Provisions relating to CSR, Accounts and Auditors

-Companies Act 2013

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KNOWLEDGE THAT MATTERS. EXPERIENCE THAT COUNTS.

What are we covering today

- Corporate Social Responsibility- Advisory Role
- Books of Accounts & Financial Statements
- Appointment, qualification and disqualification of Auditors
- Other Key Points including Recent Changes
- Key challenges in above

Corporate Social Responsibility

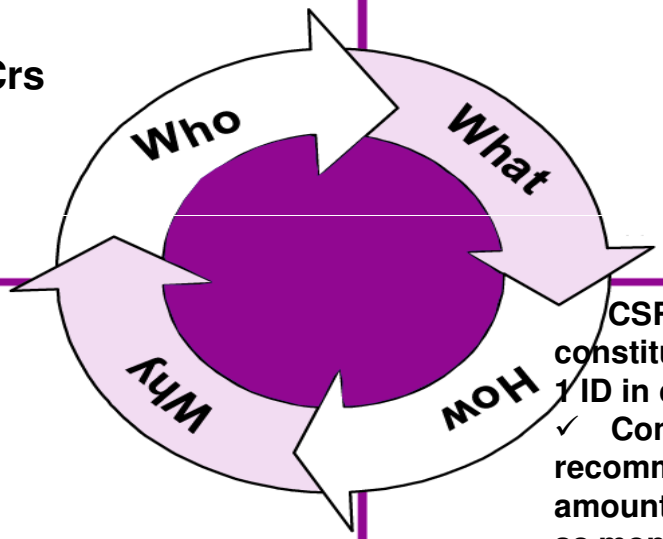
CORPORATE SOCIAL RESPONSIBILITY

✓ Networth ≥ 500 Crs or

✓ Turnover ≥ 1000 Crs or

 Net Profits ≥ 5 Crs

✓ CSR spend of at least 2% of avg. net profits made during 3 immediately preceding FYs



To promote welfare initiatives

CSR Committee to be constituted (3+ Dir incl. at least 1 ID in case of listed company)

✓ Committee shall formulate & recommend CSR policy & amount of expenditure as well as monitor CSR activities (CSR policy on web)

✓ Preference to local areas in which the company operates

✓ Areas specified in Schedule VII

CORPORATE SOCIAL RESPONSIBILITY

- CSR Activities to be undertaken as projects or programmes
- Excluding activities undertaken in pursuance of the normal course of business of a company
- In the area nearby the operations of the company
- May implement the same through trust/society set up by company or otherwise having track record of three years
- Activities to be undertaken within India
- Activities not exclusively for the benefit of employees or their family members
- Nature of projects to be covered for eradicating extreme hunger and Poverty, for promotion of education…..etc. as given in schedule VII

CORPORATE SOCIAL RESPONSIBILITY

- ‘spend or explain’ approach taken by the MCA

- FAQ issued by ICAI
  - Whether expense or appropriation
  - Whether provision for unspent amount to be made or not
  - Disclosure of expenses
- Tax deductibility of expenses/ donations
- Whether any penalty for non spending
- Applicable to all companies
- ICAI Corporate Social Responsibility Award
- MCA circular –broad guidelines as to what will or will not constitute CSR expenses

Books of Accounts &

Financial Statements

Books of Accounts & Rules

- Section 2(12): “book and paper” and “book or paper” include books of account, deeds, vouchers, writings, documents, minutes and registers maintained on paper or in electronic form;

- Section 2(13): “books of account” includes records maintained in respect of—
  - all sums of money received and expended by a company and matters in relation to which the receipts and expenditure take place;
  - all sales and purchases of goods and services by the company;
  - the assets and liabilities of the company; and
  - the items of cost as may be prescribed under section 148 (cost audit provisions) in the case of a company which belongs to any class of companies specified under that section.

Books of Accounts & Rules

- Section 128 of the Companies Act 2013- records can be prepared and kept in hard copy or in electronic mode (conditions as prescribed in Rule 3 of Companies (Accounts) Rules 2014 ('Rules') to be complied.

