

ICAI-NFRA Clash Should Trigger Holistic Reforms to Spot Corporate Frauds

SEPTEMBER 21, 2021

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TWO

statutory bodies, National Financial Reporting Authority (NFRA) & the Institute of Chartered Accountants of India (ICAI), have again made news for a wrong reason.

The other day a business daily ran a story headlined: '**CA Institute lashes out at NFRA over TAC report**'. As put by the story, **"It's official. Two audit regulators - ICAI and NFRA - are daggers drawn, and in public too, with the CA Institute rejecting outright the Technical Advisory Committee (TAC) report of March 2021"**.

The story is obviously based on two documents released a few days back: 1) NFRA Conclusions on Questions Posed in Consultation Paper (CP) based on Report of the TAC on Enhancing Engagement with Stakeholders and 2) Public (ICAI included) comments on CP.

NFRA-ICAI showdown is deplorable. It is obviously due to the Government's inability to create an effective system to keep a hawkish watch on quality of audit of corporate finances. The inability has ensured the system fails time and again in nipping in bud the corporate frauds. The auditors are often found deficient in such cases. So are the governments and their appendages.

It is thus unfair to single out auditors/chartered accountants (CAs) for public bashing as has been done by NFRA and its parent ministry, Ministry of Corporate Affairs. Blame-game is not the solution to any problem.

The solution lies in implementing holistic reforms after consulting all stakeholders. All stakeholders should accept their respective share of contribution to corporate and banking frauds that have recurred over many decades. The eroding public confidence in economic governance must be restored to create healthy environment.

NFRA is still in its infancy and this was its first CP. It did not discuss CP with NFRA board that includes three top-notch representatives of ICAI. Had it done that, ICAI would perhaps have not penned down its strong comments on CP.

In its exhaustive comments submitted in July 2021, ICAI pointed out that the both NFRA and ICAI have to work for common public good and not as competing entities. The covering letter says:

"It has been that rather non-collaborative approach is being adopted by NFRA and the way in which TAC report and consultation paper is worded, wherein NFRA has also given its preliminary view in the said report, it seems that NFRA feels that for so many years there was no regulator for accounting and auditing profession".

The letter, signed by ICAI President, cautions NFRA to not act as super regulator of auditing profession. It adds:

"this damaging report is surely believed to harm the image of the CA profession. The Report may also harm the national interest due to change in investment rating and other parameters taken in consideration by World Bank in preparing Ease of Doing Business Report".

Like NFRA, MCA had issued a CP on Enhancing Audit Independence and Accountability during February 2018. It pitched for requisite amendments to relevant laws.

Does MCA believe that creation of NFRA won't prevent or at least minimise corporate frauds? The Government formed NFRA in October 2018 through amendment to Companies Act after prolong efforts by ICAI to convince it to abort this idea of independent monitoring of auditors.

Instead of creating NFRA, the Government should have carved out Quality Review Board (QRB) from ICAI into a separate statutory authority. This would have prevented scope for NFRA-ICAI clash over assessing quality of audit and fixing accountability of CAs.

In March 2018, Cabinet clipped wings of Govt-controlled QRB while approving formation of NFRA. It decided that NFRA's jurisdiction to probe CAs would extend to their audit of listed companies and large unlisted public companies, the thresholds for which shall be prescribed in the rules under the Companies Act.

The Cabinet also decided that ICAI's QRB will also continue to conduct quality audit in respect of private limited companies, public unlisted companies below prescribed threshold and also with respect to audit of those companies that may be delegated to QRB by NFRA. Further, ICAI shall continue to play its advisory role with respect to accounting and auditing standards and policies by making its recommendations to NFRA. Later, MCA notified rules demarcating the responsibilities of NFRA and QRB.

No wonder that several stakeholders in the comments on NFRA's CP have demanded clarity of overlapping role of regulators. It is here pertinent to note that audit deficiencies are also unearthed by MCA's Serious Fraud Investigation Office (SFIO) in its investigative reports. Not a single report is, however, available in public domain. This means cover-up of frauds process.

SFIO should learn from NFRA which last month made public its Audit Quality Review (AQR) report on Jaiprakash Associates Limited. We hope it would make public AQR reports on other companies too. QRB should also make public its reports on companies where audit deficiencies were noticed. So should RBI.

Such disclosures would empower investors, consumers and other stakeholders to look for audit cover-up in annual reports of other companies. If the Government is indeed sincere about preventing frauds, then it should make it mandatory for all companies, trusts and other NGOs to make public their annual reports that incorporate audited accounts. Disclosure itself acts as a deterrent against future frauds.

Coming to MCA's CP, it stated:

"Recently various instances of failure of auditors have been noticed such as IL&FS case etc., and it is also seen that the quality of audit reports have been compromised. In most of the cases the auditor appears to be hand in glove with the management and therefore the question on their independence and accountability have been arisen. In order to pluck the aforesaid scenarios/instances, the Ministry is of the view that the existing regulatory provisions relating to Audit and Auditors in Companies Act, 2013 and its Rules along with Standard of Auditing need to be reviewed".

MCA should finalize amendments to relevant laws based on feedback it got on its CP. Simultaneously, it should allow NFRA to adequately equip itself with trained manpower. It should be exempted from usual practice of government organisations hiring **ad hoc** staff on deputation or transfer basis from other similar entities.

It must create a separate portal on which companies of all sorts should be asked to upload their annual reports. This would be a big leap towards preventing and detecting discrepancies in corporate world.