

# Companies Bill 2012

## Accounts , audit and inspection

By

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# **SOME KEY PROVISIONS-ACCOUNTS**

## S 52 (S 78)

- **Securities premium:**
- For prescribed class of companies following set off against securities premium will not be permitted:
  - Issue of fully paid preference shares
  - w/off expenses /commission/discount on preference shares/debentures
  - W/off of preliminary expenses
  - **Providing premium payable on redemption of redeemable preference shares /debentures**

# S 123 (S 205)

- **Depreciation:**

Schedule II	Schedule xiv
Useful life and residual value prescribed (generally not more than 5%)	Depreciation rate prescribed
Straight line after considering residual value (also no. of production units)	Straight line and WDV ; revenue based amortisation for infra cos.
a) Cos complying with AS –use rates/values or justify other nos. b) Regulated cos-regulatory authority prescribed rates; c) other cos- not higher than prescribed	One rate for all cos as minimum rate
Useful lives increased/decreased as compared to Sch xiv- ex. ocean going liners 25 years (20); Furniture 10(15) – <b>higher charge will result</b> in general esp. when assets nearing end of life	Generally depreciation was lower – Compare useful lives for non RCC frame buildings 58 years (now 30!); CPP: 18 years (now 8!)

# S 123 (S 205)

- **Depreciation contd.:**

Schedule II	Schedule xiv
Componentisation required (note 4)	Componentisation was not required; allowed under AS 10
No 100% depreciation	100% depreciation for assets costing less than Rs 5000
No ESA rate- 50% more for 2 shifts; 100% more for 3 shifts for period	Rates specified for ESA
More sub divisions in individual assets like for Buildings ; separate rates for some industries;	Less sub divisions and less industries
Where remaining useful life nil charge to Opening retained earnings	Always to Statement of P&L
Revalued assets –depreciation to P&L?	The differential depreciation was taken to revaluation reserve

# S 129 (*S 211*)

- Consolidated Financial statements:
  - Where any company has a subsidiary (which definition includes associate or JV Co)
    - Consolidated FS to be prepared and laid before AGM along with standalone FS (now for all cos)
      - If no subsidiary but associate/ JV is there will consolidation apply?  
It looks like
    - Option to prepare under IFRS per listing agreement goes
  - CG may provide rules for consolidation of accounts
    - Statement containing salient features also continues!
      - Will apply to associates and JV also now

# S 129 (*S 211*)

- Conflict between Co law and Accounting standard:
  - Subsidiary definition in S 2(87) states ‘control of more than one-half of total share capital’ whereas in AS 21 it is “one-half of the voting power”
    - For purposes of CFS, AS definition may prevail
    - For statement to be enclosed, Co law definition will have to be used
  - Also S 2 (87) talks of control of composition of board of directors only, whereas AS 21 has in addition “to obtain economic benefits from its activities”

# S 129 (*S 211*)

- Consolidated FS issues:
  - Do we have to give all the disclosures per Sch III in CFS also as in standalone?
    - I guess not.
      - as Sch III states the schedule will be followed **mutatis, mutandis** (ie with necessary changes)
      - Also AS 21 gives exemption from statutory information (Cl 6 exp c)
      - Such information on an aggregate basis may not really help users of FS but confuse them!
        - » For instance: what is the earthly use of aggregating audit fee of all group cos or disparate information like raw materials or goods purchased which make sense only for standalone cos; or imports and expenditure in foreign currency of foreign subsidiaries?