- Rule 3: Manner of books of account to be kept in electronic mode
  - Books of account & other records shall be accessible in India for subsequent reference.
  - Original format to be retained
  - Information contained shall remain complete and unaltered
  - Information received from branches shall not be altered and shall be kept in a manner where it shall depict what was originally received from branches.
  - Information shall be capable of being displayed in a legible form.

Books of Accounts & Rules

- Proper system for storage, retrieval, display or printout shall be there as audit committee if any or Board may deem appropriate.
- Such records shall not be disposed off or rendered unusable unless permitted by law.
- Back up of the books of account and other books and papers of the company maintained in electronic mode, including at a place outside India, if any, shall be kept in servers physically located in India on a periodic basis.
- Intimate to the Registrar of Companies (RoC) following details on an annual basis at the time of filing of financial statement.
  - (a) Name of the service provider;
  - (b) Internet protocol address of service provider;
  - (c) Location of the service provider (wherever applicable);
  - (d) Where the books of account and other books and papers are maintained on cloud, such address as provided by the service provider.

Books of Accounts & Rules

- First proviso to section 128(1)- records have to be retained at registered office or any other location in India as decided by Board of directors.

- In case records are maintained at any other location in India, notice has to be given to Registrar of Companies (RoC) within 7 days of Board's decision giving full address of that location. Similar conditions apply for every change thereafter.

- Non compliance -section 128 (6)- MD, WTD in charge of finance, CFO or any other person charged by Board with the duty to comply with Section 128 shall be punishable with imprisonment for a term upto 1 year or fine which shall not be less than Rs.50,000 maximum upto Rs.500,000 or with both.

Books of Accounts & Rules

- Section 134(3)(c) - Board of Directors in their Directors' Responsibility Statement are required to mention that the directors have taken proper and sufficient care for maintenance of adequate accounting records in accordance with the provisions of the Act & for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities.

- Section 143(3)(b) - Statutory auditor required to comment:
  - whether proper books of account as required by law have been kept by the company
  - proper returns adequate for the purposes of his audit have been received from branches not visited by him.
  - Further, clause (*h*) of section 143(3) of the Act requires statutory auditor to report any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith.

Maintenance of books of account [Section 128]

- No change in period of 8 years for which books of account to be retained
  - Financial statements to be retained for all years
  - Books and papers of company covered by following to be retained until permission for disposal sought & is granted by Central Government:
    - the Company which has amalgamated with the company or
    - of the company whose shares have been acquired by the Company under section 235 relating to dissenting shareholders or section 236 relating to minority shareholders
- In case where an investigation has been ordered, books of account have to be kept as may be determined by Central Government

Financial statements [Section 128]

- Financial year (FY) can only be from April - March
  - Shorter / extended period possible only in case of new companies. Earlier 15 / 18 months accounts were permitted.
  - Different FY possible for subsidiary of foreign company with tribunal approval. No exemption for associate & JV.
  - Existing companies has to align FY within 2 years
- Financial statements now defined & includes
  - Balance sheet,
  - Profit & Loss account,
  - Cash flow,
  - Statement of Changes in Equity (if applicable) and
  - Explanatory notes

Financial Statements

- Section 129- to be prepared as per Schedule III (erstwhile Revised Schedule VI)

- Consolidation financial statements:
  - Mandatory even for private companies
  - For one year 2014-15, CFS not necessary if only Associate or Joint Venture or foreign subsidiary
  - Not required for an intermediate wholly-owned subsidiary unless immediate parent is a company incorporated outside India

- CFS will also be placed before the shareholders in AGM

- Section 129(3)- 'subsidiary' shall include associate company and joint venture

Re-opening of Financial Statements (FS)- yet to be notified

- Section 130-Reopening on order of Court
  - Earlier accounts were prepared in fraudulent manner
  - Affairs of the company mismanaged casting a doubt on reliability of financial statements

- Section 131- Voluntary revision of FS or report of the Board
  - Revised FS for upto previous 3 years
  - Approval of Tribunal
  - Such revision not to be prepared or filed more than once in a financial year

- Earlier MCA Circular 1/ 2003 dtd. 13.01.2003 clarified that voluntary reopening of accounts possible to comply technical requirement of any other law to give true & fair view.

