

## AUDIT COMMITTEE

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### Abstract:

*The Audit committee has occupied a prominent position in the corporate governance. Audit committees maintain communication with the company's chief financial officer and controller. It refers to a body in a form that is responsible for choosing an audit firm, guiding the auditors, reviewing reports made by auditors and also informing the top managers of the results of the auditing process. This committee also determines the type of audit to be carried out and why it is necessary. The audit committee's role includes the oversight of financial reporting, the monitoring of accounting policies, the oversight of any external auditors, regulatory compliance, and the discussion of risk management policies with management. . In the present study we are analysing the conceptual framework of audit committee, and the various changes made from time to time in the legal provision of audit committee.*

### Purpose/objective of the study

The purpose of this study is to analysis the working of audit committee  
What changes have been made in the audit committee from time to time

**Methodology adopted for the study:** secondary sources have been used for the study. Various journals, articles, websites have been used to assess information

**Key Contribution:** The study will help to understand the concept of audit committee why it should be there in every organisation, in this process, the affected individuals, companies, and society at large are likely to benefit

### INTRODUCTION

An audit committee refers to a body in a form that is responsible for choosing an audit firm, guiding the auditors, reviewing reports made by auditors and also informing the top managers of the results of the auditing process. This committee also determines the type of audit to be carried out and why it is necessary.

### SOME DEFINITION OF AUDIT COMMITTEE

**Institute of Internal Auditors definition:** "The Audit committee refers to the governance body that is charged with oversight of the organization's audit and control functions. Although these fiduciary duties are often delegated to an audit committee of the board of directors, Practice Advisory is also intended to apply to other oversight groups with equivalent authority and responsibility, such as trustees, legislative bodies, owners of an owner-managed entity, internal control committees, or full boards of directors".

Please cite this Article as : Poonam and Yashpal , "AUDIT COMMITTEE" : Tactful Management Research Journal (May ; 2014)

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In Nigeria, the Audit Committee is defined as a “Committee of Directors and the enterprises shareholders representatives whose specific responsibility is to review the annual financial statements before submission to the Board of Directors”.

### OBJECTIVE/PURPOSE

The object of having the Audit Committee is to provide an overview on the reporting process of the Company's financial and accounting matters and the disclosure of its financial statements in a correct, sufficient and credible format. The Audit Committee's primary purpose is to:

#### 1. Assist the Board in its oversight responsibilities to shareholders, specifically with respect to:

The integrity of the Company's financial statements,  
the Company's compliance with legal and regulatory requirements the qualifications and independence of the independent auditor and internal auditing function,  
the performance of the Company's internal audit function and independent auditor  
the risks associated with the foregoing

#### 2. Prepare the audit committee report required by the SEC's proxy rules to include in the Company's annual proxy statement.

Audit committee under section 292A companies act 1956

When it was first introduced in India

Audit committee comes under the companies act 1956 under section 292A. A new Section. 292A has been inserted in the Companies Act, 1956 by the Companies (Amendment) Act, 2000, which puts obligation on certain companies to form Audit Committees. This obligation can be fulfilled by the Board of Directors by forming the audit committees. As per the new S. 292A, the Audit Committee should be constituted immediately after the Amendment Act comes into force.

Which type of companies are covered

As per the provision of the act, every public company which has paid up capital of Rs.5.00 crore or more must constitute an audit committee. In other words the company must be a public company and it must have minimum paid up capital of Rs.5.00 crore.

From which date is it applicable:

The Companies (Amendment) Act was notified on 14-12-2000 and it has come into operation from that date. Therefore, the provisions of S. 292A are applicable with effect from 14-12-2000.

#### How many directors should an Audit Committee have:

Audit Committee shall have minimum three (3) directors. There can be more number of directors if the Board of the Company so decides.

Two-third of the total members of audit committee shall be other than the managing or whole-time directors.

As and when Audit Committee meeting is called, it is obligatory on the part of the committee to have discussions with the Auditors, Internal Auditors (if any) and Director-in charge of finance.

#### Who will take part in Audit Committee meetings:

Audit committee include audit Committee members, Internal Auditors and Director-in charge of finance shall be taking part in the Audit Committee meetings.

