



Secretarial audit-A tool for good corporate governance

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Abstract

Secretarial Audit is not just on audit of the diligent compliance or that of the adherence to the law in true letter and spirit but has proved to be a strong founding pillar of the governance framework of the Indian Corporate Sector and a futuristic torchlight for the entire Indian Economy Secretarial Audit, as a result of faith of the law makers and the Regulatory Authorities in the Governance Professionals or as the law puts it, in the practicing company secretaries, bestows a huge responsibility on the Secretarial Auditors.

In the era of minimum government, maximum governance, the Secretarial Audit postulates for an independent verification of the records, books, papers and documents by a Company Secretary to check the compliance status of the company according to the provisions of various statutes, laws and rules & regulations and also to ensure the compliance of legal and procedural requirements and processes followed by the company. Secretarial Audit is, therefore, an independent and objective assurance intended to add value and improve operations of a company. It helps to accomplish the organisation's objectives by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control, and governance processes.

Secretarial audit can be an effective multi-pronged weapon to assure the regulators, generate confidence amongst the shareholders, the creditors and other stakeholders in companies, assure Flls/FI's/SFCs/SIDCS/Banks and instil self-regulation and professional discipline in companies. It is a tool of risk mitigation and will allow companies to effectively address compliance risk issues.

Keywords: Company secretary, corporate governance, regulatory compliance, secretarial audit, the company's act 2013

Introduction

The term "Secretarial Audit" refers to the mechanism which is connected with the audit of the non-financial aspects of the company. It gives necessary comfort to the investors, management, regulators and other stakeholders, as to the compliance of all applicable laws by the company and certifies the existence of adequate systems and processes for ensuring compliance of laws in the company.

The genesis of the Secretarial Audit can be traced to the Companies (Amendment) Act, 1988 which amended Section 161 of the Companies Act, 1956. This amendment introduced the requirement of certification of annual return of listed Companies by a Practising Company Secretaries. Thereafter, Companies (Amendment) Act, 2000 amended Section 383A of the Companies Act, 1956. By this amendment, it was mandated that companies which had a paid-up share capital of Rs.10 lakh or more and which did not require to employ a Whole-time Company Secretary had to obtain a Certificate from a Practising Company Secretaries on annual basis regarding the compliance of the various provisions of the Act.

This certificate was to be attached with the Board's Report, in 2002, Naresh Chandra Committee Report on Corporate Audit and Governance recommended introduction of Compliance Audit. Later in the year 2003, the Ministry of Corporate Affairs (MCA) introduced the Companies (Amendment) Bill, 2003, which introduced the concept of Secretarial Audit by giving powers to Central Government to order, at any time, the secretarial compliance audit of the company for any period. Similarly, the Concept Paper published by MCA in 2004, contemplated to enact a new Company Law in which the concept of the Secretarial Compliance Audit was Included. Later on, Corporate

Governance Voluntary Guidelines, 2009 was released in December 21, 2009, which insisted on adoption of Secretarial Audit for public companies and private companies, particularly the bigger ones. Para V of the Guidelines stated that: "Since the Board has the overarching responsibility of ensuring transparent, ethical and responsible governance of the company, it is important that the Board processes and compliance mechanisms of the company are robust.

To ensure this, the companies may get the Secretarial Audit conducted by a competent professional. The Board should give its comments on the Secretarial Audit in its report to the shareholders. Thereafter, the 21st report of the Parliamentary Standing Committee on Finance on the Companies Bill, 2009 also specified about Secretarial Audit. At last, Secretarial Audit for bigger Companies has been notified from 1st April 2014 under the Companies Act, 2013 (the Act). As the Public shareholders subscribe to the shares of listed entities and public companies, it is necessary that the interest of the public is protected from the impact of non-compliances of the various provisions of the Act and other Corporate Laws. Besides, this would insulate the directors and other stakeholders like employees, suppliers, banks and financial institutions from the ill effects of non-compliance.

