

Secretarial Audit – A Measure to Strengthen Corporate Governance

Secretarial audit plays a crucial role in ensuring compliance with regulatory requirements and identifying any non-compliance issues within companies. It has become an essential tool for enhancing transparency and accountability, thereby fostering investor confidence and strengthening corporate governance practices. With advancements in technology, secretarial audit processes have become more efficient through digitalization and automation, enabling auditors to streamline procedures and manage data effectively.



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INTRODUCTION

The evolution of secretarial audit in India reflects the changing regulatory landscape and the growing emphasis on corporate governance and compliance. The concept of secretarial audit was initially introduced in the Companies Act, 1956 regime, wherein it focussed only on ensuring compliance with statutory provisions. With time, the amendments to Companies Act and other regulatory requirements have resulted in providing impetus to the secretarial audit framework and enhancing its scope and relevance. One of the major provisions enhancing the significance was introduction of the SEBI (Listing Obligations and Disclosure Requirements) Regulations in 2015 ('SEBI(LODR)'). These regulations required the listed companies to mandatorily have secretarial audits, reinforcing the importance of transparency and accountability in the corporate sector. Moreover, the Companies Act, 2013 brought about substantial changes, expanding the scope of secretarial audits to cover various aspects such as related party transactions and Corporate Social Responsibility.

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have become more efficient through digitalization and automation, enabling auditors to streamline procedures and manage data effectively.

Continual refinement of the secretarial audit framework is necessary to keep pace with evolving regulatory standards and corporate governance norms. Auditors must stay updated with amendments to laws and regulations, aligning their procedures with international best practices to ensure effectiveness and relevance.

REGULATORY LANDSCAPE

In India, the requirements of secretarial audit are primarily governed by the provisions of the Companies Act, 2013, and SEBI (LODR). Following are the key aspects:

- **Mandatory requirement:** As per Section 204 of the Companies Act, 2013, certain classes of companies are required to obtain a secretarial audit report from a practicing Company Secretary, which include:
 - ♦ Every listed company is required to conduct a secretarial audit of its records every year,
 - ♦ Any public company with a paid-up share capital of at least ₹50 crores or a yearly revenue of at least ₹250 crores,
 - ♦ Every company having outstanding loans or borrowings from banks or financial institutions of ₹100 crores or more.
- **Scope of audit:** Secretarial audit covers various aspects such as compliance with the provisions of the Companies Act, applicable rules and regulations, Memorandum and Articles of Association of the company, and other relevant laws.
- **Corporate governance:** Secretarial audit assesses the effectiveness of corporate governance practices adopted by the company, including the constitution and functioning of the Board of Directors, board committees, and comply with corporate governance guidelines in true letter and spirit.
- **Compliance with SEBI regulations:** For listed companies, compliance with SEBI regulations, including LODR, forms an integral part of the



secretarial audit. This includes disclosures, reporting requirements, and adherence to corporate governance norms prescribed by SEBI.

- **Disclosure and reporting:** The auditor is required to prepare a comprehensive report detailing their findings, observations, and recommendations. This report is submitted to the board of directors and is also disclosed in the company's annual report.
- **Penalties for non-compliance:** Non-compliance with the requirements of secretarial audit can attract penalties under the Companies Act, including fines and other legal consequences. Therefore, it is imperative for companies to ensure timely and accurate compliance with the provisions.
- **Continuous monitoring and compliance:** Secretarial audit is not a one-time exercise; it is conducted periodically to ensure continuous monitoring and compliance with regulatory requirements. This helps companies in identify and rectify any non-compliance issues in a timely manner.

RELEVANCE OF SECRETARIAL AUDIT

The principle logic behind mandating secretarial audit lies in promoting good corporate governance, enhancing transparency, and ensuring compliance with regulatory requirements in the corporate sector. Some of the pertinent reasons include:

- **Enhancing corporate governance:** Secretarial audit necessitates the companies to adhere to the principles

of good corporate governance. By examining the company's internal controls, processes, and compliance with laws and regulations, secretarial audit contributes to the efficient functioning of the Board of Directors and the overall governance structure.

- **Ensuring regulatory compliance:** Companies operate within a complex regulatory environment, with numerous laws, regulations, and guidelines to adhere to. Mandating secretarial audit ensures that companies comply with these requirements, reducing the risk of non-compliance, legal disputes, and penalties.
- **Protecting stakeholder interests:** Secretarial audit helps to protect the interests of various stakeholders, including shareholders, employees, creditors, and the public. By providing assurance on the company's compliance with laws and regulations, secretarial audit instils confidence among stakeholders and fosters trust in the company's management and operations.
- **Detecting and preventing fraud and mismanagement:** Secretarial audit plays a crucial role in detecting and preventing fraud, mismanagement, and other irregularities within the company. By conducting a thorough examination of the company's records, transactions, and internal controls, auditors can identify potential areas of concern and recommend corrective measures.
- **Improving transparency and disclosure:** Transparency is essential for maintaining trust and confidence in the corporate sector. Mandating

secretarial audit ensures that companies disclose relevant information accurately and transparently, enabling stakeholders to make informed decisions about their investments, transactions, and dealings with the company.

