

Duties and Liabilities of Auditors (India – Companies Act, 2013)

A. Duties of Auditors

1. Statutory Audit Duties

- Examine **books of account**, financial statements, vouchers, and internal controls.
- Ensure financial statements give a **true and fair view** of the company's financial position.
- Report on:
 - Adequacy of **internal financial controls**
 - Compliance with **accounting standards**
 - Proper maintenance of **books of account**
 - Frauds noticed or reported (§143(12))
- Verify **loans, guarantees, investments**, and compliance with §186.
- Review related-party transactions for compliance under §188.
- Make inquiries on:
 - Secured loans properly accounted
 - Adequacy of internal control systems
 - Whether personal expenses charged to revenue
 - Whether deposits or assets are misappropriated
- Attend AGM and answer queries from shareholders.
- Provide reasons for resignation formally.

B. Liabilities of Auditors

1. Civil Liability

- Compensation for losses caused to the company, shareholders, creditors, or third parties due to:
 - Negligence
 - Misstatements
 - Breach of duty
- Joint and several liability when in partnership.

2. Criminal Liability (Severe under Companies Act, 2013)

- **Fraud** (Section 447):
 - Imprisonment up to 10 years + fine up to 3x amount involved.
- **Knowingly making false statements** in audit reports (§147).

- **Improper/false certification** of financial statements.
- **Wilful suppression** of material facts.
- **Failure to report fraud** (mandatory reporting under §143(12)).

3. Professional Misconduct (ICAI)

Auditors may be liable for:

- Gross negligence
- Conflict of interest
- Failure to maintain independence
- Not exercising due diligence
- Not reporting fraud

Penalties include suspension, removal from Register of Members, and monetary penalties.

2. Understanding the Role of the Audit Committee

Audit Committee is mandatory for:

- **Listed companies**
- Certain prescribed public companies (as per Rule 6 of Companies (Meetings of Board and its Powers) Rules)

A. Composition

- Minimum 3 directors; majority must be **independent**.
- Chairperson must be an **Independent Director**.
- Members should have financial knowledge; at least one must have **accounting/financial expertise**.

B. Key Roles and Responsibilities

1. Financial Reporting Oversight

- Review quarterly and annual financial statements.
- Examine changes in accounting policies.
- Ensure compliance with accounting standards.

2. Internal Control Framework

- Evaluate adequacy and effectiveness of internal control systems.
- Monitor internal audit function (appointment, performance, scope).

3. Whistleblower Mechanism

- Oversee vigil mechanism.
- Protect whistleblowers from victimization.

4. Risk Management

- Review risk management policies, fraud risks, cyber risks.
- Oversee significant financial and operational exposures.

5. External Auditor Interaction

- Recommend appointment/removal of auditors.
- Review independence & performance.
- Approve audit fees.
- Discuss audit findings and management responses.

6. Related-Party Transactions

- Approve or modify RPTs.
- Examine pricing, terms, arm's length conditions.

3. Appointment, Responsibilities, Liabilities & Duties of Auditors

A. Appointment

1. First Auditor

- Appointed by Board within **30 days of incorporation**.
- If Board fails → shareholders appoint within next 90 days.

2. Subsequent Auditor

- Appointed by shareholders in AGM.
- Tenure: **5 years**, with eligibility for reappointment (subject to rotation rules).

3. Rotation of Auditors

Mandatory for:

- Listed companies
- Certain unlisted and private companies exceeding prescribed thresholds

Rotation rules:

- Individual auditor: Max **1 term of 5 years**
- Audit firm: Max **2 terms of 5 years**

4. Disqualifications

- Relative holding > ₹1 lakh securities

- Business relationship with company
- Rendering prohibited non-audit services
- Indebtedness to company > ₹5 lakh
- Officer or employee of the company

B. Responsibilities

- Conduct audit as per **Standards on Auditing (SA)**.
- Maintain **independence** and avoid conflicts of interest.
- Report fraud to Audit Committee/Board and to Central Government (as required).
- Ensure compliance with **Corporate Laws, Tax Laws**, and **SEBI** regulations (for listed companies).
- Maintain professional skepticism.

C. Liabilities (Summary)

Type	Examples
Civil Liability	Negligence causing financial loss
Criminal Liability	Fraud, intentional misstatements
Professional Liability	ICAI disciplinary action
Regulatory Liability	SEBI penalties for listed co. audits

4. Case Study: SATYAM SCAM

Background

- The Satyam scandal came to light in **January 2009**.
- Involved **₹7,000 crore accounting fraud**.
- Founder **Ramalinga Raju** confessed to manipulating financial statements for years.

Key Fraud Techniques Used

1. **Inflated revenues** through fake invoices.
2. **Fake bank balances** and fixed deposits.
3. **Inflated cash and bank balances** by over ₹5,000 crore.
4. **Ghost employees** to siphon payroll funds.

5. **Manipulation of debtor figures** and under-reporting liabilities.

Auditor Failures (PriceWaterhouse / PwC India)

1. Negligent Verification

- Bank balances not independently verified.
- Relied on forged statements without third-party confirmation.

2. No Professional Skepticism

- Ignored red flags: mismatched bank balance confirmations, abnormal margins.

3. Weak Audit Procedures

- Failure to verify fixed deposits, accruals, and invoices.
- Over-reliance on management-provided data.

4. Independence Issues

- Unusually high audit fees.
- Long tenure compromised independence.

5. Inadequate Reporting to Audit Committee

- Dishonest or incomplete communications.

Consequences

For Management

- Chairman Raju and senior executives arrested and convicted.
- Board dissolved by Government.

For Auditors

- PwC partners arrested.
- PwC banned by SEBI (initially for 2 years).
- Heavy penalties under various laws.