Need of Secretarial Audit

The need for secretarial audit arises from several factors, all of which contribute to ensuring corporate transparency, compliance with laws and regulations, and the overall health of the organization. Here are some key reasons why secretarial audit is essential:

- **Compliance Verification:** Secretarial audit helps verify compliance with various laws, regulations, and guidelines applicable to the company, such as the Companies Act, SEBI regulations, FEMA regulations, etc. It ensures that the company operates within the legal framework and fulfils its statutory obligations.
- **Corporate Governance:** Secretarial audit plays a crucial role in promoting good corporate governance practices. By reviewing the company's governance structure, board procedures, disclosure practices, and adherence to ethical standards, it helps identify areas for improvement and ensures transparency and accountability.
- **Risk Mitigation:** Conducting regular secretarial audits helps identify potential risks and deficiencies in internal controls, policies, and procedures. By identifying these risks early on, companies can take proactive measures to mitigate them and prevent potential legal, financial, or reputational damage.



- **Stakeholder Confidence:** Secretarial audit enhances stakeholder confidence by demonstrating the company's commitment to transparency, compliance, and ethical business practices. It provides assurance to investors, lenders, regulators, and other stakeholder's that the company's affairs are conducted in a responsible and lawful manner.
- **Preventing Fraud and Mismanagement:** Secretarial audit helps detect instances of fraud, mismanagement, or irregularities within the organization. By examining the company's records, transactions, and governance practices, auditors can identify red flags and investigate further to prevent or mitigate potential fraud or misconduct.
- **Legal Requirements:** In many jurisdictions, secretariat audit is a legal requirement for certain types of companies or for companies above a certain size threshold. Failure to conduct a secretarial audit or comply with its findings may lead to legal and regulatory consequences, including penalties, fines, or even legal action against the company and its officers
- **Improving Efficiency and Effectiveness:** Through the process of secretarial audit, companies can identify inefficiencies in their administrative and compliance

processes and implement measures to improve efficiency and effectiveness. This can lead to cost savings, enhanced productivity, and better utilization of resources.

In conclusion, secretarial audit is indispensable for ensuring legal compliance, promoting good corporate governance, mitigating risks, enhancing stakeholder confidence, preventing fraud and mismanagement, complying with legal requirements, and improving overall organizational efficiency and effectiveness. It is a valuable tool for companies to maintain integrity, transparency, and accountability in their operations.

Secretarial Audit - A Crucial Corporate Governance Tool

Secretarial audit serves as a crucial corporate governance tool by ensuring transparency, compliance, and accountability within organizations. Here's how secretarial audit contributes to effective corporate governance



- **Ensuring Regulatory Compliance:** Secretarial audit verifies compliance with various laws, regulations, and guidelines applicable to the company. By reviewing corporate records, governance practices, and statutory filings, secretarial auditors ensure that the organization operates within the legal framework and fulfils its regulatory obligations.
- **Monitoring Corporate Practices:** Secretarial audit monitors corporate practices to ensure they align with ethical standards and best practices. By assessing board procedures, decision-making processes, and governance structures, secretarial auditors help identify areas for improvement and ensure that the organization adheres to principles of good governance.
- **Assessing Board Effectiveness:** Secretarial audit evaluates the composition, independence, and performance of the board of directors. By reviewing board meeting minutes, director appointments, and adherence to governance guidelines, secretarial auditors assess the effectiveness of the board in fulfilling its oversight responsibilities and promoting the interests of stakeholders.

- **Enhancing Transparency and Disclosure:** Secretarial audit promotes transparency by ensuring accurate and timely disclosure of information to stakeholders. By reviewing disclosure practices, communication channels, and shareholder relations, secretarial auditors help maintain open and transparent communication with investors, regulators, and other stakeholders, building trust and confidence in the organization.
- **Identifying Risks and Controls:** Secretarial audit helps identify risks and evaluate the effectiveness of internal controls within the organization. By assessing compliance mechanisms, risk management frameworks, and corporate policies, secretarial auditors assist in identifying potential risks, such as legal liabilities or reputational risks, and recommend measures to strengthen internal controls.
- **Supporting Strategic Decision-Making:** Secretarial audit provides insights that support strategic decision-making processes. By identifying governance gaps, compliance issues, and opportunities for improvement, secretarial auditors help management and the board make informed decisions that promote the long-term success and sustainability of the organization.

Overall, secretarial audit plays a crucial role in promoting good corporate governance practices, fostering trust among stakeholders, and ensuring the integrity and credibility of the organization. By providing independent assurance on governance processes and compliance practices, secretarial audit helps organizations uphold their commitments to transparency, accountability, and ethical conduct.

