

# Appointment of first auditors – issues to be addressed

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## Introduction

Subject to the provisions of Chapter 'X' of the Companies Act, 2013 (Act), on 'Audit and Auditors,' every company shall, at the first annual general meeting ("AGM"), appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting and the manner and procedure of selection of auditors by the members of the company at such meeting shall be such as prescribed under Rule 3 of the Companies (Audit and Auditors) Rules, 2014 **[section 139(1)]**.



Notwithstanding anything contained in sub-section (1), the first auditor of a company, other than a government company, shall be appointed by the Board of directors within 30 days from the date of registration of the company and in the case of failure of the Board to appoint such auditor, it shall inform the members of the company, who shall within 90 days at an extraordinary general meeting appoint such auditor and such auditor shall hold office till the conclusion of the first annual general meeting **[section 139(6)]**.

Accordingly, the first auditors are appointed:

- a) By the Board of directors in Board meeting within 30 days from the date of incorporation;
- b) If the Board fails to appoint, the members will appoint the first auditors in extra-ordinary general meeting within **90 days**.

## Time frame for filling the position of first auditors

It is provided that the first auditors of the company shall be appointed by the Board of directors within **30 days from the date of incorporation** and if it fails to appoint such first auditors, it shall inform the members of the company, who **shall within ninety days** at an extraordinary general meeting appoint such auditor and such auditor shall hold office till the conclusion of the first annual general meeting.

However, it is not clear from the provisions, if the Board has failed to appoint first auditors, then within how much time the Board shall intimate the same to the members, who will thereupon appoint first auditors at the general meeting. There is no time limit prescribed for the Board of directors within which the general meeting of shareholders will be called for, for appointment of first auditors. The law is silent regarding from when this time limit of 90 days is reckoned.

As per section 139(6), the Board has to appoint auditor within 30 days or if the Board fails to appoint, then on 31st day onwards, it is the Board's duty to inform the members about such failure of the Board for appointment of first auditor. The members, shall within 90 days from the date of information being sent to them, appoint auditor and such auditor shall hold office till the conclusion of the first annual general meeting. As stated above, the duty of the Board to inform members about their failure to appoint first auditor, triggers immediately on expiry of the 30 days period whereas the duty of the members of the company to appoint first auditor, triggers immediately on receipt of information of non-appointment by the Board. The members of the company cannot be presumed to be aware of the fact that the first auditor has not been appointed by the Board and in the absence of receipt of any information or notice of extraordinary general meeting in this regard, it cannot be said that the shareholders are required to appoint first auditor before expiry of 120 days from the date of registration/ of the company. The duty or the power of members of the company to appoint first auditor triggers from the date of being informed about such non-appointment by the Board of directors.

In the absence of any clear provisions in the Act, different practices are being followed in the corporate world.

**Case 1:** If the Board fails to appoint first auditors within 30 days, the members shall within 90 days from the date of incorporation appoint first auditors.

**Case 2:** If the Board fails to appoint first auditors, then on 31st day onwards, it is the **Board's duty** to inform the members about such failure and upon information, the members shall appoint the first auditors within period of 90 days from such information.

**Case 3:** If the Board fails to appoint first auditors, it is on the **will** of the Board to inform the members. Upon information, the members shall appoint the first auditors within period of 90 days from such information.

This gap needs to be addressed.

## Shareholders fail to appoint

The next gap to be addressed is, when the shareholders fail to appoint the first auditors for any reason, who will take necessary steps to appoint such first auditors?

There is no express provision in the Act, as how to fill vacuum in the appointment of first auditors in case, first the Board and subsequently, the shareholders fail to appoint the first auditors in the company.

Whether the Registrar of Companies or Central Government will be handed over the responsibility for appointment of First Auditors in the above case, is another issue.

These questions need to be addressed as there are no clear provisions in the Act.

## Penal provisions

Once the company fails to appoint the first auditor in the company, the company will be in default, and as per section 147 of the Companies Act, 2013, the company will be liable as per the section reproduced below:

If any of the provisions of section 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less **than twenty-five thousand rupees** but which may extend to **five lakh rupees** and every officer of the company who is in default shall be **punishable** with fine which shall not be less than **ten thousand rupees** but which may extend to **one lakh rupees**.

However, in the absence of any clarity on the timelines on both the situations, the penal provisions are redundant, I suppose.

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[mca.gov.in/SearchableActs/Section147.htm](http://mca.gov.in/SearchableActs/Section147.htm)

### 147. Punishment for contravention

(1) If any of the provisions of sections 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees 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 shall not be less than ten thousand rupees but which may extend to one lakh rupees, or with both.

(2) If an auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees: Provided that if an auditor has contravened such provisions knowingly or wilfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.

(3) Where an auditor has been convicted under sub-section (2), he shall be liable to—