

Company Auditor Series

Chap. 2 - Qualifications & Disqualifications



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Namaste

In Chapter 2 of this series, we would discuss the qualification and disqualifications of an auditor. Unless a person is qualified **and** is not disqualified, he/she/it cannot be an auditor of a company.

Qualification

Basically, there is only one qualification for a person to be appointed as an auditor of a company, which in simple language is that he/she should be a Chartered Accountant in Practice. Section 141(1) of the Act provides that a person shall be eligible for appointment as an auditor of a company only if he is Chartered Accountant.

Chartered Accountant has been defined in section 2 (17) of the Act as under:

“Chartered Accountant” means a chartered accountant as defined in clause (b) of subsection (1) of section 2 of the Chartered Accountant Act, 1949 (38 of 1949) who holds a valid certificate of practice under sub section (1) of section 6 of that Act.”

Further, as per section 2(1)(b) of the Chartered Accountant Act, 1949, ‘Chartered Accountant’ means a person who is a member of the Institute and section 6(1) of the said Act states that no member of the institute shall be entitled to practice whether in India or elsewhere, unless he has obtained from the council a certificate of practice. Hence, it is clear that the word “Chartered Accountant” has been used throughout the Act, unless the context otherwise requires, to mean a Chartered Accountant in practice.

Not only an individual but a firm or LLP may also be appointed as an auditor. However, proviso to section 141(1) clarifies that only such audit firms would be eligible to be appointed as auditor of the company where majority of the partners practicing in India are Chartered Accountants.

Section 141(2) states that where a firm including a Limited Liability Partnership (LLP) is appointed as an auditor of a company, only the partners who are Chartered Accountants shall be authorized to act and sign on behalf of the firm. The provision envisaged the position when Multi-Disciplinary Partnerships (MDPs) is allowed by the regulators i.e., ICAI, ICSI, ICMA, etc., which has already been put in place by ICAI and the Form 18 under ICAI regulations has been amended

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on approval by MCA on 1st July 2021. ICAI has issued Guidelines for Formation of Multi-disciplinary Partnership (MDP) effective from 8th July 2021. According to it, members of following professional bodies have been permitted to become a partner as on date:

- a) Company Secretary, member, The Institute of Company Secretaries of India.
- b) Cost Accountant, member, The Institute of Cost and Works Accountants of India.
- c) Advocate, member, Bar Council of India (However Bar Council of India, currently does not allow the same).
- d) Engineer, member, The Institution of Engineers, or Engineering from a University established by law or an institution recognized by law.
- e) Architect, member, The Indian Institute of Architects.
- f) Actuary, member, The Institute of Actuaries of India (who is not in practice as per IAI).

Hence, the following are qualified to be appointed as an auditor of a company as on date:

1. A Chartered Accountant in Practice (Individual or sole proprietor)
2. A Partnership Firm, whereof all of the partners are Chartered Accountants practicing in India.
3. A Partnership Firm being Multi-disciplinary Partnership (MDP), whereof majority of partners are Chartered Accountants practicing in India
4. A Limited Liability Partnership (LLP), whereof all of the partners are Chartered Accountants practicing in India.
5. A Limited Liability Partnership (LLP) being Multi-disciplinary Partnership (MDP), whereof majority of partners are Chartered Accountants practicing in India

However, in a MDP, only the partners who are Chartered Accountants shall be authorized to act and sign on behalf of the firm as auditor.

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Disqualifications

A person may be qualified to be appointed as auditor, yet if he/she/it is disqualified due to provisions of section 141(3) of the Act, then he cannot be appointed as an auditor of a company. The said sub-section is to be read along with Rule 10 of Companies (Audit and Auditors) Rules 2014 to understand the disqualifications. For better understanding, these disqualifications may be divided into following categories:

- Absolute disqualification
- Disqualification based on a relationship
- Disqualification based on conflict of interest
- Disqualification based on services rendered

Absolute Disqualification

A person would be disqualified to be appointed or re-appointed as an auditor irrespective of his relationship or conflict of interest or nature of services rendered, in the following cases:

1. A Body Corporate, other than a Limited Liability Partnership (as LLP is a body corporate) – [S. 141(3)(a)]
2. A person in full-time employment elsewhere [S. 141(3)(g)]. However, Clause (11) of Part I of the First Schedule of the Chartered Accountants Act, 1949 read with relevant regulations and Council decisions requires specific and prior approval of the council for a member in practice to be in full-time or part-time employment. Hence, a member in part-time employment too cannot be appointed as an auditor.
3. An employee or officer of the company [S. 141(3)(b)]. Officer as per section 2(59) of the Act would include any:
 - a. Director