#### Frequency,

S. 292A is silent about the frequency of the Audit Committee meetings. In other words periodicity of meeting is not specified in the Section. Frequency of the audit committee meetings has to be decided by the Board of Directors

#### Quorum:

There is no mention about the quorum of the Audit Committee Meetings.

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This has also to be decided by the Board of Directors. In case board is also not deciding then the quorum of normal board meeting should be assumed to be the quorum of Audit Committee meetings.

Attendance record should be maintained and signed by the members present in the meeting.

### **Chairman of the Audit Committee:**

The audit committee is to elect chairman who will attend the annual general meeting. It is common practice that for conducting the meetings of the Board of Directors, a chairman is elected. Similarly, Ss.(3) provides for the election of the chairman of the audit committee. The authority for appointment of Chairman of the Audit Committee is vested in the members of the audit committee. Accordingly the members shall elect a chairman from amongst themselves.

### **Secretary of the Audit Committee:**

There is no specific mention in the Section about the Secretary of the Audit Committee. Therefore, this point has also to be decided by the Board of Directors. In case board is also not deciding then the Secretary of the Company will act as the Secretary of the Audit Committee.

### **Remuneration/fees to be paid to the members of the audit committee:**

In the absence of any mention about this aspect, in the first meeting of the audit committee while deciding the procedure for deliberation, etc. remuneration or fee, if any, to be paid to the members of the audit committee should be decided to avoid any dispute or conflict at a future date. As the internal auditor and statutory auditors are also going to attend the audit committee meetings regularly, the matter is of utmost importance and should be decided in advance so as to avoid future misunderstanding or point of dispute.

### **Responsibility of audit committee**

The main responsibility of the audit committee is to ensure transparency and that financial disclosure and financial statements are correct and creditable. It will also ensure that frauds, irregularities, failure of internal control system within the organization are minimized. Some responsibilities are discussed below:

- Review the efficacy of internal control mechanism.
- Monitor the risk management policies adopted by the company.
- Examine accounting, taxation aspects of all significant transactions.
- Preparing the financial statements following the various accounting standards issued by the Institute of Chartered Accountants of India.
- Review the reports furnished by the Internal auditors and draft audit report submitted by the Statutory auditors and suggest suitable steps/actions in respect thereof
- Reasons and necessity of material departures from the practices followed by the company.
- Review of accounting policies followed and applied consistently.
- Judgements and estimates made are reasonable and prudent so as to give a true and fair view of the state of affairs of the Company as at a given date and of the profit or loss of the Company for the period ended on that date.
- Proper and sufficient care for the maintenance of adequate accounting records in accordance with the law.
- Proper safeguard for the assets of the Company and for preventing and detecting fraud.
- Proper safeguard for avoiding other irregularities.
- Compliance of provisions of the Act with regard to disqualifications of directors, creation of Debenture Redemption Reserve.
- Financial statements are prepared on a going concern basis.
- Review of half-yearly and annual financial statements.
- Statutory dues are properly deducted and paid to the credit of government.
- Reasons for defaults in the payment of interest and refund of deposits.
- Acceptance of loans, giving loans and making investments within the permissible limits.
- Deposit of unpaid dividends, interest on deposits, debentures, etc. to the Investors Protection Fund.
- Related party transactions.

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Compliance in respect of various other provisions of company law and other applicable laws.

### **Authority of the Audit Committee**

The audit committee has the authority to investigate into any matter in relation to the items specified in this Section or referred to it by the Board and for this purpose, shall have full access to information contained in the records of the company and if necessary, can also seek professional advice.

### **Recommendations of the Audit Committee:**

It is responsibility of the board of directors that any recommendation made by the Audit Committee in respect of financial management and audit report shall be binding.

In case the Board of Directors does not accept the recommendations of the Audit Committee then the Board shall record the reasons therefore and the same should be communicated to the shareholders.

The correct procedure for recording the reasons for not accepting the recommendations of the Audit Committee shall be to convene the Board Meeting, discuss the recommendations made by the audit committee and record in the minutes, either by way of note or by way of passing a resolution in this respect.

### **Consequences for non-compliance of S. 292A:**

For non-compliance of the provisions of this Section, both the company and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year, or with fine which may extend to fifty thousand Rupees, or with both.

### **Steps for compliance of provisions relating to audit committee:**

To call the Board Meeting and constitute the Audit Committee.

