

SECRETARIAL AUDIT - PROFESSIONAL LIABILITY

Section - 447

Any person who is found to be guilty of fraud,
shall be punishable with **imprisonment** for a term which
shall **not be less than six months** but
which may **extend to ten years** and
shall also be liable to fine which
shall not be less than the amount involved in the fraud, but
which may extend to three times the amount involved in the
fraud:

Where the fraud in question involves public interest,
the term of imprisonment shall not be less than three years.

Explanation.—For the purposes of this section—

- (i) “fraud” in relation to affairs of a company or anybody corporate, includes any act, omission, concealment of any fact or abuse of position committed **by any person or any other person with the connivance in any manner, with intent** to deceive, to gain undue advantage from, or **to injure the interests of, the company or its shareholders or its creditors or any other person**, whether or not there is any wrongful gain or wrongful loss;
- (ii) “wrongful gain” means the gain by unlawful means of property to which the person gaining is not legally entitled;
- (iii) “wrongful loss” means the loss by unlawful means of property to which the person losing is legally entitled.

INTENTION IN CONTEXT OF FRAUD:

The definition of Fraud in Section 17 of the Indian contract act includes:

Fraud” means and includes any of the following acts:

- (1) the suggestion as a fact, of that which is not true, by one who does not believe it to be true;
- (2) the active concealment of a fact by one having knowledge or belief of the fact;
- (3) a promise made without any intention of performing it;
- (4) any other act fitted to deceive;
- (5) any such act or omission as the law specially declares to be fraudulent.

FRAUDULENT ACTIONS WILL BE CONSIDERED AS FRAUD BASED ON THE INTENTIONS TO PERFORM THE SAME

FRAUD IN CONTEXT OF BOARD OF DIRECTORS:

- **Companies are prosecuted and investigated when some of its employees engineer a scheme to commit a fraud.**
- **Law itself sometimes fails to recognize the distinction between the perpetrators and the company, aggrieved shareholders have no choice but to prosecute the company.**
- **The new companies' law seeks to strengthen shareholders' action against a company and, in future, this would only increase liability of the company and its directors for the unauthorized, illegal and criminal acts of some employees.**
- **In such cases, it is imperative for directors and employees of the company to demonstrate that the company's decisions were in good faith and the actions of the fraudsters were unauthorized.**

Section - 448

If in **any return, report, certificate**, financial statement, prospectus, statement or other document required by, or for, the purposes of any of the provisions of this Act or the rules made thereunder, **any person** makes a statement,—

- (a) which is false in any material particulars, knowing it to be false; or
- (b) which omits any material fact, knowing it to be material, he shall be liable under section 447.

Professional misconduct in relation to Company Secretaries in Practice

A Company Secretary in practice shall be deemed to be guilty of professional misconduct, if he—

- (1) discloses information acquired in the course of his professional engagement to any person other than his client
- (2) without the consent of his client, or otherwise than as required by any law for the time being in force;

certifies or submits in his name, or in the name of his firm,

a report of an examination of the matters relating to company secretarial practice and related statements unless

the examination of such statements has been made by him or

by a partner or

an employee in his firm or

by another Company Secretary in practice;

permits his name or name of his firm

to be used

in connection with any report or statement contingent

upon future transactions in a manner which may

lead to the belief that

he vouches for the accuracy of the forecast;

expresses his opinion on any report or statement given
to any business or enterprise in which
he, his firm, or a partner in his firm
has a substantial interest;

fails to disclose a material fact known to him in his
report or statement but

the disclosure of which is necessary in making such
report or statement, where

he is concerned with such report or statement in a
professional capacity;

(6) fails to report a material mis-statement known to him and with which he is concerned in a professional capacity;

(7) does not exercise due diligence, or is grossly negligent in the conduct of his professional duties;

(8) fails to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion;

(9) fails to invite attention to any material departure from the generally accepted procedure relating to the secretarial practice;

(10) fails to keep moneys of his client other than fees or remuneration or money meant to be expended in a separate banking account or to use such moneys for purposes for which they are intended within a reasonable time.