- **Aligning with international best practices:** Many countries around the world, mandate some form of corporate governance and compliance auditing. By mandating secretarial audit, India aligns itself with international best practices, demonstrating its commitment to global standards of corporate governance and transparency.

GLOBAL TRENDS

Secretarial audit has also evolved in global context and it has resulted in:

- **Global adoption of Corporate Governance codes:** Many countries have adopted or updated corporate governance codes, which often include provisions related to secretarial audit or similar compliance mechanisms.
- **Increase in regulatory scrutiny and enforcement:** Regulatory bodies worldwide have been increasing scrutiny on corporate governance practices, leading to a rise in enforcement actions and penalties for non-compliance.
- **Rise in demand for compliance services:** There has been a growing demand for compliance services, including secretarial audit, as companies seek to navigate complex regulatory requirements and mitigate compliance risks. According to a report by Grand View Research, the market size of global compliance management software was valued at \$2.8 billion in 2022 and is expected to grow at Compounded annual growth rate (CAGR) of 11.6% reflecting the increasing emphasis on compliance.
- **Focus on ESG and sustainability reporting:** Environmental, Social, and Governance (ESG) factors have become integral to corporate governance and reporting practices. According to a survey by Deloitte, 88% of executives identified sustainability as a significant priority and will impact their business, indicating a growing focus on non-financial reporting and compliance.
- **Adoption of technology in compliance:** The adoption of technology, including AI, data analytics, and automation, has been accelerating in compliance processes, including secretarial audit. A survey by PwC found that 91% of compliance officers believe that technology will fundamentally change how compliance is conducted over the next five years.

While these statistics may not directly relate to secretarial audit alone, they provide insights into broader trends in corporate governance, compliance, and regulatory oversight that impact the demand for and evolution of secretarial audit practices.

Secretarial audit covers various aspects such as compliance with the provisions of the Companies Act, applicable rules and regulations, Memorandum and Articles of Association of the company, and other relevant laws. In India, the requirements of secretarial audit are primarily governed by the provisions of the Companies Act, 2013, and SEBI (LODR).

STRENGTHENING CORPORATE GOVERNANCE

Strengthening corporate governance through secretarial audit involves implementing measures to enhance transparency, accountability, and compliance with regulatory requirements. Some of the steps include:

- **Expand scope of secretarial audit:** Widen the scope of secretarial audit to cover additional areas relevant to corporate governance, such as risk management practices, ethical standards, and sustainability initiatives. This will ensure a comprehensive examination of governance practices beyond statutory compliance.
- **Enhance reporting requirements:** Introduce more robust reporting requirements for secretarial audit reports, mandating detailed disclosures on governance practices, Board effectiveness, and compliance with codes and standards. This would provide stakeholders with greater insights into the company's governance framework.
- **Regular Board evaluations:** Require companies to conduct regular evaluations of the Board of Directors and its committees, with the findings included in the secretarial audit report. This helps to identify areas for improvement and enhances the effectiveness of the board in overseeing corporate affairs.
- **Whistle blower mechanisms:** While whistle blower mechanism is mandatory for select class of companies, expanding its coverage and requiring the secretarial auditor to assess the effectiveness of such mechanisms, will go a long way in promoting transparency and accountability within the organization. This encourages the reporting of unethical behaviour and misconduct.
- **Training and awareness programs:** Introduce mandatory training programs for Directors, senior management, and employees on corporate governance principles, regulatory requirements, and ethical conduct. The secretarial auditor can assess the effectiveness of these programs in promoting a culture of governance and compliance.



- **Disclosure of related party transactions:** Strengthen disclosure requirements for related party transactions and require the secretarial auditor to scrutinize such transactions for potential conflicts of interest or abuse. Enhanced transparency in related party transactions improves investor confidence and mitigates risks of insider dealings.
- **Review of internal controls:** Conduct a thorough review of the company’s internal control systems specifically relating to compliances, as part of the secretarial audit process. Identify weaknesses or deficiencies in internal controls and recommend measures to strengthen them, thereby reducing the risk of fraud, mismanagement, and non-compliance.
- **Benchmarking against best practices:** Encourage companies to benchmark their governance practices against international best practices and industry standards. The secretarial auditor can assess the company’s governance framework relative to these benchmarks and provide recommendations for improvement.
- **Board diversity and independence:** Promote Board diversity and independence by introducing guidelines or regulations requiring companies to have a diverse Board composition with adequate representation of Independent Directors. The secretarial auditor can evaluate the Board’s composition and independence as part of the audit process.
- **Stakeholder engagement:** Emphasize the importance of stakeholder engagement in governance practices and require companies to disclose their engagement policies and initiatives. The secretarial auditor can assess the effectiveness of stakeholder engagement efforts in promoting accountability and responsiveness to stakeholder interests.
- **Policies and procedures:** As per the requirements of SEBI (LODR), listed companies are required to develop

various policies like policies on material subsidiaries, related party transactions, dividend, etc. Ensuring that the transactions are within the ambit of these policies as defined and approved by the Management and Board of Directors, contribute in strengthening the corporate governance practices.

