19th October 2020

To
Shri Rajesh Verma, IAS
Secretary
Ministry of Corporate Affairs
Government of India
Shastri Bhawan
Dr. Rajendra Prasad Road
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Respected Sir,

Sub: Representation for making joint audit mandatory for certain class of Companies

ABOUT C.V.O. CHARTERED & COST ACCOUNTANTS' ASSOCIATION (CVOCA)

C.V.O. Chartered and Cost Accountants' Association is a four decade old, non-profit professional organization established in 1973. It has acclaimed a premier position in society. Its objective is to disseminate knowledge in the field of Taxation, Accounting, Finance and Allied laws. It has membership strength of more than 1850 members. Members of the Association have acclaimed respectable position in the CA practice and industry where they serve. It also organizes general public awareness program. One of the flagship programs is on Union Budget, which is organized in Gujarati Language for general public. The Association also publishes monthly Newsletter which is called 'CVO CA News & Views'. Besides these activities Association also supports students who are pursuing CA, CS & CWA by providing them financial assistance in the form of scholarships and interest free loans.

BACKGROUND AND REPRESENTATION:

The Ministry of Corporate Affairs came out with a consultation paper in February 2020 seeking comments on how to improve audit quality where one issue is on joint audit. We understand a committee has been set up to discuss the feedback received on the Consultation paper. We strongly believe that mandatory Joint Audit for large Companies is essential to improve Independence & audit quality in this challenging macro-economic environment.

The Hon'ble Prime Minister of India Shri Narendra Modi during his address at an ICAI program on 1st July 2017, has shared the dream that India should develop indigenous large audit firms. Providing for joint audit would lead to an increase in competition. The choice in the audit market is one of the ways to build better capabilities and improve quality naturally.

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In the UK, the Competition and Markets Authority (CMA) has proposed that the 350 largest listed companies either appoint joint auditors, with one being a challenger firm (non-big 4 firm) or appoint a challenger firm as their sole auditor. The objective is to enable challenger firms to expand their capabilities and scale to compete more effectively with Big Four firms. Similarly in France, too joint auditors are mandated for larger listed Companies Audit[1]. Shared and joint audits in India have declined as audit firms which are part of the largest international networks making it businesses opt only for a single audit firm globally

A professional accountant is required to comply with the fundamental principles as issued by the Institute of Chartered Accountants of India (ICAI). These fundamental principles are issued as per the guidelines issued by the International Federation of Accountants of which ICAI is a member. One of the fundamental principles is that of independence and objectivity. Appointment of Joint auditor reinforces these principles. It reduces the risk of over-familiarity through rotating the allocation of fieldwork between the joint auditors after a set number of years. The joint auditor reiterates the principle of "four-eyes". It brings a critical eye on the respective work of each auditor. Audit client enjoys a larger spectrum of skills from more than one firm at the same time. There is also a richer discussion on complex issues. During sequenced rotation, the client would experience limited disruption. Further, it provides scope for comparison of services level which would untimely lead to better service quality. It will also lead to better Corporate Governance.

The empirical findings suggest that companies opting to employ joint audits have a higher degree of earnings conservatism, lower abnormal accruals, better credit ratings and lower perceived risk of becoming insolvent within the next year than other firms. The study concludes the view that joint audits are positively associated with audit quality in a relatively low litigious setting both for public and private firms[2].

Beside UK, France various countries in European Union like Belgium, and in Africa joint Audits are mandated for companies in the financial services sector.

The Auditing standard similar to NEP-100 as introduced in France can set out high-level requirements for balance in the allocation of work, for each auditor to make an assessment of audit risks and the control environment, and to perform critical reviews of the work performed by the other firm.

The Companies Act, 2013 vide section 139(3) permits audit to be conducted by more than one auditor. Though Companies Act does not mandate application of joint audit, corporate houses like Reliance, Birla's, etc. as a practice engage joint auditors in their various entities. All large PSUs like ONGC, Indian Oil, NTPC, etc. have joint audit arrangements. Till about a decade or so ago even the House of Tata's had joint auditors in almost all its large entities for many decades. 'Joint Audit' as a concept has been widely prevalent in India for more than 50 years.

