



ROLE OF AUDIT COMMITTEE IN CORPORATE GOVERNANCE

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Abstract

In present era audit committees are seen as Key pivot of the Organizations. The Audit committee acts as major pillar of the corporate governance system. The present study aims at examining the roles and responsibilities of audit committees. It is based on the analysis of annual reports of Nifty 50 companies. The Objectivity is achieved through the codes of corporate governance practices. Revised clause 49 is taken as benchmark for the current study. The results of the study have revealed that there is high level of transparency in role played by audit committee. Majority of the companies have followed the provisions of clause 49 of audit committee. The study covers the Introduction, literature review, objectives, analysis and findings and conclusion.

Keywords: *Corporate Governance, Clause 49, Audit committee, Sarbans-oxley act, CNX NIFTY 50, Blue Ribbons committee report, OECD.*

INTRODUCTION

Corporate Governance is considered as fair and transparent mechanism to run the corporations in such a way which would enhance the long term shareholder value and provides benefits to the society. But increase in the number of frauds committed by high profile companies (e.g. Enron, WorldCom, AIG Insurance, Lehman Brothers, Satyam etc) has shaken the public confidence in financial reporting process and audit functions. Auditors are expected to be overseers of the organizations, who are responsible for promoting transparency, fairness and accountability relating to participants of organizations. There are many instances of auditors indulging in unethical practices and failed to whistle blow when things went wrong in the organization. The primary function of audit committee is to fulfill its oversight responsibilities by reviewing the financial statements that will be provided to the shareholders and others. After a series of corporate scandals, the whole world is paying close attention to the issues of how to strengthen information asymmetry. To protect the investors from deceptive accounting practices of organizations, regulatory bodies as well as Indian Government appointed many Committee, R.D Joshi Committee, Kumar Mangalam Committee, Narayana Mirthy Committee and Naresh Chandra Committee played important role in framing role and responsibilities of Audit committee. In October 2004, SEBI announced the revised clause 49, which made major changes in the strengthening the roles and responsibilities of audit committees. The companies shall be required to comply with the requirements of Clause 49 in relation to audit committee. The Current study aims at investigating the roles and responsibilities of audit committee by taking clause 49 as benchmark.

LITERATURE REVIEW

The Issue of Audit committee is much debated worldwide. There are number of studies on Audit committee's role in Corporate Governance.

J Donald, Kirk and Siegal Arthur (1996) have analyzed How Directors and Auditors can improve Corporate Governance. Advisory Panel in this report has suggested the ways to enhance the value of audit. This study has suggested "best practices" by shifting its focus from a compliance and rule-oriented audit to one recognizing the board to directors as its client and by becoming part of what is called a "corporate governance "approach to improve financial reporting.

Lillis Bob and Lane Robin (2007) have analyzed the study on auditing the Strategic role of Operations. This study made a contribution to furthering understanding of the auditing of the strategic role and contribution of operations



by conducting a review and critique of established ideas, practices and approaches from both strategy formulation perspectives. It argued that the reported methodologies reflect the traditional outside-in perspective to strategy formulation.

R. Robinson Diana, N.C, Lisa A .Owens-Jackson (2009) have investigated Audit Committee characteristics and Audit Changes. This Study has examined whether five audit committee characteristics (Independence, Financial Expertise, Diligence, Governance Expertise and firm seeking knowledge) are related to Audit Changes. Increased independence, financial expertise and firm-specific knowledge are significantly related with reduced incidences of auditor changes. Alternatively, diligence and governance experience did not seem to have any real effect on reducing auditor changes.

Saibaba M D and Valeed Ahmed Ansari (2011) have done a study on Audit Committees and Corporate Governance. This study examined the relationship between the Independence of the audit committee, board independence and firm performance of listed firms segmented between BSE 100 and BSE 200 indices, for the year 2007 and 2008. Firm performance has been measured by Tobin's Q. The Results have shown positive relationship between Audit committee index and firm value.

OBJECTIVES OF THE STUDY

The study has the following two objectives:

1. To examine the role and responsibilities of audit committee.
2. To know the status of compliance of audit committee with the revised clause 49.

RESEARCH METHODOLOGY

Period of the study: This study is based on the annual reports of the year 2012-13.