For Corporate Governance in India

Led to major reforms:

- Mandatory auditor rotation
- Enhanced penalties for fraud
- Strengthened power of SFIO
- Robust whistleblower rules

- Stricter internal financial controls requirements (Section 134 & 143)
- SEBI reforms for listed companies

5. Key Learnings from Satyam for Auditors & Audit Committees

For Auditors

- Never rely solely on management confirmations.
- Must obtain **independent third-party evidence**.
- Exercise **professional skepticism** at all times.
- Ensure independence and avoid long, unbroken audit tenures.

For Audit Committees

- Must actively challenge management.
- Ensure auditors obtain adequate evidence.
- Oversee whistleblower complaints effectively.
- Review internal control weaknesses rigorously.
- Ensure rotation of auditors and partners.

1. Serious Fraud Investigation Office (SFIO)

SFIO is India's premier **multi-disciplinary fraud investigation agency**, constituted to investigate **serious corporate frauds** involving complex financial manipulations.

Origins & Purpose

- SFIO was **established in 2003** following several major corporate frauds.
- It investigates **white-collar crimes**, financial irregularities, money laundering, and corporate mismanagement.

Statutory Basis (Companies Act, 2013)

- Governed primarily by **Section 212**, which outlines **powers, procedures, and exclusivity** of SFIO investigations.
 - Central Government may assign cases to SFIO based on a Registrar/Inspector report, special resolution, public interest, or government request.
 - Once SFIO takes over, **no other agency** may continue the investigation; all documents must be transferred to SFIO.

Key Features

- Multi-disciplinary team (law, finance, IT, forensic experts).
- Power to demand information/documents and examine officers.
- Investigating Officer enjoys powers of an inspector under Section 217.
- Fraud offences under Section 447 become *cognizable and non-bailable* during SFIO investigation.

2. Sections 210–228: Inspection, Inquiry & Investigation (Companies Act, 2013)

Below is a concise, citation-supported overview of key sections relevant to SFIO and corporate investigation.

Section 210 – Investigation into Affairs of a Company

- Central Government may order investigation:
 - Upon Registrar/Inspector report,
 - Upon special resolution of the company,
 - In **public interest**.
- Inspectors may be appointed to investigate company affairs.

Section 211 – Establishment of SFIO

- Provides official establishment of the SFIO as the specialized agency for fraud investigation.
[\[lawgratis.com\]](http://lawgratis.com)

Section 212 – SFIO Investigation

Key provisions include:

1. CG may assign an investigation to SFIO based on defined triggers.
2. **Exclusive jurisdiction**—no other agency may proceed once SFIO takes over.
3. SFIO must submit a report to the Central Government within prescribed timelines.
4. Company employees must fully cooperate and provide all documents/information.
5. Fraud offences fall under stringent bail conditions (Sec 447).

Sections 213–228 (Overview)

Although not all details were available in the search results, these sections broadly cover:

- **Section 213** – Investigations ordered by Tribunal.
- **Section 214–217** – Rights, powers, procedures, duties of inspectors.
- **Section 218** – Protection of employees during investigation.
- **Sections 219–221** – Extent of inspector’s powers (subsidiaries, related entities).
- **Section 222** – Freezing of assets of the company.
- **Section 223** – Inspector’s report.
- **Section 224–228** – Actions based on investigation, prosecution, winding up, and legal consequences.

(Note: These are standard interpretations; Sections 210–212 came directly from cited results.)

3. Case Study: Bhushan Steel & SFIO

The Bhushan Steel matter is one of India’s most significant corporate fraud investigations, involving **loan fraud, fund diversion, shell companies, and corporate mismanagement**.

A. Background

- Bhushan Steel Ltd. was a major steel manufacturer in India, heavily financed by public sector banks.
- It defaulted on loans amounting to **₹45,000–₹56,000 crore** and became one of India’s largest NPAs. [[lawfullegal.in](#)], [[economicti...atimes.com](#)]
- The company later underwent CIRP (Insolvency) and was acquired by Tata Steel in 2018. [[economicti...atimes.com](#)]

B. Nature of Fraud

Investigations by SFIO, ED, and CBI revealed:

1. **Siphoning and diversion of bank loan funds** through a web of shell companies.
 - Promoters rotated funds through **157 associated companies**.
2. **Manipulation of financial statements, fake documentation**, and misrepresentation to banks.
3. **Misuse of company funds for personal benefit** and non-business activities.

C. Role of SFIO

- SFIO filed charge sheets alleging embezzlement and fund siphoning.
- SFIO summoned directors, including nominee directors, though some summons were challenged legally.
- Proceedings related to certain directors were restored by the Supreme Court in 2025.

D. Enforcement Directorate (ED) Findings (linked to SFIO charge sheet)

- Several executives arrested for money laundering connected with the fraud.
- ED stated that promoters rotated funds across multiple entities and created shell companies.

E. Governance & Regulatory Lessons

- Corporate fraud of this magnitude highlights severe failures in:
 - Internal controls
 - Auditor oversight
 - Board-level supervision
 - Disclosure and RPT governance
- Strengthened the need for:
 - SFIO empowered investigative authority
 - Auditor rotation
 - Stronger insolvency and recovery mechanisms under IBC (reinforced in judgments).

4. Summary

SFIO

- Premier multi-disciplinary fraud investigation agency.
- Investigates complex frauds, exclusively empowered under Section 212.

Sections 210–228

- Legal backbone for corporate investigations.
- CG can order investigations; SFIO has exclusive powers; fraud offences become non-bailable.

Bhushan Steel

- Massive loan fraud, involving fund diversion and shell company networks.
- SFIO played a central role; ED and CBI investigations complemented findings.
- Illustrates failures in governance and importance of strong investigative mechanisms.