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[1] ICAEW thought leadership - Future of Audit
[2] https://doi.org/10.1080/09638180.2012.678599

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Corporate Governance Guidelines issued by the IRDAI, with certain exceptions, also requires insurance companies to have minimum two auditors as joint auditors. The guidelines further require that a joint auditor of an insurer shall not include another associate/ affiliate firms which are under the same network or whose name or trademark or brand is used by the firm or any of the partners of the other joint auditor.

The public sector banks also adopt a joint audit model. These banks appoint more than one auditor as the central statutory auditors depending upon the size and nature of the banks apart from hundreds of branch auditors. Even, some of the private banks have a practice of joint audits.

During 2018, a press note issued by the Department of Industrial Policy & Promotion (Ministry of Commerce & Industry) on review of Foreign Direct Investment (FDI) policy on various sector introduced prohibition of restrictive conditions regarding audit firm.

Standard on Auditing 299 issued by the ICAI, lays down the principles for the effective conduct of joint audit to achieve the overall objectives of the auditor and deals with the special considerations in carrying out the audit by joint auditors. It tries to provide a uniform approach to the process of joint audit.

It is expected that the joint audit would enable

- Countering collusion and providing more ammunition to tackle management.
- Make the market less monopolistic
- Stop giving a false perception about lack of options and A false sense of too big to fail
- Stimulate innovation, awareness, and due care through rotating fieldwork.
- An increased spectrum of skills and critical thinking.
- Comparison of service levels between the firms and also knowledge sharing driving up the service quality.
- Companies to benefit from the technical expertise of more than one audit firm and to have a richer discussion on complex technical issues.
- Reducing the risk of over-familiarity
- Reducing the time of completion of audits

The biggest criticisms against a joint audit are potentially high cost. However, this is not founded on statistics. Technically, this should not be so, as auditors split the total responsibility and audit are opened up to market forces rather than a small group of firms.

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In the UK, the Competition and Markets Authority has suggested that the additional costs (if any) incurred by listed companies could be offset by a lower cost of capital because investors would have higher levels of confidence in the audited financial statements.

We in India should be evaluating ideas on Audit & Accounting independently by keeping ground reality and national interest in mind. We should as a country do everything to make the Indian Audit Profession '**Atmanirbhar**'

Also, there is no empirical data or research carried out so far in India to prove that joint audits are costlier or result in more effort and lower quality. It's a fear-induced by Vested Interests not wanting Joint Audits.

The joint audit would enable a smooth and sequenced rotation of audit firms which minimises disruption to the client by harmoniously transferring knowledge and understanding of the company's operations and culture.

The joint audit would also encourage healthy dialogue between the two or more audit firms appointed bringing a critical eye on the respective work of each auditor.

Further, during the current period we have observed a lot of resignation of auditors on various reasons. If the Company is having joint auditors, the situation of the resignation of one of the auditors may not result in much disturbance for the Company.

The French experience showcases joint audit as a proven mechanism in enabling new entrants into the audit market and Stimulates competition between a greater number of audit firms from different cultural backgrounds, resulting in more innovation and better response to market needs.

Through the introduction of joint audit, even the small and medium-sized would get an opportunity there to enhance the skill sets.

The Indian PSU's practice of joint audit has enabled mid-tier firms to participate in the niche sectors like Oil & Gas sector, Nuclear sector etc., thus creating a talent pool which can / does mitigate the risk of audit concentration amongst a few firms

Joint audit thus does offer benefits in terms of Macro-economic policy, Independence and Quality and can lead to an increase in the effectiveness of the audit. Besides, keeping the audit market healthy, less dependent on a few firms and less polarised is critical for the national interest as audit firms effectively sign off on financial health card of every business in India. More specifically, developing local firms by creating opportunities for them is important in the long term.

The Ministry in the consultation paper cited that joint audit would encourage more competition between audit firms and envisioned Big Four then becomes the best seven or eight, as more firms are given the opportunity to demonstrate their capabilities.

CONCLUSION

Joint audits are not a ready remedy and would require sustained investment of regulatory time and efforts. Implementation of joint audit might be a challenging one, but it is the need of the hour. The lawmakers should put their foot forward making joint audit applicable to large companies, for example Companies having turnover more than INR 750 crores or having borrowings more than INR 500 crores.

Accordingly, we request you to consider it to making joint audit mandatory for certain class of companies in the interest of improving Corporate Governance, improve independence and audit quality and developing the Audit Profession.

Thanking you,

Yours sincerely,

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