# S 130 /S 131 –new

- **Reopening/recasting of accounts – Court/Tribunal order (130)/ Voluntary (131):**
- Who can apply?
  - CG
  - IT authorities
  - SEBI
  - Any other statutory/regulatory authority
  - Board/Company- S 131
- To
  - Court /Tribunal – S 130
  - Tribunal – S 131

# S 130/ S 131-new contd.

- **Reopening contd.**

- Conditions for reopening S 130

- Accounts prepared in fraudulent manner
- Affairs of the company was mismanaged during the relevant period casting a doubt on reliability of FS

- Conditions S 131

- FS or Board report not in compliance with S 129/S 134

## **S 130/ S 131- contd.**

- Notice to same authorities only viz CG, IT, SEBI, other statutory regulatory body S 130
- Notice to CG, IT S 131
- Reopening/recasting only on order by court/Tribunal S 130 / Tribunal S 131
- Accounts so recast shall be final S 130

# **S 130/S 131 –New contd.**

- S 131 – revision of FS/Board report
  - Revision for any of the 3 preceding FY
  - Not more than once in a FY
  - Detailed reasons to be disclosed in Board report
  - Where already filed with ROC revision to be confined to correction to the extent of non compliance with S 129/S 134 and consequential corrections
  - CG to frame rules including functions of company auditor
- Recently SEBI issued circular which empowers it to order revision of FS –thus there are 3 ways

# **S 130/S 131 –new**

- **Questions that arise:**

- How many years can be reopened not clear in S 130
- For application by authorities nothing provided for opportunity of being heard to Company! S 130
- Finality is provided in S 130 not in S 131!
- S 131 revisions every year possible!
- Revision of CFS possible?

# S 132 – NFRA (S 210A)

- NACAS becomes NFRA
- Reach extends to audit standards and overview of audit profession also
- NFRA has powers to investigate professional or other misconduct
  - Suo moto or on reference by CG
  - ICAI can't initiate/ continue any proceedings where NFRAS initiates action
  - Misconduct of CFO/Co. officials also covered
- Nfra has powers of civil court

## S 132 NFRA contd.

- Penalty action if member(CA) proved guilty
  - Penalty not < Rs 1Lakh upto 5 times fees received for individual
  - Penalty not < Rs 10 lakhs upto 10 times fees received for firms
    - Fees for how many years?
  - Debarring member or firm min. 6 months max. 10 years
- Appeal to Appellate authority possible

# S 135 CSR

- Applicable to:
  - Company with
    - networth Rs 500 cr or more or
    - Turnover Rs 1000 cr or more or
    - Net profit Rs 5 cr or more in any FY
- Constitute CSR committee –
  - 3 or more directors at least one being independent
- Spend
  - At least 2% of average net profit of 3 immediately preceding FY (per S 198)



# S 135 CSR

- CSR committee to:
  - Formulate and recommend to Board corporate social responsibility policy (CSR) –activities to be undertaken per sch vii
  - Recommend amount to be spent
  - Monitor CSR
- Board to
  - Approve CSR , place it on website
  - Ensure CSR activities undertaken per policy
- Schedule III requires
  - Disclosure of CSR expenses

# S 136, 137 ( S 219, 220)

- **Copies of FS /filing:**
  - CFS also to be sent to members etc
  - **Listed** co can send statement containing salient features to members etc provided it makes them available for inspection at regd office (in view of cl 32 they can't send abridged CFS)
  - Listed cos to place CFS and standalone FS on website
  - All companies with subsidiary need to place separate audited a/cs of subsidiary/ies on **website**
    - **Thus unlisted cos having subsidiary need a website? and**
    - Need not place the holding co a/cs or cfs on website!

# S 138

- Internal auditor
  - Such class of cos as may be prescribed
  - Shall appoint a
    - Ca or
    - Cost accountant or
    - Such other professional as decided by Board
- CG rules for manner /intervals of IA
- Internal auditor should include a firm also?