Sample Size: Sample size is Nifty 50 companies. Out of 50 Nifty companies, 3 companies (ACC LTD, Ambuja Ltd and Ranbaxy laboratories ltd) annual reports are not available. So study includes total 47 companies.

Data collection: Data has been collected through annual reports, websites of companies.

ANALYSIS AND FINDINGS

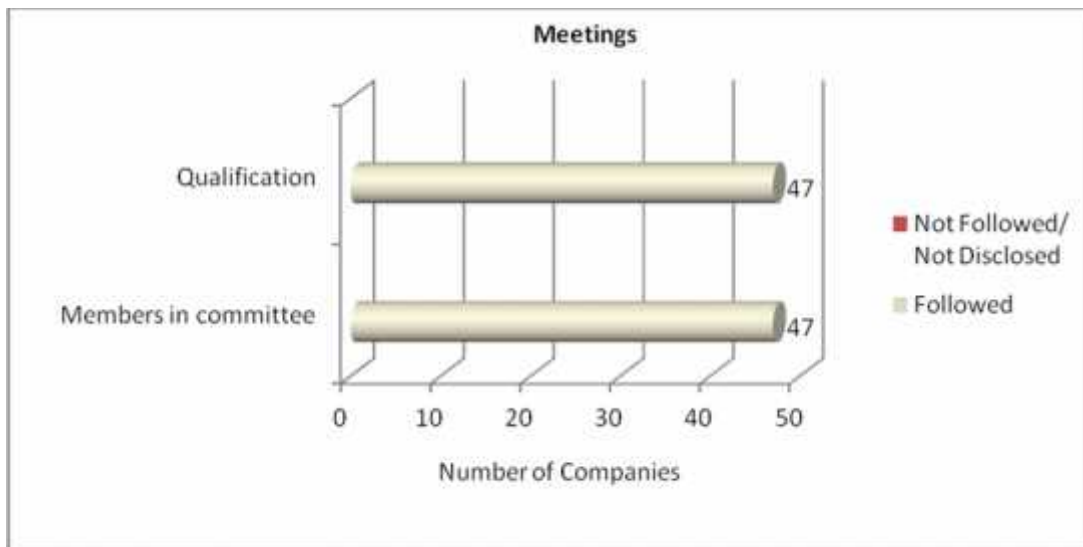
A detail of analysis along with graphical representation has been provided. The analysis is presented on the basis of revised clause 49.

1. **Qualified and independent committee :** As per clause 49 companies should have qualified and independent committee which includes:
 - a) No. of members in a committee (Minimum three)
 - b) Qualification of members (Financially literate)
 - c) Chairman to be independent director
 - d) Chairman to be present at AGM
 - e) Company secretary act as secretary to the audit committee.

It was found that all the companies had followed the provisions of clause 49 with regard to establishment of audit committee with an independent director, all the members of audit committee were financially literate and chairman of audit committee was present at AGM. Only 2 companies had not provided any information regarding company secretary act as secretary to the audit committee.



2. **Meetings of audit committee:** As per clause 49 Committee should meet at least four times in a year and not more than gap of four months between two meetings. And the quorum should be either two members or 2/3rd members of audit committee whichever is greater. But two minimum independent directors should be present. It was observed that all 47 companies have followed the provisions regarding meetings and quorum.