Objectives of a Secretarial Audit

The objectives of a secretarial audit encompass various aspects of ensuring legal compliance, promoting good corporate governance, and enhancing transparency within an organization. Here are the key objectives of secretarial audit

1. **Verification of Compliance:** To verify compliance with the provisions of applicable laws, regulations, and guidelines governing the company's operations, including the Companies Act, SEBI regulations, FEMA regulations, and other relevant statutes.
2. **Assessment of Governance Practices:** To assess the adequacy and effectiveness of corporate governance practices within the organization, including the composition and functioning of the board of directors, adherence to governance guidelines, and ethical standards.
3. **Identification of Legal and Regulatory Risks:** To identify potential legal and regulatory risks faced by the company and assess the adequacy of internal controls and compliance mechanisms in mitigating these risks.
4. **Evaluation of Board Procedures:** To evaluate the procedures and processes followed by the board of directors in discharging their duties and responsibilities, including decision-making processes, meeting protocols, and adherence to statutory requirements.

5. **Review of Statutory Registers and Records:** To review the maintenance and accuracy of statutory registers, records, and filings required under company law, ensuring that they are up-to-date and compliant with legal requirements.
6. **Examination of Disclosures and Reporting:** To examine the accuracy and completeness of disclosures made by the company to regulators, shareholders, and other stakeholders, ensuring transparency and accountability in reporting practices.
7. **Assessment of Related Party Transactions:** To assess the adequacy of controls and disclosures related to transactions with related parties, ensuring compliance with regulatory requirements and safeguarding against potential conflicts of interest.
8. **Detection of Fraud and Mismanagement:** To detect instances of fraud, mismanagement, or irregularities within the organization by conducting a comprehensive review of corporate records, transactions, and governance practices.
9. **Recommendation of Remedial Measures:** To recommend remedial measures to address any deficiencies or weaknesses identified during the audit, ensuring that the company takes corrective action to enhance compliance and governance practices.
10. **Enhancement of Stakeholder Confidence:** To enhance stakeholder confidence by providing Independent assurance on the company's compliance and governance practices, fostering trust and credibility among investors, regulators, and other stakeholders.

Provision under the Companies Act, 2013

Section 204(1) of the Companies Act, 2013 read with rule 9 of the Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014 provides that-

- a. Every Listed Company;
- b. Every public company having a paid-up share capital of fifty crore rupees or more, or
- c. Every public company having a turnover of two hundred fifty crore rupees or more;
- d. Every company having outstanding loans or borrowings from banks or public financial Institutions of one hundred crore rupees or more

shall annex with its Board's report made in terms of sub-section (3) of section 134 of the Act, a Secretarial Audit report given by a Practising Company Secretaries., in form No MR-3, as attached as Annexure-A

Explanation to this sub-rule clarifies that the paid-up share capital, turnover, or outstanding loans or borrowings as the case may be, existing on the last date of latest audited financial statement shall be taken into account.

Section 204 (2): It shall be the duty of the company to give all assistance and facilities to the company secretary in practice, for auditing the secretarial and related records of the company.

Section 204 (3):The Board of Directors, in their report made in terms of sub-section (3) of section 134, shall explain in full any qualification or observation or other remarks made by the company secretary, in practice in his report under sub-section (1)

Section 204 (4): If a company or any officer of the company or the company secretary in practice, contravenes the provisions of this section, the company, every officer of the company or the company secretary in practice, who is in default, shall be liable to a penalty of 2,00,000 rupees.

Further, Section 204 is applicable to a private company which is a subsidiary of a public company, and which falls under the prescribed class of companies.

Although, the companies which are not covered under section 204 may opt for conducting Secretarial Audit voluntarily as it provides an independent assurance of the compliances of applicable laws by the company.

A Company Secretary in practice is a professional who is well-versed in matters of statutory, procedural and practical aspects of laws applicable to companies, both listed and unlisted public and private companies. A strong knowledge base makes him a competent professional to conduct Secretarial Audit. In terms of section 204(1), only a member of the Institute of Company Secretaries of India holding certificate of practice (Company Secretary in Practice) can conduct Secretarial Audit and Issue the Secretarial Audit Report to the company.

The Process of Secretarial Audit

Secretarial, Audit is a process to check compliance with the provisions of all applicable laws and rules/regulations/procedures; adherence to good governance practices with regard to the systems and processes of seeking and obtaining approvals of the Board and/or shareholders, as may be necessary, for the business and activities of the company, carrying out activities in a lawful manner and the maintenance of minutes and records relating to such approval or decisions and implementation. The secretarial auditor is also expected to express an opinion, after satisfying himself, that there exist adequate systems and processes in the company commensurate with the size and operations of the company to monitor and ensure compliance with applicable laws, rules, regulations and guidelines. The secretarial auditor has to verify whether diverse requirements under applicable laws have been complied with.