# **SOME KEY PROVISIONS –AUDIT**

## S 139 (S 224)

- Audit appointment till conclusion of 6<sup>th</sup> agm (*against* conclusion of next agm)
  - Ratification at AGM every year
- Company to inform auditor and ROC (*auditor was filing F 23B*)
- Audit committee to recommend auditor
- Listed and other prescribed class of cos to rotate auditor
  - If individual after 5 years
  - If firm after 10 years
    - Cooling period 5 years after such rotation

## S 139 (*S 224*) *contd.*

- Rotation of auditors in listed and other prescribed cos (contd.)
  - No audit firm with common partner of firm whose tenure has expired, to be appointed for 5 years
  - For existing cos/auditors 3 years' time provided to comply
    - Thus a firm which has continued for say 7 years has 3 more years to comply
    - A firm which has completed even 30 years on the date the law comes into force will also have 3 years to comply
  - Members may decide on audit partner team rotation and joint audit
  - CG To prescribe rules for rotation

# S 141 (S 224(1B)/ 226)

- Additional disqualifications:
  - Relative, partner can't hold security or interest in company (above Rs 1000 FV) in the Company/ subsidiary /holding co/ associate/ subsidiary of holding co
  - Relative , partner can't be indebted (or give guarantee or provide security) to the company/subsidiary/holding co/associate / subsidiary of holding co

# S 141 (S 224(1B)/ 226) contd.

- Additional disqualifications contd.
  - Auditor or firm directly or indirectly can't have business relationship with Company/ subsidiary or holding co/associate /**associate** or subsidiary of holding co. as prescribed. (S 141(3)(e ))
  - Auditor can't have a relative as a director or whole time director, or KMP in the Company
  - Auditor not to have more than 20 audits (previous exemption of private companies no longer available; even S8 cos included? What about CFS/Branch /Joint audits?)



## S 141 (S 224(1B)/ 226) contd.

- Additional disqualifications contd.
  - Person convicted by a court of an offence involving fraud for 10 years
  - Provision of specialized services u/s 144
- Previous extension of disqualification of an auditor disqualified in subsidiary or holding company or a co-subsiary –is removed now

# S 141 ( S 224(1B)/226)

- Issues:
  - The list is too long
  - Checking what shares relatives hold or what they owe is going to be a nightmare- we will need to take declarations!
    - A spouse who wants to divorce can easily put the auditor to difficulty by buying shares for FV of Rs 1001 in cos where he is auditor!
  - Relative or partner can't owe money or hold shares but can have business relations!
  - As auditor includes firm , firm cannot hold shares or have debts due also (expl. 2 S 140)
  - We should await rules to see what is 'business relationship'

# S 143 (S 227)

- Enquiry by auditor
  - Good old 6 clauses u/s 227(1A) still there! WHY?
- Holding company auditor to have access to subsidiary records so far as it relates to consolidation
  - SA 600 is not yet mandatory in India but does this mean holding co auditor is responsible for subsidiary also even if audited by another CA?
  - Auditor does not have access to associate/JV company books still

# S 143 (*S 227*)

- *Italics* /**Bold** for qualifications no longer exists
- Report to have additionally:
  - Observation or comments on financial transactions or matters which have any adverse effect on functioning of the Company
  - Any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith
  - Whether company has adequate internal financial control system in place and the operating effectiveness of such controls
  - Such other matters prescribed
- CG may prescribe audit standards or addendums!

# S 143 (S 227)

- Reporting fraud to CG:
  - Presently only in respect of money laundering there is a requirement to report to CG (Implementation of S 51A of Unlawful activities (Prevention) Act 1969 ICAI circ. dated 22 Apr 2010)
  - Now if an auditor has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company he shall report it to CG within such time in such manner as may be prescribed
  - No duty of auditor regarded as contravened if such reporting done in good faith

# S 143 (S 227)

- Reporting fraud to CG:
  - Are we opening a Pandora's box?
  - Will aggrieved auditors report/ send reports to CG to take revenge on management?
  - No materiality is mentioned here!
  - What about past frauds?
  - Officers will include directors also! There is no mention of notice being given to the directors/ officers /employees!