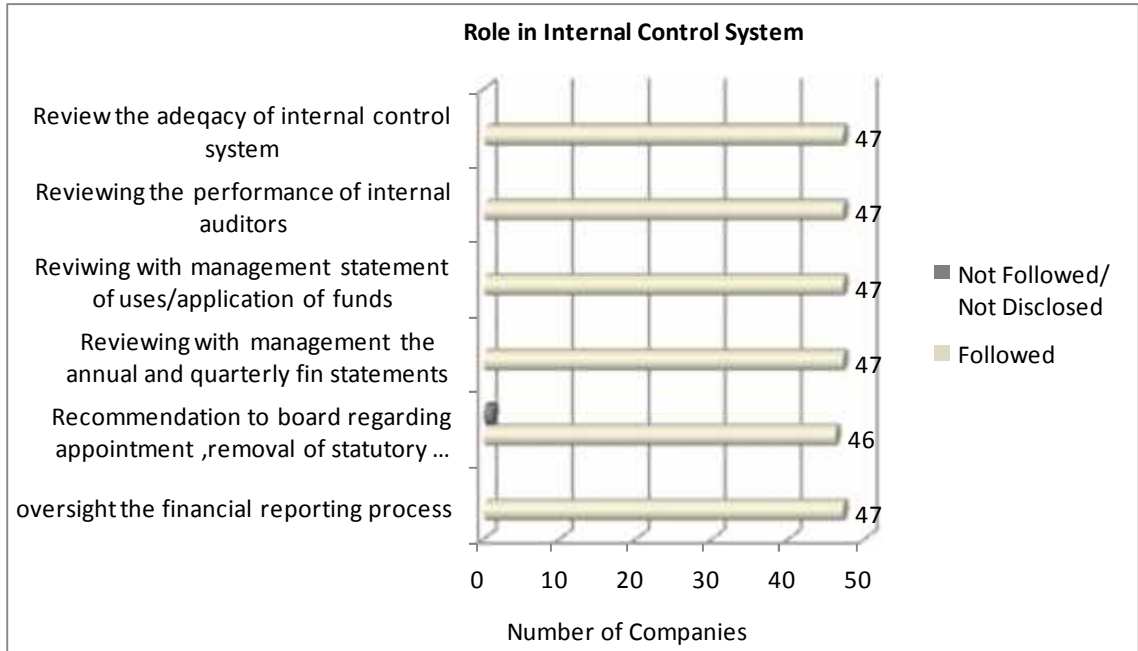


3. **Role of audit committee:** Audit committee is the major pillar of corporate governance which plays an important role in checking corporate misconduct. It plays significant role in oversight company's risk management policies. It has been expected from the audit committee to certify the accounts in fair and transparent manner. There are various instances where auditors involved themselves in unethical practices and failed to whistle blow when things went wrong.

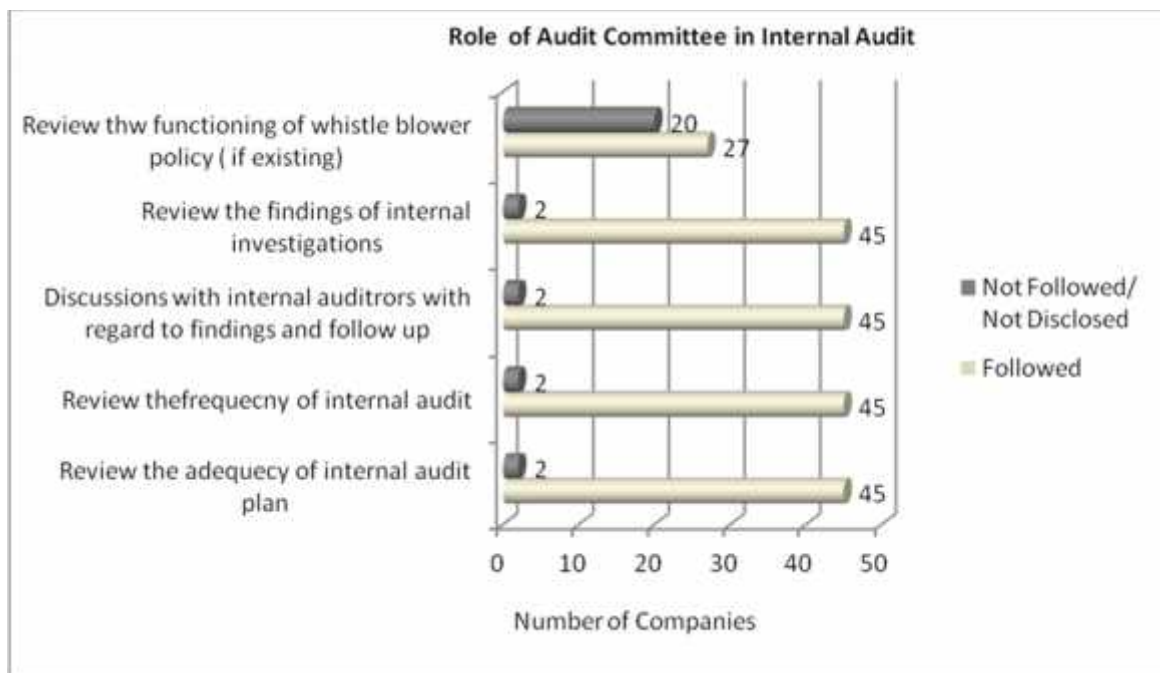
The role of audit committee is covered under three sub headings:



- a) **Role of audit committee in internal control system:** It was found from the analysis that, audit committees of all the companies complied with the provisions of internal control system. Only one company has not provided information regarding audit committees role in appointment or removal of statutory auditor.

