

# Hazy disclosures, vague reasons: how auditor exits continue to play with investor confidence

**ET** [economictimes.indiatimes.com/prime/corporate-governance/hazy-disclosures-vague-reasons-how-auditor-exits-continue-to-play-with-investor-confidence/primearticleshow/78858518.cms](https://economictimes.indiatimes.com/prime/corporate-governance/hazy-disclosures-vague-reasons-how-auditor-exits-continue-to-play-with-investor-confidence/primearticleshow/78858518.cms)





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Concept by Muhabit ul haq

## Synopsis

**Nearly three dozen listed companies have seen auditor resignations this year. One of those cases, the UPL fiasco, highlights how patchy and insufficient disclosures on such departures spring nasty surprises on the market. While Sebi tried to plug this with a set of norms on mid-term cessations in October 2019, not everyone is sticking to them.**

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The shares of UPL (formerly United Phosphorus), were in for a beating earlier this month after the crop-solutions company said an affiliate of KPMG has pulled out of audit of a key Mauritius-based subsidiary. Quick clarifications from the management followed, but the heat on the stock continued.

Unlike 2019, audit resignations have not made much of a splash this year. However, a closer look at the month-wise data shows premature cessations have continued steadily throughout 2020 – peaking in August, just before the deadline for finalising annual accounts.

Nearly three dozen listed companies have seen auditor resignations this year, with 11 by audit firms affiliated to the Big Four – KPMG, EY, Deloitte, and PwC. In comparison, over 60 companies in 2019 reported their auditors' resignations before their term got over.

Since auditors did not share the exact reasons for their exits, or often gave vague reasons, investors were in the dark. This helped speculators and bear cartels spread rumours. Sometimes, investors were in for crude surprises. Manpasand Beverages, where large-scale irregularities were unearthed, is a case in point

In October 2019, market regulator Securities and Exchange Board of India (Sebi) decided to step in. In a circular, detailing disclosure requirements, Sebi said, “Resignation of an auditor of a listed entity/its material subsidiary before completion of the audit of the financial results for the year due to reasons such as pre-occupation may seriously hamper investor confidence and deny them access to reliable information for taking timely investment decisions.”

Apart from mandating the auditor to provide limited reviews of the accounts before resigning, the regulator also prescribed a format for resignations of auditors of listed companies and their material subsidiaries.

While these measures seem to have helped reduce the uncertainty and speculation around auditor resignations, the odd surprise has not ceased to pop up.

### **Reconstructing the UPL fiasco**

ET Prime went through the sequence of events in UPL – from its exchange filings to subsequent statements in the public domain.

On October 15, the shares of UPL closed at INR506.45. A few hours after the markets closed, a little past 8pm, UPL communicated to the exchanges: “This is to inform you that the company has received the attached communication dated October 14, 2020, from UPL Corporation Limited, Mauritius, a material subsidiary of the company. As per the said communication, M/s. KPMG, Mauritius has resigned as the auditor of UPL Corporation Limited w.e.f. October 8, 2020.”

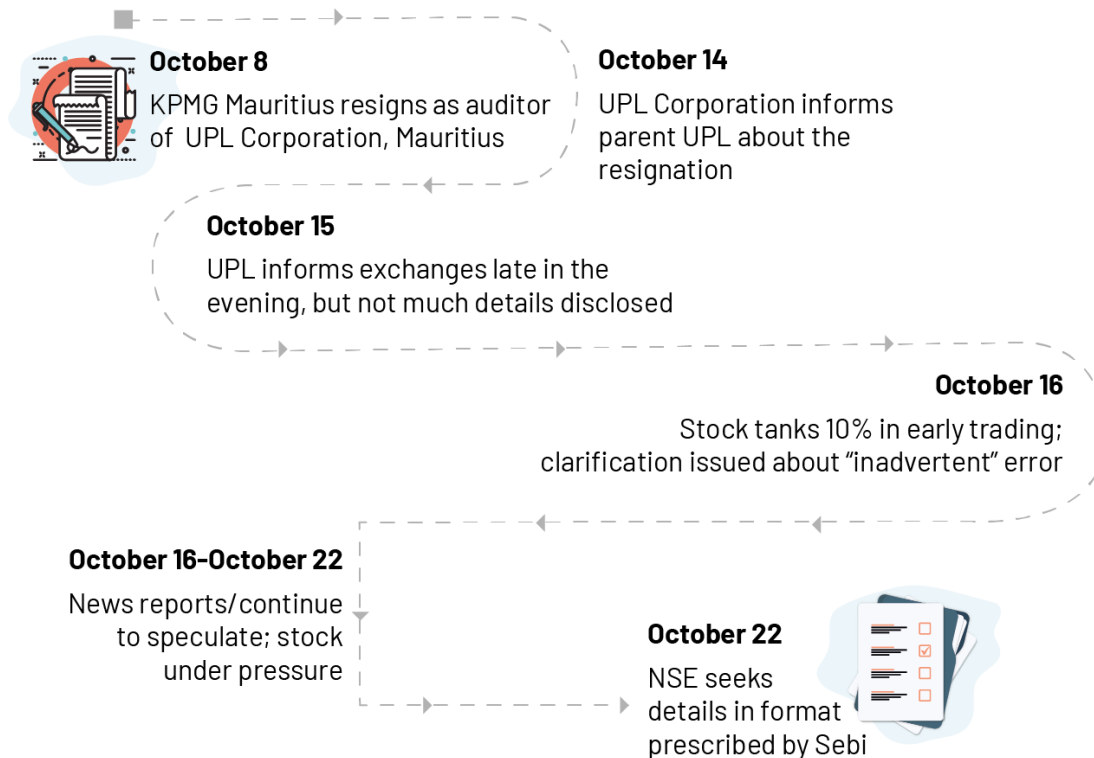
The letter from Port Louis, Mauritius-based UPL Corporation was not very detailed. It only said: “We wish to inform you that KPMG, Mauritius has resigned as auditors of UPL Corporation Limited, effective from October 8, 2020. Kindly find enclosed a copy of the resignation letter for your records.”