# S 143 (S 227)

- **Other Issues:**
- Equivalent of CARO u/s 227(4A) – S 143(11) what it will contain we need to wait and see
- Observations on adverse effect on functioning of co- does it mean propriety audit? Does it extend audit responsibility?
- Reporting on adequacy of IC and effectiveness of IC is going to be Herculean task! Not required anywhere in the world! SA also does not require this! (Caro talked of only 2 –sales and purchase)

# S 144 new

- **Non audit services -directly or indirectly to Company/ Holding /Subsidiary:**
  - To be approved by Board or audit committee other than following:
    - Accounting; Internal audit; Design and implementation of Financial info system; Actuarial services; Investment advisory ;Outsourced financial services; Management services; Others as prescribed
      - Existing work- To comply with before closure of first FY
- Applies to auditor, firm, partners, parent, subsidiary/ associate/ any other entity where firm/partner has significant influence/ control or common trade mark/ brand



# S 144 new contd.

- Non audit services -directly or indirectly to Company/  
Holding /Subsidiary:
  - Issues:
    - List is too long but **associate** is not covered but what about S 141(3)(e)?
    - IFAC / IESBA code do not prohibit these services in all companies; stricter rules apply to **only Public interest entities**- so this is harsher than International standards
    - If Company or subsidiary abroad obviously the restriction can't apply?
    - What is management services? S141(3)(i) talks of consulting and specialized services
    - The limit of statutory audit fee as prescribed by ICAI has no applicability now ?
    - indirect recognition to multi national firms? (trade mark/brand)

# Penal provisions

- Penalties /prison time go up sky high!
- Refund of remuneration/ paying damages etc contemplated
- Liability extends to partners who have acted in a fraudulent manner also.
  - Will it cover, for instance, an engagement quality control reviewer who may not have the full facts?
- Joint and several liability to firm/partners
- Action by NFRA/ Tribunal provided for
- Class action suits arrive in India
- Will an LLP help at all?
- Will audit be a very onerous and thankless job?
  - TIME ALONE WILL TELL US
  - GOD HELP US!

**SOME OTHER KEY PROVISIONS  
RELEVANT FOR AUDIT**

# S 2(57) Net worth

- Reserves created out of
- Write back of depreciation and amalgamation
- Excluded
  - As auditors we need to note this carefully.

# Sec 5(3) entrenchment-New

- The articles can now contain provisions for entrenchment –
  - ie. specified provisions of the articles may be altered only if conditions or procedures that are more restrictive than those applicable in the case of a special resolution, are met or complied with
- We should as auditors to ensure that If there is such a provision in articles, resolutions passed are as prescribed
- Similarly if Board meeting called at short notice and no independent director present, whether independent director has ratified decisions later (S 173(3))

## S 180/181/182 (S 293/293A)

- The clause regarding investment in trust securities now applies to compensation received by company *as a result of merger or amalgamation*
- Donations now for bona fide charitable and other funds above 5% of average net profits for 3 immediately preceding years will require *prior* permission of company in general meeting. (*Rs 50000 lower limit removed*)
- Political parties donation hiked to 7.5% from 5%

## S 185- Loans to directors etc. (S295)

- Loans /guarantees /providing security to director or any other person in whom director interested prohibited (director of lending co or holding co or partner/relative of such director; any firm where such director or relative is partner; private co of which such director is director or member; any BC where over 25% voting power exercised by such director/directors together; or where Board is accustomed to act according to instruction of board or directors of lending co)
  - Except for
    - loan to MD/WTD as part of service condition extended to all employees or per scheme approved by members by special resolution
    - Loans in the ordinary course at rates of interest not less than bank rate

# S 186 -Loans/investments(S 372A)

- Only two layers of investment companies
  - Unless acquiring another company out of India
  - Subsidiary having investment subsidiary to meet requirements of any law
- Giving of loans/guarantee/security extended to any person/body corporate (not only corporates)
- Prior approval by special resolution needed if limits exceeded for loans/Guarantee/security/Investment (i.e 60% of PUC/Free reserves/Securities premium or 100% of free reserves incl. securities premium)



# Loans/investments contd.

- No loans /investments if in default of repayment of deposits
- Rate of interest not less than prevailing yield on 1 year/3 years/ 5 years /10 years Government security, closest to tenor of loan (previously bank rate)
- Disclose in FS details of loans/investments/guarantee/security, purpose
- No exemptions for private cos, wholly owned subsidiary etc
- CG may make rules

