

Even with all their 'ifs', 'buts' and 'wherefores', and with disclaimers that sometimes amount to self-preservation, auditors, through their reports, provide significant insights to stakeholders. What happens if they opt for 'flight' rather than 'fight'? Is there a way out of this imbroglio? The stakeholders want to know.

Editor

AUDITORS' DILEMMA – TO SIGN OR TO RESIGN?



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The spate of resignation by auditors has been perceived by some as the last nail in the coffin of Corporate Governance. The cynics who continuously look for evidence that Corporate Governance is dying, if not dead, are anxiously awaiting more resignations. Having long subscribed to the view that the biggest are necessarily the best governed, the apologists for the corporates that held themselves out as the shining examples of governance in India, are now feeling vindicated when auditors in smaller companies are opting out of their assignments.

An auditor in a corporate entity is one of the custodians of the faith and trust of the multitude of stakeholders. It is on account of the comfort, that an investor draws from the certification of the accounts as giving a fair and correct picture, that he/she stays invested in the company. When auditors throw up their hands or walk away, investor confidence suffers a mortal blow and share prices ordinarily experience a very steep fall.

Attributing the phenomena of increasing auditor resignations to any one reason would amount to oversimplification. There are those that believe that regulatory action, against the auditors in the case of a major corporate fraud, has induced a sense of fright in the auditing profession. There are others who subscribe to the view that the coming into being of National Financial Reporting Authority (NFRA), a statutory body with disciplinary powers, might have been the trigger for some resignations since the comfort of self-regulation by a membership body has got circumscribed by the higher powers vested in the NFRA. The fear of being arraigned in class action suits is yet another possible reason for the exit of auditors.

While the reasons may be many and varied, what ought to engage stakeholders as well as students of Corporate Governance is the question whether the auditors are doing the right thing by exiting either before the completion of the audit or immediately thereafter. Put differently, is exit the only option for an auditor unable to discharge his/her functions because of non-cooperation by the auditee or for other reasons? Is there an element of abdication of responsibility having regard to the fact that an auditor's exit leaves a vacuum which cannot be immediately filled, and consequently causes considerable disquiet in the minds of stakeholders?

The more common reason cited by exiting auditors is that the information they have sought, in the course of audit, has not been made available to them. It is entirely possible that managements withhold information which, if taken into account by auditors, could lead to non-certification of accounts as presenting a true and fair picture. Should information be withheld or delayed, there are options other than exit available to the auditor. It is open to the auditor to approach the Audit Committee (AC) at any point of time, and not only when the quarterly meetings take place, to bring to the committee's notice that complete and correct information is not being made available by the management. In fact, in most companies, that practice high standards of Corporate Governance, and where the auditor has interactions with the AC in the absence of management, one common question put by the committee to the auditors is whether the information flow is timely and comprehensive. For an auditor to not avail this opportunity is to act in a manner inconsistent with the expectations from that high office.

Auditors also have the unfettered right to qualify accounts if they believe that the position taken by the management in regard to some matters is inconsistent either with the facts or with the accounting policies that are

followed. The purpose of the qualification is to put stakeholders on notice that the results indicated by the management should not be fully relied on to make investment decisions. Since qualifications in the accounts place the corporates at a severe disadvantage vis-à-vis the stakeholders and also the regulators, it is unlikely that managements will refuse to fall in line if the auditor signals the possibility of a disqualification.

Yet another option available to the auditors, especially when fraud is suspected, is to alert the Board and the Registrar of Companies (ROC). More often than not, it is fraudulent action on the part of the management that stands in the way of their sharing complete information with the auditors. In such a situation, it is incumbent on the auditors to assess whether a fraud has taken place or is suspected, and to alert the Board to such a possibility.

Notwithstanding every alternative that is available, it is possible that the circumstances are so adverse as to not leave the auditor with any option but to quit. In such a situation, it must be made mandatory for the auditor to disclose, in sufficient detail, the reason for resignation and steps taken by the auditor to address the matters that finally precipitated his/her resignation. If for example, auditor has been denied information, the resignation letter should indicate, in sufficient detail, the efforts made by the auditor, including approaching the AC, and the auditor's assessment as to why information is being withheld. In doing so, the auditor's position would be considerably strengthened by the fact that Independent Directors (IDs) are also expected to ensure the timeliness and adequacy of information flowing to the Boards. Making common cause with IDs in pursuit of the objective of ensuring that the accounts reflect the correct position of the company is an approach that auditors should always embrace. A resignation letter by the auditor indicating detailed reasons for resignation should ordinarily trigger a regulatory enquiry to ferret out the truth. One possible safeguard against hasty resignations could be a requirement for the exiting auditor to appear before the shareholders at the next Annual General Meeting (AGM) and to personally indicate to them the reasons for resignation. Since they are appointees of shareholders, this alone can bring their assignment to a legitimate conclusion.

To sign or to resign seems to be the auditors' dilemma. The way out is simple. When the going gets tough, the tough get going. They don't leave.

Some of the above points emerged at our by-invitation roundtable on the topic.

READERSPEAK (in alphabetical order) – BRAKING VIEWS

"Anami Roy, Former Director General of Police, Maharashtra"

"Simply outstanding! So true and hilarious too. Love the cookies and nuts (the edible variety...) bit. But seriously an occasion for IDs to have a fresh hard look at things."

"Anupam Puri, Formerly of Mc Kinsey & Co"

"Bravo! This is really, really good, and needless to say, very funny as well."

"Apurva Purohit, President, Jagran Prakashan"

"What an excellent missive – Extremely valid points with dollops of wit and lashings of irony! My favourite type of communication!"

"PM Kumar, Former Business Chairman and Board Member, GMR Group"

"Hard hitting and so real – the Emperor wears no clothes – PG Wodehouse plus plus!!"

"TV Mohandas Pai, Chairman, Manipal Global Education"

"Very nice, very relevant."

"Vinita Bali, former Managing Director, Britannia Industries"

"Masterpiece!"

"V Sumantran, Former Vice Chairman, Hinduja Automotive and Ashok Leyland"

"Thank you for this exquisite piece of prose. This one combining everything from Englebert Humperdinck to cricket to Sir Humphrey Appleby (?) is one more piece to treasure."

Do let us know of any specific issues you would like to see addressed in subsequent issues.

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