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- b. Manager
 - c. Key Managerial Personnel
 - d. Any person in accordance with whose directions or instructions the director(s) or Board is accustomed to act.
4. A person or a partner of a firm at the date of appointment or reappointment holds appointment as auditor of more than 20 companies [S. 141(3)(g)]. However, in case of appointment in a private company, the following would not be counted in the limit of 20 Companies:
- a. One Person Companies (OPC)
 - b. Dormant Companies
 - c. Small Companies
 - d. Private Companies having paid-up share capital less than Rs. 100 Crores
 - e. Foreign Companies [as they are not Company as per definition given u/s 2(20)]
 - f. Branch of a Company (as per Circular No. 21/75(35/3/75-CL.III) dated 24-9-1975)
5. A person who is convicted by the court for an offence involving fraud and 10 years have not elapsed since the conviction date [S. 141(3)(h)].

Disqualification based on a Relationship

A person would be disqualified to be appointed or re-appointed as an auditor based upon his relationship in the following cases:

- 1. A person who is a partner of an officer of the company [S. 141(3)(c)].
- 2. A person who is a partner of an employee of the company [S. 141(3)(c)].
- 3. A person who is in the employment of an officer of the company [S. 141(3)(c)].
- 4. A person who is in the employment of an employee of the company [S. 141(3)(c)].

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5. A person who's relative is:
- a. a director, or
 - b. in the employment of the company as a:
 - i. Director or
 - ii. Key Managerial Personnel [S. 141(3)(f)]

Relative as per section 2(77) would mean:

- Members of HUF
- Husband and wife
- Father (including step-father)
- Mother (including step-mother)
- Son (including step-son)
- Son's wife
- Daughter
- Daughter's husband
- Brother (including step-brother)
- Sister (including step-sister)

Disqualification of Auditor based on Conflict of Interest

A person would be disqualified to be appointed or re-appointed as an auditor based upon his conflict of interest in the following cases:

1. A person or his partner is holding any security of or interest (without any minimum exemption limit) in:
 - a. the company, or

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- b. its subsidiary, or
 - c. its holding company, or
 - d. associate company, or
 - e. subsidiary of such holding company [S. 141(3)(d)(i)]
2. A person's relative is holding any security of or interest in the company of face value exceeding Rs. 1 Lakh. However, in the event of acquiring any security or interest by a relative, above Rs. 1 Lakh, the corrective action to maintain the said limit shall be taken by the auditor within 60 days of such acquisition or interest to not be disqualified as an auditor [Proviso to S. 141(3)(d)(i) read with Rule 10(1)]
3. A person, or his relative or partner is indebted in excess of Rs. 5 Lakhs to:
- a. the company, or
 - b. its subsidiary, or
 - c. its holding company, or
 - d. associate company, or
 - e. subsidiary of such holding company [S. 141(3)(d)(ii) read with Rule 10(2)]
4. A person, or his relative or partner has given a guarantee or provided any security in connection with the indebtedness of any third person in excess of Rs. 1 Lakh to:
- a. the company, or
 - b. its subsidiary, or
 - c. its holding company, or
 - d. associate company, or
 - e. subsidiary of such holding company [S. 141(3)(d)(iii) read with Rule 10(3)]
5. A person, or the firm whether directly or indirectly, has business relationship with:

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- a. the company, or
- b. its subsidiary, or
- c. its holding company, or
- d. associate company, or
- e. subsidiary of such holding company

The term "business relationship" shall be construed as any transaction entered into for a commercial purpose, except those commercial transactions which are:

- in the nature of professional services permitted to be rendered by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts
- in the ordinary course of business of the company at arm's length price - like sale of products or services to the auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses.