Eligibility of auditors [Section 141]

- Eligibility for appointment of auditor:
  - Individuals who should be a CA
  - A firm with majority of partners practicing in India
  - LLP if registered with ICAI

Disqualification of auditors [Section 141]

- Additional disqualification added
  - Holding any securities of or interest by relative or partner in the company, subsidiary, holding, associate (exemption upto face value of Rs.1 Lac for relative of an auditor)
    - Corrective action to be taken by auditor within 60 days of such acquisition or interest
  - Given any guarantee / provided any security by himself, relative or partner to the subsidiary, holding, associate or fellow subsidiary (exemption upto Rs.1 Lac)
  - Maximum of 20 companies allowed. Even private companies are included in the limit

Disqualification of auditors (contd..)

- Indebted to subsidiary, holding, associate or fellow subsidiary (exemption upto Rs.5 Lacs.)
- Person or firm has any business relationship
  - Term business relationship is explained in Rules
- Person convicted by court for fraud & 10 years has not elapsed
- Person whose relative is a director / KMP (section 2(51) of the Company
- Any person(individual / Firm / LLP) whose subsidiary, associate or any other form of entity is engaged in consulting or specialized services as prescribed u/s 144

Disqualification of auditors (contd..)

- As per Rules its clarified that Business relationship shall be construed as any transaction entered into for a commercial purpose except
  - Commercial transactions in the nature of professional services permitted to be rendered as an auditor under the Act and CA Act
  - Commercial transactions which are in ordinary course of business of the company at arm's length price. E.g. sale of products/services to auditor by companies engaged in telecommunications, airlines, hospitals, hotels and such other similar business.

Disqualification of auditors (contd..)

- In case of auditors of listed companies, auditor has to mandatorily obtain ‘Peer Review certificate’ from Peer Review Board of the ICAI.

Consent of Auditor [Section 139]

As per 2nd proviso to section 139(1) auditor has to give a written consent to become auditor of the company & a certificate stating that appointment is in accordance with conditions prescribed.

- The person being appointed is eligible for appointment and is not disqualified for appointment under the Act and the CA Act.
- The proposed appointment is as per the term provided under the Act.
- The proposed appointment is within the limits laid down
- The list of proceedings pending with respect to professional matters of conduct, as disclosed in the certificate, is true and correct.
- Holding valid peer review certificate (if applicable)

Intimation to ROC for appointment of Auditor [Section 139]

The company shall inform the auditor regarding appointment/ reappointment and also file a form ADT-1 to ROC within 15 days of the meeting in which the auditor is appointed.

- Generally observed that ADT -1 are filed beyond due dates with penal fees
- Also observed that companies are filing ADT-1 without receiving consent letters from Auditors. Instead of consent letters, companies are attaching eligibility letters along with ADT-1.
- ADT-1 to be pre certified
- Additional fees is payable on delay in filing of forms [minimum one time of normal fees on delay of 15 days to maximum 12 times on delay of 180-270 days]

Rotation of auditors

- Compulsory rotation of auditor every 5 years
  - Calculation has to be done with retrospective effect (as per Rules)
  - Appointment of auditor would be for a term of 5 years and at every AGM such appointment is to be ratified by the shareholders
- Individual as an auditor can not be reappointed after 5 years
- Audit firm is eligible to be reappointed for another term of maximum of 5 years. Thereafter cooling period of five years.
- Company can also resolve that auditing partner and his team shall be rotated at prescribed intervals

Rotation of auditors (contd..)

- Rotation applicable to following except one person company and small companies
  - Listed companies
  - Unlisted public companies having paid up share capital of Rs.10 crores or more
  - Private companies having paid up share capital of Rs.20 crores or more
  - All unlisted public companies and private companies not covered above but has public borrowings from financial institutions, banks or public deposits of Rs. 50 crores or more at any time during the year

Rotation of auditors (contd..)

- Individuals/ Firms not eligible for reappointment in following cases
  - Audit firm having common partners can not be appointed after the rotation period
  - Individual or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under same network which includes operating or functioning hitherto or in future under same brand name, trade name or common control (as per Rules)
  - If existing partner retires and joins other firm, such other firm shall also be ineligible (as per Rules)

Rotation of auditors (contd..)