Companies can strengthen their corporate governance mechanism and practices thereby, fostering a culture of transparency and accountability. The role of secretarial audit is pivotal in ensuring observance of these measures and promoting good governance standards across the corporate sector.

ARTIFICIAL INTELLIGENCE (AI) AND SECRETARIAL AUDIT

The buzzword and the most relevant concept today is ‘artificial intelligence’. AI is ubiquitous and has relevance in every sphere of personal and professional lives. AI has the potential to revolutionize the field of secretarial audit by automating repetitive tasks, enhancing data analysis capabilities, and improving overall efficiency and accuracy. The following steps can be considered to integrate the AI with the procedures performed:

- **Automation of routine tasks:** AI technologies can automate routine tasks involved in the audit process, such as data collection, document analysis, and report generation. This frees up auditors’ time to focus on more complex and strategic aspects of the audit, improving productivity and efficiency.
- **Data analytics and pattern recognition:** AI-powered data analytics tools can analyze large volumes of data to identify patterns, trends, and anomalies that may indicate potential compliance issues or irregularities. This helps auditors uncover insights more effectively and prioritize areas for further investigation. Natural language processing (NLP) can assist auditors in extracting relevant information from textual

documents and identifying compliance requirements more efficiently.

- **Risk assessment and predictive analytics:** AI algorithms can assess the risk associated with various compliance areas and predict potential areas of non-compliance based on historical data and patterns. This enables auditors to proactively address risks and prioritize audit activities accordingly.
- **Continuous monitoring and surveillance:** AI-powered monitoring systems can continuously monitor corporate activities, transactions, and communications in real-time to detect potential compliance breaches or fraudulent behavior. This proactive approach helps companies to identify and address issues before they escalate.
- **Robotic process automation (RPA):** RPA bots can perform repetitive and rule-based tasks such as data entry, reconciliation, and compliance checks with high accuracy and speed. Integrating RPA into the audit process reduces manual effort, minimizes errors, and enhances audit efficiency.
- **Blockchain technology:** It can be leveraged to improve the integrity and transparency of audit trails by creating immutable records of transactions and activities. This enhances the reliability and trustworthiness of audit findings and ensures the integrity of audit processes.

Integration of AI into secretarial audit processes has the potential to revolutionize the way audits are conducted, making them more efficient, effective, and insightful. With the use of AI technologies, auditors can enhance their capabilities, improve risk assessment, and contribute to stronger corporate governance and compliance practices.

ROLE OF PROFESSIONALS

Company Secretaries play a vital role in strengthening secretarial audit and adding value to the audit process through their expertise, knowledge, and experience they can contribute by:

- **Expertise in corporate law and governance:** Company Secretaries possess in-depth knowledge of corporate law, regulations, and governance practices. They ensure that the secretarial audit process complies with relevant legal and regulatory requirements, providing assurance on the company's meeting corporate governance standards.
- **Facilitating compliance:** Company Secretaries facilitate compliance with statutory requirements by ensuring that corporate actions, decisions, and filings are in accordance with applicable laws and regulations. They maintain proper records, documentation, and registers, which are essential for the secretarial audit process.
- **Advisory role:** Company Secretaries advise the Board of Directors and senior management on corporate governance matters, regulatory changes,

and compliance obligations. They provide guidance on best practices, risk management, and corporate governance frameworks, adding value to the audit process by helping to mitigate risks and enhance governance practices.

- **Ensuring Board effectiveness:** Company Secretaries play a key role in ensuring the effectiveness of the Board of Directors and its committees. They assist in organizing board meetings, preparing agendas and minutes, and facilitating communication between Board members. This ensures proper oversight and governance, which are integral to the secretarial audit process.
- **Managing stakeholder relationship:** Company Secretaries manage shareholder relations by facilitating communication, managing shareholder meetings, and ensuring compliance with shareholder rights and obligations. They play a crucial role in ensuring transparency, accountability, and fairness in dealings with shareholders, which contributes to the integrity of the audit process.
- **Risk management and internal controls:** Company Secretaries contribute to risk management and internal control processes by identifying, assessing, and mitigating risks related to compliance, governance, and regulatory matters. They establish robust internal control mechanisms and compliance frameworks, which are essential for the effectiveness of the secretarial audit process.
- **Continuous professional development:** Company Secretaries engage in continuous professional development to stay updated with changes in corporate laws, regulations, and governance practices. They leverage their knowledge and expertise to enhance the quality and effectiveness of the secretarial audit process, ensuring that it remains relevant and valuable to the organization.

Company Secretaries play a multifaceted role in strengthening secretarial audit and adding value to the audit process. Their expertise in corporate governance, compliance, and regulatory matters, combined with their advisory role and commitment to professional development, contributes to the integrity, transparency, and effectiveness of the audit process, ultimately enhancing corporate governance practices and adding value to the organization.

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