The company should send intimation in writing about the constitution of the audit committee to the Statutory Auditors, Internal Auditors and all the other audit committee members along with the terms of reference that the Audit Committee has been constituted.

the audit committee should meet to decide about the procedure to be followed at audit committee meetings for the deliberations, for fixing the quorum, leave of absence, frequency of the meeting, appointment of chairman and secretary of the audit committee, procedure for recording, approving and signing of the minutes of the audit committee meetings, remuneration, if any, to be paid to the members of the audit committee and audit committee report, etc.

### **Minutes of the Audit Committee meetings:**

There is no specific mention in the Section about maintenance of the minutes of the meetings of the audit committees. As the Audit Committee is the requirement of Law, and also to avoid any misunderstanding at a future date, it is suggested that minutes of the proceedings of the audit committees be prepared. For this purpose the secretary of the company or the secretary of the audit committee should prepare the draft minutes and send the same to audit committee members which of course will include the Internal Auditors and External Auditors, well within a reasonable time and after receiving the comments or suggestions, if any, from the audit committee members, the Internal Auditors and External Auditors, suitably incorporate them while finally drafting the minutes of the Audit Committee meetings.

### **Audit Committee Report:**

The main purpose of incorporating the provisions of Audit Committee in the Companies Act, 1956 is that the real owners of the company viz. the shareholders are kept properly informed that the financial statements are properly drawn following the provisions of company law and other applicable laws.

There is no specific mention in the Section about the preparation of Audit Committee Report and publishing of the same. In view of what is discussed above it is suggested that an audit committee can itself decide for framing the audit committee report. In case it is decided to frame the report, then the same can be framed on the following lines, of course within the parameters of terms of reference and publish the same by way of a reference in the directors' report.

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### **Role of audit committee**

The audit committee's role should be viewed within the context of the organization's governance process as a whole. As a committee of the board, the audit committee must carry out its duties within the framework of governance principles and practices established by the board of directors. Good governance promotes accountability of the key players, and ensures that they work in the best interests of the organization and its shareholders to enhance shareholder value, while taking into account the legitimate interests of other stakeholders. The audit committee's role, and its commensurate accountability to the board, is directly related to the way the board chooses to discharge its oversight function. Since its effectiveness is directly linked to that of the board, many of the issues that affect the audit committee's effectiveness are also likely to impact the board's effectiveness.

Audit committee as per listing agreement clause 49

### **Qualified and Independent Audit Committee**

As per clause 49 of listing agreement a qualified and independent audit committee shall be set up, giving the terms of reference subject to the following:

- i. The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors.
- ii. All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.

### **(B) Meeting of Audit Committee**

The audit committee should meet at least four times in a year and not more than four months shall elapse between two meetings. The quorum shall be either two members or one third of the members of the audit committee whichever is greater, but there should be a minimum of two independent members present.

### **(C) Powers of Audit Committee**

**The audit committee shall have powers, which should include the following:**

1. To investigate any activity within its terms of reference.
2. To seek information from any employee.
3. To obtain outside legal or other professional advice.
4. To secure attendance of outsiders with relevant expertise, if it considers necessary.

### **(D) Role of Audit Committee**

**The role of the audit committee shall include the following:**

1. Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.
2. Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.
3. Approval of payment to statutory auditors for any other services rendered by the statutory auditors.
4. Reviewing, with the management, the annual financial statements before submission to the board for approval, with particular reference to:
  - a. Matters required being included in the Director's Responsibility Statement to be included in the Board's report in terms of clause (2AA) of section 217 of the Companies Act, 1956
  - b. Changes, if any, in accounting policies and practices and reasons for the same
  - c. Major accounting entries involving estimates based on the exercise of judgment by management
  - d. Significant adjustments made in the financial statements arising out of audit findings
  - e. Compliance with listing and other legal requirements relating to financial statements
  - f. Disclosure of any related party transactions
  - g. Qualifications in the draft audit report.
5. Reviewing, with the management, the quarterly financial statements before submission to the board for

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approval

5A. Reviewing, with the management, the statement of uses / application of funds raised through an issue (public issue, rights issue, preferential issue, etc.), the statement of funds utilized for purposes other than those stated in the offer document/prospectus/notice and the report submitted by the monitoring agency monitoring the utilisation of proceeds of a public or rights issue, and making appropriate recommendations to the Board to take up steps in this matter.

