Why are auditors silent?

POWERPOINT

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Auditors seem to be finally taking their role seriously. Look at their new-found aggression: According to data provided by Prime Database, in just five months of this calendar year, as many as 32 firms have resigned as auditors of companies mid-term. The number in the past one month alone was 15. That's a big change from the numbers in the earlier years.

In the past couple of weeks, three companies saw their auditors resign abruptly just ahead of the quarterly results. While Deloitte quit Manpasand Beverages, Price Waterhouse (PW) resigned from Atlanta and Vakrangee within days of each other. The reason for the decision was almost identical: The failure of managements in providing adequate relevant information on time. Shares of all these companies have since then taken a huge hit, reflecting the nervousness of investors. Since April 27, the day PW stopped Vakrangee's auditing job, the stock price has lost more than two-thirds of its value. The Manpasand stock is down more than half since Deloitte resigned.

While auditors have come in for a lot of praise for their proactive stand against what they perceive to be dodgy practices followed by companies, there is still a long way to go. Consider the poor disclosure of information by the auditors. While PW has cared to give some details about its concerns related to Vakrangee's bullion and jewellery businesses, Deloitte has shared nothing except a brief statement saying the company did not give "significant information" relating to some of its businesses. This is strange as the auditors have taken the extreme step of resigning and are duty-bound to give detailed explanation to shareholders about the exact reasons.

What makes it even more intriguing is that Deloitte has been the auditors for Manpasand for several years and none of its previous reports came with any qualification. That's all the more reason for Deloitte to come out in the open about what went wrong suddenly. After all, shareholders have lost money and can't be kept clueless about the circumstances under which the auditors have resigned. Besides, the incoming auditor ought to know the nature of the information that was withheld by the company. Detailed disclosure is nothing but good governance.

The excuse of client-confidentiality and code of conduct does not wash, as auditors are required to give detailed information under the revised Companies Act. It's true that the Institute of Chartered Accountants of India does not yet have a framework for such information (it needs to take a hard look at this aspect), but that can hardly be a shield for auditors from withholding material information.

The response from the companies is equally strange. Manpasand, for example, lost the auditor it had since it did an initial public offer in 2015, and yet it described the event as a "minor hiccup". It also flatly denied all the charges in its brief statement. Vakrangee was no better. Terming the resignation of its auditor as an "old event" in its response to the stock exchanges, the company merely said it is fully compliant with the Ind-AS accounting standards and that its statements present the true and fair view of the state of the affairs of the company. There was not a word on the specific charges made by the auditor.

It's clear from the responses that the boards of both the companies have taken a serious matter like auditor resignation lightly, reflecting poor corporate governance. This is completely against the spirit of the Companies Act and the October 2017 report of the Uday Kotak-led committee on corporate governance, which has been accepted by Sebi. The committee said, "For the sake of greater transparency, the committee believes it is important for companies to disclose the reasons for the resignation of its audit firm. Moreover, audit firms, too, must be encouraged to truthfully disclose the reasons."

It's good that the auditing community is trying hard to shake off the reputation issues it faced ever since the Satyam issue emerged. The biggest push to their change of approach came from the prime minister (PM) who, at an ICAI meeting, asked why it took the institute years to take punitive action when 1,400-plus cases were pending against auditors who helped tax evaders. The PM's statement followed the revised Companies Act, which imposed bigger liabilities on errant auditors; the Sebi action against PW in the Satyam case and the Cabinet green signal to the proposal to set up the National Financial Reporting Authority (NFRA), intended to serve as an independent regulator for the auditing profession. The Companies Act also now allows for class-action suits, and there is greater scrutiny from the Reserve Bank of India, following a spate of bad loans.

Whatever be the reasons, now that auditors have taken the first step, it may not be a bad idea to take care of the disclosure requirements as well. After all, ordinary shareholders should not be at the receiving end — always.