# S 188-Related party transactions (S 297)

- Related party definition widened
- Special resolution required for related party transactions exceeding prescribed amount and no vote by a related party (wrongly mentioned as 'not exceeding' in section) and paid up share capital (previously CG approval if PUC over Rs 1cr)
- New items now brought under related party transactions if not on an arm's length basis:
  - Leasing of property; selling/buying property; appointment of agents for purchase/sale of materials/service/property; appointment to office or place of profit in Company/subsidiary/associate; underwriting securities/derivatives
    - Arm's length V IT department Transfer pricing?
    - How to determine arm's length? And document?

# S 192-Non cash transactions -directors

- Director of company/holding/subsidiary/associate co. or person connected with him (not defined) requires prior approval of Company in GM (also GM of holding co if director of holding co) for:
  - Acquiring assets from Company or
  - For Company to acquire from the above
    - for consideration other than cash

# S 197/Sch V –Minimum managerial remuneration

Sr. No.	Slabs for Effective Capital	Limits on yearly remuneration not exceeding (can be double if approved by Special resolution)
1.	Negative or less than Rs. 5 crores	Rs. 30 lakhs
2.	Rs. 5 crores and above but less than Rs. 100 crores	Rs. 42lakhs
3.	Rs.100 crores and above but less than Rs. 250 crores	Rs. 60 lakhs
4.	Rs. 250 crores and above	Rs. 60 lakhs plus 0.01% of the effective capital in excess of Rs. 250 crores

# S 221 Freezing of assets-New

- The Tribunal, on reference made to it by the Central Government or in connection with any inquiry or investigation into the affairs of a company or on any complaint made by such number of members as specified or a creditor having Rs 1 lakh amount outstanding against the company or any other person
- having a reasonable ground to believe that the removal, transfer or disposal of funds, assets, properties of the company is likely to take place in a manner that is prejudicial to the interests of the company or its shareholders or creditors or in public interest,
- it may by order direct that such transfer, removal or disposal shall not take place during such period not exceeding **three** years as may be specified in the order or may take place subject such conditions prescribed

# Final word..

- This is only half the story...
- The rest is coming by way of many rules
  - and
- We need to keep pace with the changes in the rules also

**OTHER PROVISIONS-  
ACCOUNTS/AUDITING**

# S 2 (41)

- **Financial year**
  - Uniformly Mar 31
  - A holding/ subsidiary of foreign co. can follow different FY with permission of Tribunal
    - Two years time for conversion to Mar 31
- **Result:**
  - More work for companies and auditors due to peaking up



# S 2 (85) new

- Small company
  - Paid up share capital- Rs 50 lacs to Rs 5cr as prescribed
  - Turnover per last P&L –Rs 2cr to Rs 20cr as prescribed (Rs 50cr under AS)
    - Exempt:
      - Holding or subsidiary
      - S 8 co
      - Cos under special act

## S 2 (85) contd.

- **Small company-Issues:**

- Definition different from AS for SMC which is
  - TO not exceeding Rs 50 cr (Cos bill says Rs 2 to 20cr as prescribed)
  - Criteria reg. Borrowings Rs 10cr not there in Cos bill
- So cash flow statement becomes applicable for companies with turnover per cos bill limit which is smaller;
- What about companies with Turnover less than co. law limit but borrowings exceeding Rs 10cr ?