6. Reviewing, with the management, performance of statutory and internal auditors, and adequacy of the internal control systems.

7. Reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure coverage and frequency of internal audit.

8. Discussion with internal auditors any significant findings and follow up there on.

9. Reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the board.

10. Discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.

11. to look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non payment of declared dividends) and creditors.

12. To review the functioning of the Whistle Blower mechanism, in case the same is existing.

12A. Approval of appointment of CFO (the whole-time Finance Director or any other person heading the finance function or discharging that function) after assessing the qualifications, experience & background, etc. of the candidate.

13. Carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

### **(E) Review of information by Audit Committee**

#### **The Audit Committee shall mandatorily review the following information:**

1. Management discussion and analysis of financial condition and results of operations;
2. Statement of significant related party transactions (as defined by the audit committee) submitted by management;
3. Management letters / letters of internal control weaknesses issued by the statutory auditors;
4. Internal audit reports relating to internal control weaknesses; and
5. The appointment, removal and terms of remuneration of the Chief internal auditor shall be subject to review by the Audit Committee

Audit committee as per new company act 2013

177. (1) The Board of Directors of every listed company and such other class or classes of companies, as may be prescribed, shall constitute an Audit Committee. In other words in every listed company and such other class of company the board of directors should constitute an audit committee, earlier only public companies are required to form audit committee but as per the new law all the listed companies are required to form audit committee.

#### **Number of directors minimum=3**

(2) The Audit Committee shall consist of a minimum of three directors with independent directors forming a majority: Provided that majority of members of Audit Committee including its Chairperson shall be persons with ability to read and understand the financial statement. the minimum number of directors who are required to attend the meeting is three including the independent directors forming the majority.

#### **When to hold it-**

#### **Within one year from the commencement of this act**

(3) Every Audit Committee of a company existing immediately before the commencement of this Act shall, within one year of such commencement, be reconstituted in accordance with sub-section (2).

Decision which is to be taken in the audit committee

(4) Every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, inter alia, include,—

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- (i) Decision related to the recommendation for appointment, remuneration and terms of appointment of auditors of the company;
- (ii) To review and monitor the auditor's independence and performance, and effectiveness of audit process;
- (iii) To examination of the financial statement and the auditors' report thereon;
- (iv) To give approval or any subsequent modification of transactions of the company with related parties;
- (v) Scrutiny of inter-corporate loans and investments;
- (vi) Valuation of undertakings or assets of the company, wherever it is necessary;
- (vii) To evaluate the internal financial controls and risk management systems;
- (viii) To monitor the end use of funds raised through public offers and related matters.

## AUTHORITY OF AUDIT COMMITTEE

(5) The Audit Committee may call for the comments of the auditors about internal control systems, the scope of audit, including the observations of the auditors and review of financial statement before their submission to the Board and may also discuss any related issues with the internal and statutory auditors and the management of the company.

(6) The Audit Committee shall have authority to investigate into any matter in relation to the items specified in sub-section (4) or referred to it by the Board and for this purpose shall have power to obtain professional advice from external sources and have full access to information contained in the records of the company.

(7) The auditors of a company and the key managerial personnel shall have a right to be heard in the meetings of the Audit Committee when it considers the auditor's report but shall not have the right to vote.

(8) The Board's report under sub-section (3) of section 134 shall disclose the composition of an Audit Committee and where the Board had not accepted any recommendation of the Audit Committee, the same shall be disclosed in such report along with the reasons

9) Every listed company or such class or classes of companies, as may be prescribed, shall establish a vigil mechanism for directors and employees to report genuine concerns in such manner as may be prescribed.

(10) The vigil mechanism under sub-section (9) shall provide for adequate safeguards against victimisation of persons who use such mechanism and make provision for direct access to the chairperson of the Audit Committee in appropriate or exceptional cases: Provided that the details of establishment of such mechanism shall be disclosed by the company on its website, if any, and in the B

## CONCLUSION

To conclude our discussion on audit committee we can say that to safe guard the interest of stakeholders audit committee plays a crucial role .it helps in preventing fraudulent reporting and ensure transparency and correctness of financial statements. For this various steps have been taken from time to time from section 292A ,then listing agreement and lastly to new company act 2013 .To conclude, the backbone of corporate governance is to ensure adherence to ethics and audit committee can act as a monitor to ensure the ethical conduct.

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