[S. 141(3)(e) read with Rule 10(4)]

Disqualification based on Nature of Other Services Rendered

A person would be disqualified to be appointed or re-appointed as an auditor based upon his nature of other services rendered in the following cases:

1. A person who, directly or indirectly, renders any service referred to in section 144 to:
 - a. the company or
 - b. its holding company or
 - c. its subsidiary company [S. 141(3)(i)]

The services referred in section 144 are:

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- a) accounting and book keeping services
- b) internal audit
- c) design and implementation of any financial information system
- d) actuarial services
- e) investment advisory services
- f) investment banking services
- g) rendering of outsourced financial services
- h) management services

The term “directly or indirectly” for the purposes of disqualifications shall include rendering of services by the auditor:

- in case of auditor being an individual:
 - either himself or
 - through his relative or
 - any other person connected or associated with such individual or
 - through any other entity, whatsoever, in which such individual has significant influence or control, or
 - whose name or trade mark or brand is used by such individual
- in case of auditor being a firm:
 - either itself or
 - through any of its partners or
 - through its parent, subsidiary or associate entity or
 - through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or
 - whose name or trade mark or brand is used by the firm or any of its partners.

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Casual Vacancy

There could be a case that at the time of appointment of the auditor, he/she/it is qualified as well as not disqualified. However, later after appointment the auditor is disqualified due to any of the reasons stated above, then, he shall vacate his office and it shall deem to be a casual vacancy in the office of the auditor.

I hope this document is of use to you. I thank *CA. Shreya Jain and CA. Himani Gupta* in assisting me to compile this part of the series. Your suggestions and comments would be highly appreciated.

Best Regards

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EARLIER CHAPTER

<i>Chapter No.</i>	<i>Title</i>	<i>Link</i>
1	Types of Audits	F_6984.pdf (lunawat.com)

(Disclaimer: Though full efforts have been made to state the interpretations correctly, yet the author is not responsible / liable for any loss or damage caused to anyone due to any mistake / error / omissions)

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ABOUT CA. PRAMOD JAIN

He is a commerce graduate [B. Com (H)] from Shri Ram College of Commerce (SRCC). He is a fellow member of the Institute of Chartered Accountants of India (FCA). He is a fellow member of the Institute of Companies Secretaries of India (FCS). He is a fellow member of the Institute of Cost Accountants of India (FCMA). He is a Bachelor of Law (LL.B). He has qualified Information System Auditor [DISA (ICAI)]. He is also a member of All India Management Association (MIMA). He is also an Insolvency Professional (IP). He has also passed the Certificate Course on CSR of ICAI. He has also passed the Proficiency Self-Assessment Test for Independent Director's Databank. He has passed certification course NCFM of National Stock Exchange of India (NSE). He has also done certification course CAAT of ICAI. He has also done post qualification certificate course on Valuation of ICAI.

He has been elected as Central Council Member of ICAI for the period 2019 – 2022. Apart from being member in more than 25 committees / groups / directorates of ICAI, he is / was:

- Chairman of Committee on International Taxation (CITAX) for Year 2021-22
- Chairman of Taxation Audit Quality Review Board (TAQRB) for the year 2021-22.
- Chairman of Valuation Standards Board (VSB) for the year 2020-21.
- Chairman of CSR Committee of ICAI for year 2020-21.
- Vice-Chairman of Committee on MSME & Start-up for the year 2021-22.
- Vice-Chairman of Women Members Empowerment Committee (WMEC) for 2021-22.
- Vice-Chairman of Direct Tax Committee (DTC) for year 2019-20 and 2020-21.
- Vice-Chairman of Committee on International Taxation (CITAX) for Year 2019-20.
- Member of ICAI Disciplinary Committee Bench 1 for year 2020-21.
- Nominated as Member of Quality Review Board (QRB) for 3 years from 2020 to 2022.

He is the conceptualizer of the portal www.expertspanel.in which is a one stop solution for all professional queries which has given around 29000 answers since its launch in mid of year 2018.

He is delivered more than 1300 lectures and articles on various topics of Income Tax, Corporate Laws, LLP, Audits, Peer Review, Quality Review, etc. at more than 200 forums throughout the country. Most of his presentations and articles since 2013 are available for free download from www.lunawat.com and from 2018 at www.expertspanel.in also.

He is president, founder convener and member of various Boards, Directorate, Committees, Study Circles, etc. of ICAI, ICSI and other prestigious bodies and associations. He has been a Technical Reviewer with FFRB and Quality Review Board and Peer Reviewer with Peer Review Board. He has authored 13 books including “Chartered Accountant’s Documentation and Compliance for Audits and Reviews”, *Limited liability Partnership – A Complete Resource Book*”, and “Accounting Standards and CARO”.