# S 123 (S 205)

- **Dividends:**

- Transfer of current profits to reserves rule go- transfer will be at discretion of company
- No power to declare dividend without providing for depreciation with CG approval
- Interim dividend:
  - Out of surplus in P&L and out of profits of the FY
  - If loss during CY upto previous quarter , rate not to be higher than average dividends during immediately preceding 3 FY
- Declaration of dividend out of reserves to be as per rules
- No dividend if S 73/74 (deposits acceptance and repayment) not complied with

# S 128 (S 209)

- **Books of accounts-Type/details:**
  - Recognises electronic mode
  - *No details of account books like money received, expended , assets and liabilities and cost of material and labor (S 209(1)(d)) in new bill*
- **Branch:**
  - Branch returns periodically (*previously not more than 3 months*)

## S 128 (*s 209*) contd.

- **Inspection:**
  - Inspection of subsidiary books by a person authorised by a resolution of Board
- **Preservation of books:**
  - in case of investigation under ch xiv, CG may direct longer period than 8 years

## S 128 (s.209) contd.

- **When books not maintained:**
  - No longer to have defence that *a competent and reliable person was charged with the duty*
  - *Willful offense* not required for imprisonment
- **Responsible person:**
  - *Director (where no MD) and every officer removed*
  - Now it is MD, WTD and CFO or any other person charged by Board with the duty

# S 134 (S 215-217)

- **Authentication of FS:**

- Chairperson where authorised by Board or
- Two directors including MD/CEO director
- **CFO** (need not be director)
  - New /onerous requirement for **all** companies;
  - Previously only in listed companies he was required to sign a certificate that FS are free from material misstatement.
- **Secretary**
  - Does this mean if Chairperson is authorised by Board he only need sign FS?

## S 134 (*S 215-217*) contd.

- Board report to also include:
  - Extract of annual return
  - Number of meetings of Board
  - Director's responsibility statement
  - Statement on declaration by independent directors
  - Policy on director's appointment and remuneration



# S 134( S 215-217)

- **Directors report contd.**
  - Explanation by board on qualifications etc in **secretarial** audit report
  - Contracts/arrangements with related parties
  - **Risk management policy including elements of risk which may threaten existence of company**
    - **Previously this was restricted to listed cos**
  - CSR initiatives
  - For listed and other prescribed cos
    - Annual evaluation of performance of board, committees and directors
  - Others as may be prescribed
    - Board report to include summary of CFS results also?

# S 134 contd.

- **Directors' responsibility statement**
  - Applicable AS followed
  - Selection and application of accounting policies , making reasonable and prudent judgments and estimates to give true and fair view of FS
  - Proper /sufficient care for maintenance of adequate accounting records for safeguarding assets and for preventing/detecting fraud/irregularities

# S 134 contd.

- **Directors' responsibility statement contd.**
- Prepared accounts on going concern basis
- Proper systems to ensure compliance with provisions of all applicable laws and such systems were adequate and running effectively
- Constitution of CSR committee where applicable ; disclose CSRP and reasons for not spending 2% of avg profits on CSR (S 135)
- In listed company,
  - Laid down internal financial controls to be followed by the company
  - These internal financial controls are adequate and operating effectively

# S 134 contd.

- **Directors' report contd**
- **Internal financial controls**
- policies and procedures adopted by the Company for ensuring orderly and efficient conduct of its business including
  - adherence to company's policies,
  - safeguarding of its assets ,
  - the prevention/detection of frauds and errors ,
  - the accuracy and completeness of accounting records, and
  - the timely preparation of financial statements

# Other sections

- Board report to include:
  - Every contract/arrangement with related party along with justification (including non cash transactions)

# S 140 (S 225)

## **Auditor removal**

Special resolution and previous approval of CG required

By Tribunal suo moto or application made, if it is satisfied that auditor has directly or indirectly acted in a fraudulent manner or abetted or colluded in any fraud by or in relation to company or its directors or officers

By Tribunal if application is made by CG

If Tribunal passes order, auditor debarred for 5 years and also liable for action u/s 447

Liability of firm and every partner who acted in fraudulent manner or abetted or colluded in the fraud

# S 140 (S 225)

## **Auditor resignation**

Auditor to file a statement indicating reasons for resignation within 30 days

Fine not filing- Rs 50k to Rs 5 lakhs!

**Even resignation is not easy!**

## S 447 (new)

- S 447 defines fraud and hence is very important from auditor's view point.