Appointment of Secretarial Auditor

As per Rule 8 of the Companies (Meetings of Board and its powers) Rules, 2014, read with Section 179 of the Companies Act, 2013, secretarial auditor is required to be appointed by means of resolution passed at a duly convened board meeting. Further the appointment shall also be in compliance with the Auditing Standards prescribed by the Institute of Company Secretaries of India.

Communication to earlier Incumbent

Whenever a company secretary in practice is engaged as a secretarial auditor in place of an earlier incumbent, he shall communicate to the earlier incumbent about the proposed engagement in writing to be sent by registered/ speed post or any other mode of delivery, as may be recognized by the Institute of Company Secretaries of India.

The Council of ICSI at its meeting held on 16th March 2019 has made amendments in Guidelines wherein for Practice Company Secretaries, communication to previous incumbent would be mandatory before accepting the assignment, in terms of Clause (8) of Part I of the First Schedule to the Company Secretaries Act, 1980. The Council has approved some services in respect of which it shall be mandatory to communicate to the previous incumbent (Company Secretary) before accepting the assignment in terms of clause (8) of part I of the First Schedule to the Company Secretaries Act, 1980, which includes the Issuance of Secretarial Audit Report in terms of Section 204 of the Companies Act, 2013 and Issue of Secretarial Audit Report to material unlisted subsidiaries of Listed entities (whose equity shares are listed) under Regulation 24A of SEBI (LODR) Regulations, 2015.

Acceptance of Appointment

A formal letter for appointment should be issued by the company to the secretarial auditor along with the copy of the board resolution for appointment. The secretarial auditor should confirm acceptance of appointment in writing

Preliminary Discussions/Surveys

It is important to have relevant information about the company. The secretarial auditor is expected to take general overview of the company and interact with the personnel involved to know about the nature of the business. He may opt for surveys for generating information about the company.

Preliminary Meeting

The preliminary meeting with the senior management and the administrative staff involved in the audit will give a fair idea of what is expected and the manner in which audit activities are to be undertaken. At this stage, a time frame of the secretarial audit should be determined and finalized. The secretarial auditor shall discuss the scope and objectives of the audit, gather information on important Board processes, evaluate existing control systems and prepare the audit plan.

Finalization of Audit Plan and Briefing the Staff

It is important to work out an audit plan. The plan involves briefing the audit staff as to allotment of work, fieldwork responsibilities and other roles. The audit plan should comprehensively outline the fieldwork and usage of auditing tools. The review of controls helps the auditor determine the areas of highest risk and design tests to be performed in the fieldwork section. It is essential that the audit plan adheres to the timelines. Detailed checklist for each aspect of secretarial audit should be prepared, and audit staff should be properly sensitized before commencement of audit.

Testing, Interviews and Analysis

The secretarial auditor may use a variety of tools and technology to gather information about the company's operations. The secretarial auditor should determine whether the controls identified during the preliminary review are operating properly, and in the manner described by the Company.

Fieldwork typically consists of interviewing with staff of the company whether formally or informally, reviewing procedure manuals and processes, testing and analysing compliance with applicable policies and procedures and

laws, Niles, regulations and assessing the adequacy of controls. This exercise may result in significant findings which the secretarial auditor may bear in mind while preparing the secretarial audit report.

Working Papers

Working papers are a vital tool of the audit process. They form the basis for expression of the audit opinion. They connect the management's records and information to the auditor's opinion. They are comprehensive and serve many purposes for the company as well as for the Auditor.

Audit Summary for Discussions

It is recommended that the findings during the course of audit are summarized and presented for initial discussions with the management for their views/clarifications/replies

Submission of Secretarial Audit Report

After considering the clarifications/replies of the management, the secretarial auditor shall prepare the secretarial audit report in Form MR-3. The report is addressed to the members but is to be submitted to the Board. The report shall contain the opinion on the statutory compliances examined by the auditor and shall state whether in his opinion the Company is carrying out/not carrying out due compliances of the applicable provisions of the various laws. The report shall be provided with or without qualifications.