Reporting with Qualification

The qualification, reservation or adverse remarks, if any, shall be stated by the PCS at the relevant places in his/her report.

It is recommended that the qualifications, reservations or adverse remarks of PCS, if any, should be stated in **thick** type or in *italics* in the Secretarial Audit Report.

If the PCS is unable to form any opinion on any matter, he / she shall state that he/she is unable to form an opinion on that matter and the reasons thereof.

If the scope of work required to be performed, is restricted on account of limitations imposed by the company or on account of circumstantial limitations (like certain books or papers being in custody of another person or Government Authority) the Report shall indicate such limitations. If such limitations are so material as to render the PCS incapable of expressing any opinion, the PCS should state that:

“In the absence of necessary information and records, he / she is unable to report compliance(s) by the Company”.

Pre-requisites

- ***Appointment***

a. **Appointment** of Secretarial Auditor and remuneration payable to him should be preferably made by the members and at the least by the Board of Directors of the Company.

b. **As** a prudent corporate practice, it is advisable that changes in the office of Secretarial Auditor, are reported to the members in the Director's Report.

- ***Communication to earlier incumbent***
 - a. Whenever a new Secretarial Auditor is appointed in place of the existing Secretarial Auditor,
 - b. he/she should communicate the appointment to the earlier incumbent **in writing by registered post**, in view of the gist of relevant pronounced judgements apart from the provisions of clause (8) of Part I of the First Schedule to the Company Secretaries Act, 1980,

- ***Assignment***

- a. After the appointment is carried out in the manner suggested, **a letter of engagement shall be issued by the Company.** Practicing Company Secretary should formally accept the letter of engagement.
- b. It would be in the interest of the new Secretarial Auditor to attempt to procure at appropriate stage, **authentic information about the remuneration paid to the earlier incumbent in view of the provisions under clause(11) of Part I of the First Schedule to the Company Secretaries Act, 1980.**

- ***Right to Information and Access to Records***
 - a. To enable a PCS to conduct Secretarial Audit ,
 - b. the Company should provide the PCS access at all times to the books, papers, minute, books, forms and returns filed under various statutes, documents and records of the company, whether kept in pursuance of the applicable laws or otherwise and whether kept at the registered office of the company or elsewhere which the PCS considers essential for the purposes of Secretarial Audit .

- c. A PCS shall be entitled to require from the officers or agents of the company, such information and explanations as the PCS may think necessary for the purpose of such Reporting. However,
- d. depending on the facts and circumstances he/she may obtain a letter of representation from the company in respect of matters where personal verification may not be practicable.

AUDIT PROCESS

- *Firstly*, make list of **applicable laws**
- *Secondly*, Make a list of **desirable practices** may be arising out of business rules, codes, policies and non-binding requirements .
- *Thirdly*, make **check lists**
- *Fourthly*, **create internal procedures and policies consistent with the law**
- *Fifthly*, **assess risks in relation to these laws and requirements.**
- *Sixthly*, **ensure that adequate controls are in place to minimize or eliminate these risks.**

AUDIT PROCESS:

- **Inspection of articles and other documents filed during incorporation.**
- **Inspection of company's file of documents filed with Registrar of Companies .**
- **Inspection of Company's file at Registrar's office.**
- **Inspection of statutory registers and other documents.**
- **Checking and verifying the agreements and dispute free business compliance.**
- **Verifying and scrutinizing the legal requirements.**
- **Inspection of Contracts & Agreements.**

AUDIT PROCESS

- **Review Board of Directors committee structure and committee charters.**
- **Review Board of Directors and committee minutes**
- **Review corporate structure, including affiliates and joint ventures.**
- **Verify that state corporate filings, including annual reports, have been made.**
- **Review whether corporate registration and/or filings should be undertaken in other jurisdictions.**
- **Review governance-related policies, including conflicts and ethics.**
- **Review insurance coverage**