general meeting or in such manner as the company in general meeting may determine.

☐☐☐☐☐☐**Remuneration of auditors appointed to fill up causal vacancy**

Fixed by the Board, if the Board does not fix such remuneration then remuneration of auditors shall be fixed by the company in general meeting or in such manner as the company in general meeting may determine.

☐☐☐☐☐☐**Remuneration of auditors appointed by the Central Government**

The remuneration may be fixed by the Central Government. But if the CG does not fix such remuneration then company in general meeting may fix the remuneration.

Remuneration includes all expenses allowed by the company

For the purposes of section 224(8), any sums paid by the company in respect of the auditors' expenses shall be deemed to be included in the expression "remuneration".