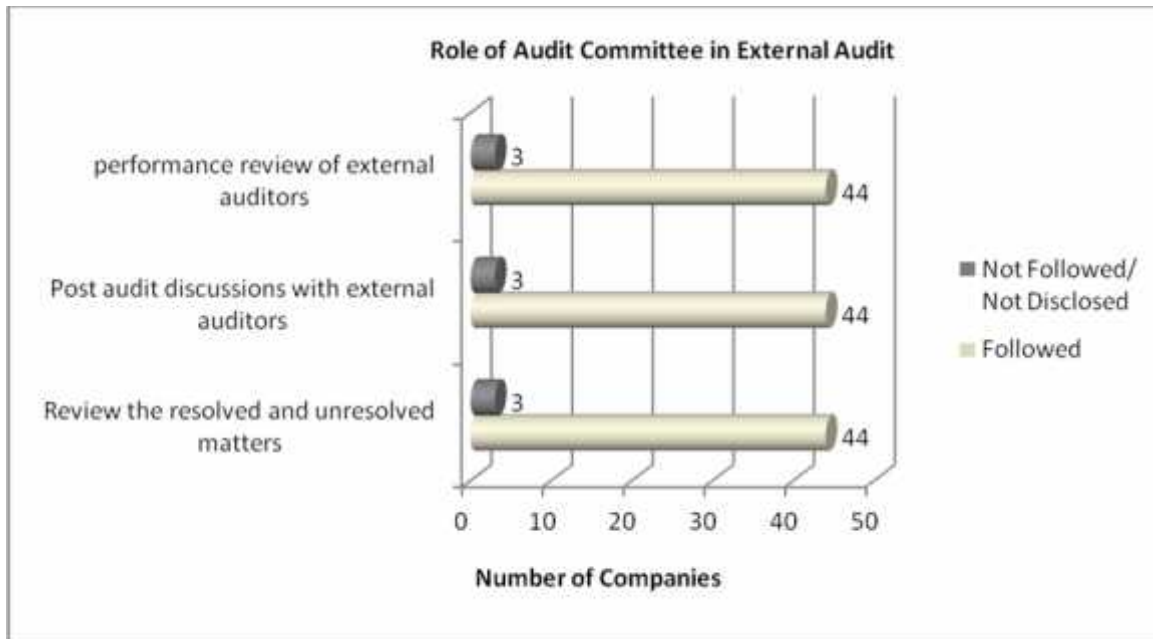


- b) **Role of audit committee in internal audit:** 45 companies provided the information on compliance of provisions on role played by audit committee in internal audit. One important provision of internal audit is to review the whistle blower policy. But unfortunately only 27 companies have adopted whistle blower policy.