- Transitional period of 3 years given to comply with rotation.
- As per the illustration given in the Rules, rotation would apply as under in case of firm:

No. of consecutive years completed as auditor (in the first AGM held after 1st April 2014)	Maximum years including transitional period	Aggregate period which the firm would complete in the same company
10 years or more	3 years	13 years or more
9 years	3 years	12 years
8 years	3 years	11 years
7 years	3 years	10 years
6 years	4 years	10 years
5 years	5 years	10 years
4 years	6 years	10 years

Rotation of auditors (contd..)

- Auditor shall hold office till conclusion of the 6th AGM
- Appointment has to be ratified in every year's AGM
- If not ratified, board shall appoint auditor as per the procedure prescribed
- Before appointment, auditor to give written consent and a certificate that appointment if made, shall be in accordance with conditions prescribed in Rules
- In case of Joint Auditors, rotation to be planned so that they do not complete their terms in the same year.

Casual Vacancy [Section 139(8)]

- Any casual vacancy in the office of an auditor shall be filled by the Board / CAG within 30 -60 days as the case may be.

- Additionally if casual vacancy is due to resignation of an auditor, such appointment shall also be approved by the company at a general meeting.

Removal and Resignation of Auditors [Section 140]

- Removal before expiry of term only by a special resolution

- After obtaining the previous approval of the Central Government [Form ADT-2].
  - Form to be filed within 30 days of resolution passed by the Board
  - Pass special resolution in general meeting within 60 days of receipt of approval from Central Government

- The auditor concerned shall be given a reasonable opportunity of being heard.

- Auditors resignation-
  - file form ADT-3 within 30 days from the date of resignation
  - with the company & ROC & also to indicate the reasons for resignation.
  - In case of non compliance- minimum fine of Rs.50,000 extendable to Rs. 5 lacs

Auditor not to render certain services [Section 144]

- Auditor can render other services subject to approval by Board or Audit Committee. Following services cannot be rendered directly or indirectly
  - Accounting and book keeping services
  - Internal audit
  - Design & implementation of any financial information system
  - Actuarial services
  - Investment advisory services, Investment banking services
  - Outsourced financial services
  - Management services
  - Other services as may be prescribed (presently not prescribed in Rules)

Auditor not to render certain services (contd..)

- In case of audit firm, restriction of services also apply to services rendered by any of
  - its partners,
  - its parent, subsidiary or associate,
  - any other entity in which firm / partner has significant influence/control or whose name/trade mark/brand is used by the firm or any of its partner
- Services rendered directly or indirectly to the Company or its holding company or subsidiary company are also covered.
- Transition provision given to comply with the provisions for such non-audit services - Time limit of one year

New Reporting Requirements

- Whether the company has disclosed impact of pending litigation on its financial position in its financial statement
- Whether the company has made provision as required under any law or AS, for material foreseeable losses, if any, on long term contracts including derivative contracts
- Whether there has been any delay in transferring amounts, required to be transferred, to the IEPF by the company
- Reporting of fraud by auditors under ADT -4 [GN issued on fraud reporting]
- Observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company [GN issued]

New Reporting Requirements [continued]

- Any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith [GN issued]
- Whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls [GN withdrawn and reporting is not mandatory for FY 2014-2015]
- Reporting under CARO 2015 [Guidance note also issued]
- CARO 2015 also applicable to Consolidated Financial Statements

Other Key Points – including Recent Changes

- Compliance with Auditing Standards mandatory
- Sec 146-Auditor (or authorised representative) to attend all general meeting unless exempted by Company (general penalty can be levied u/s 450). If company fails to give notice- minimum fine 25000 & extend upto 5.00 lac, every officer imprisonment upto 1 year or with minimum fine of Rs. 10,000 & extend upto 1.00 lac or both
- As per Rules, criminal liability of audit firm shall devolve only on the concerned partner who acted in fraudulent manner. Liability of fine will be on the firm.

Key challenges / Impact

Key challenges

- To unlearn the old Act
- Extensive usage of Rules - integral part of compliance
- Absence of legal precedents
- Complete revamping of Audit check lists

Thank You

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