Auditing Standards

Secretarial Audit should be conducted in accordance with the Auditing Standard issued by the Institute of Company Secretaries of India

Advantages of Secretarial Audit

Secretarial Audit provides an effective mechanism to ensure that compliance of various legislations and regulations including the Companies Act, SEBI Law, Secretarial Standards and other corporate and economic laws applicable to the company has been diligently done. This would give necessary comfort to the investors. Management, Regulators and Other Stakeholders.

The periodical Secretarial Audit helps to detect the instances of non-compliances and facilitates taking corrective-measures well in time to avoid any further risk

Secretarial Audit facilitates monitoring compliances with the requirements of law through a formal compliance management programme which can produce following positive results to the stakeholders of a company:

- Better compliance of laws leading to reduction in number of frauds and consequent prosecutions.
- Protecting the interest of stakeholders and strengthening their faith in the corporates.
- Protecting the company/directors from the consequences of unintended non-compliance of laws.
- Independent assurance and comfort to independent/non-executive/nominee directors that the affairs of the company have been conducted as per law.
- Instilling professional discipline and self-regulation.
- Reducing workload of regulators due to better and timely compliances.
- Enhancing quality of services to investors.
- Any qualification in the Report will immediately alert the investor.

The SEBI (LODR) Regulations, 2015

In view of the criticality of secretarial functions for ensuring efficient functioning of the Board, the Kotak Committee on Corporate Governance, in its report dated October 05, 2017, recommended that-

- a. Secretarial Audit to be made compulsories for all listed entities under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, in line with the provisions of the Companies Act, 2013.
- b. Secretarial Audit to be extended to all material unlisted Indian subsidiaries in line with the recommendations of the Committee on strengthening group oversight and improving compliance at a group level for listed entities,

Accordingly, SEBI vide circular no. CIR/CFD/CMD1/27/2019 dated February 08, 2019 notified the following provisions to be included in the SEBI (LODR) Regulations, 2015:

- **Regulation 24A:** Secretarial Audit: Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake secretarial audit and shall annex with its annual report, a secretarial audit report, given by a company secretary in practice, in such form as may be prescribed with effect from the year ended March 31, 2019,

This will ensure the strengthening of the oversight of group companies of the listed entities. The term 'Material Subsidiary' means a subsidiary, whose Turnover or net worth exceeds ten per cent (10%) of the consolidated Turnover or net worth, respectively, of the listed entity and its subsidiaries in the immediately preceding accounting year.

The above provision has been substituted by the SEBI vide amendment dated 13.12.2024 which reads as under.

- **Regulation 24A (1):** (a) Every listed entity and its material unlisted subsidiaries incorporated in India shall undertake Secretarial Audit by a Secretarial Auditor who shall be a Peer Reviewed Company Secretary and shall annex a Secretarial Audit Report in such form as specified, with the annual report of the listed entity.

Summing-up

We may opine that once the Secretarial Audit Report is submitted by the secretariat, auditor, the Government as well as other stakeholders can gauge in first instance the level of compliances or non-compliances by the company concerned, It can then immediately take suitable corrective measures under the specific applicable legislations. The measures would act as a check on frauds as well as reduce the number of prosecutions by the Government and consequent litigation on account of non-compliance with the provisions of corporate and securities laws, thereby resulting in healthy and orderly development of the corporate sector. This would, in turn, lead to reduction of investor grievances and enhance various stakeholders' confidence.

In addition to the Government and shareholders, introduction of secretarial audit would be in the interest of companies themselves. Secretarial audit besides ensuring due compliance of the statute, will act as an aid to the management by proving to be a strong internal control device. It can relieve the company and their directors from

consequences of unintended non-compliance of law. Independent directors and nominee directors can be assured that the affairs of the company are being conducted as per law. Besides the Secretarial Auditor can act as a fearless adviser to the company so that the mistakes and lapses, if any, could be rectified well in time and management is reassured that internal systems are guarded.

The inclusion of Secretarial Audit Report in the Directors' Report would go a long way in reassuring public, financial institutions and all others dealing with the company about the quality of corporate governance in the corporate entity concerned.

Companies entering into joint ventures and foreign collaborations will need such an audit to assure foreign partners that the laws of the land are duly complied with. A secretarial audit will serve as a first line due diligence. The secretarial audit will provide an in-built mechanism for enhancing corporate compliances generally and help restore the confidence of investors in the capital market through greater transparency in the corporate functioning.

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