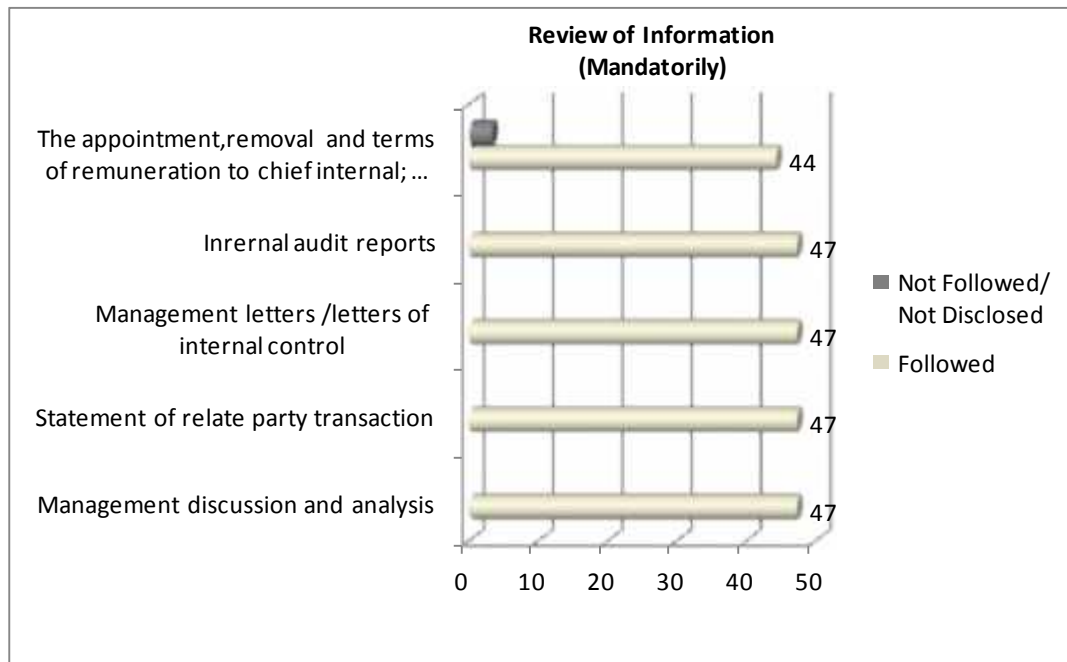




- c) **Role of audit committee in external audit:** From the analysis it was observed that 44 companies had provided proper information on role played by audit committee in external audit.



4. **Review of Information (Mandatorily):** As per clause 49, audit committee shall review important information (details are given in table1.). In all the companies, statements were reviewed by audit committee and proper information had been disclosed by companies in annual reports. One statement of review of appointment, removal, terms of remuneration of chief internal auditor, information was not provided by three companies.





Summary Table

Based on the(Year 2012-13) Annual Reports of NIFTY 50 companies

		Followed as per provision	Not followed/ Not disclosed
1	COMPOSITION OF AUDIT COMMITTEE		
1a	QUALIFIED AND INDEPENDENT COMMITTEE		
	Members in committee	47	
	Qualification	47	
	Chairman to be independent director	47	
	Chairman to be present at AGM	47	
	Company sec act as sec to audit com	45	2
2	MEETINGS		
	No. of meetings in a year	47	
	Quorum	47	
3	ROLE OF AUDIT COMMITTEE		
3a	ROLE IN INTERNAL CONTROL SYSTEM		
	Oversight the financial reporting process	47	
	Recommendation to board regarding appointment ,removal of statutory audit	46	1
	Reviewing with management the annual and quarterly fin statements	47	
	Reviewing with management statement of uses/application of funds	47	
	Reviewing the performance of internal auditors	47	
	Review the adequacy of internal control system	47	
3b	ROLE OF AUDIT COMMITTEE IN INTERNAL AUDIT		
	Review the adequacy of internal audit plan	45	2
	Review the frequency of internal audit	45	2
	Discussions with internal auditors with regard to findings and follow up	45	2
	Review the findings of internal investigations	45	2
	Review the functioning of whistle blower policy (if existing)	27	20
3c	ROLE OF AUDIT COMMITTEE IN EXTERNAL AUDIT		
	Review the resolved and unresolved matters	44	3
	Post audit discussions with external auditors	44	3
	Performance review of external auditors	44	3
4	REVIEW OF INFORMATION (MANDATORILY)		
	Management discussion and analysis	47	
	Statement of related party transaction	47	
	Management letters / letters of internal control	47	
	Internal audit reports	47	
	The appointment, removal and terms of remuneration to chief internal auditor	44	3



CONCLUSION

After the detailed analysis of Nifty 50 companies, it has been concluded that audit committees are ensuring the high level of transparency in all the areas concerned with role played in internal audit, external audit and reviewing the financial statements. Most of the companies are complying with the provisions of clause 49 of audit committees. Some organizations like Infosys and HDFC bank have adopted the audit committee charter. In the triad of relationship among external auditors, internal auditors and the Boards, audit committee is playing a critical role which ensures good Corporate Governance. But it is suggested that SEBI should take timely reviews of work audit committees which will lead better transparency, fairness and reliability.

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