However, the letter from the auditor itself was not part of the communication to the exchanges.

With very little information to understand the nature of this resignation, traders pressed the sell button as markets opened on Friday (October 16), dragging the prices of UPL shares to INR458 on the BSE. Over 250 million shares changed hands that day.

Remember, it is this very lack of information Sebi sought to address with its 2019 circular. But, the letter and spirit of the circular was spectacularly flouted just before its first anniversary.

## UPL fiasco timeline



Source: Exchanges

 ETPrime

To control the damage, UPL group CEO Jai Shroff appeared on a business news channel. "We have asked KPMG to resign in Mauritius," he said in an [interview](#) with CNBC-TV18. "It remains our global auditors, including India."

"After the acquisition of Arysta, the workload in Mauritius went up substantially, and Mauritius being a small office of KPMG, and run out of South Africa, we could never close our accounts on time because appropriate resources were not available in Mauritius to close our accounts for more than 100 subsidiaries," said Shroff.

However, it was too little too late.

Around 1.30pm that day, the company sent a notification titled "Clarification statement - auditors of UPL Corporation Limited, Mauritius". It said, "In order to reorganise the audit process to improve productivity, at the request of the company, KPMG Mauritius has resigned as statutory auditors of UPL Corporation Limited, Mauritius. M/s. BSR & Co. LLP, Chartered Accountants continues to carry out the audit of group consolidated financials of UPL Ltd, India, which includes [UPL Corporation Ltd](#), Mauritius, and its subsidiaries."

It also said it was attaching the resignation letter of the auditor which was

“inadvertently not enclosed”.

The letter from the auditor again said little and was not in the prescribed format. “We hereby submit our resignation as auditors of UPL Corporation Limited with immediate effect. There are no circumstances connected with our resignation which we consider should be brought to the notice of the members.”

Annexure A of the 2019 circular requires the auditor to disclose several details, including the detailed reasons, whether any information was not forthcoming, details thereof, etc.

The circular made it clear it was the obligation of the listed entity to get the information.

“Upon resignation, the listed entity/its material subsidiary shall obtain information from the auditor in the format as specified in Annexure A to this circular. The listed entity shall ensure disclosure of the same under sub-clause (7A) of clause A in part A of schedule III under Regulation 30(2) of Sebi LODR Regulations,” the circular said.

This clearly was not followed in the UPL case. Even worse, the resignation letter was signed off as ‘KPMG’ and not by a partner or an authorised signatory, as is normally the case.

## What KPMG gave...



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UPL CORPORATION LIMITED  
5<sup>th</sup> Floor Newport Building  
Louis Pasteur Street  
Port Louis  
Republic of Mauritius

Our ref IAAHA/sp/2395

Attention: Board of Directors

08 October 2020

Dear Sirs

**Resignation as auditors**

We hereby submit our resignation as auditors of UPL CORPORATION LIMITED with immediate effect.

There are no circumstances connected with our resignation which we consider should be brought to the notice of the members.

Yours faithfully

  
KPMG

## ...what Sebi wanted



Annexure A

Format of information to be obtained from the statutory auditor upon resignation

- Name of the listed entity/ material subsidiary;
- Details of the statutory auditor:
  - Name;
  - Address;
  - Phone number;
  - Email;
- Details of association with the listed entity/ material subsidiary:
  - Date on which the statutory auditor was appointed;
  - Date on which the term of the statutory auditor was scheduled to expire;
  - Prior to resignation, the latest audit report/limited review report submitted by the auditor and date of its submission.
- Detailed reasons for resignation;
- In case of any concerns, efforts made by the auditor prior to resignation (including approaching the Audit Committee/Board of Directors along with the date of communication made to the Audit Committee/Board of Directors)
- In case the information requested by the auditor was not provided, then following shall be disclosed:
  - Whether the inability to obtain sufficient appropriate audit evidence was due to a management-imposed limitation or circumstances beyond the control of the management.
  - Whether the lack of information would have significant impact on the financial statements/results.
  - Whether the auditor has performed alternative procedures to obtain appropriate evidence for the purposes of audit/limited review as laid down in SA 705 (Revised)
  - Whether the lack of information was prevalent in the previous reported financial statements/results. If yes, on what basis the previous audit/limited review reports were issued.
- Any other facts relevant to the resignation;

### Declaration

- If We hereby confirm that the information given in this letter and its attachments is correct and complete.
- If We hereby confirm that there is no other material reason other than those provided above for my resignation/ resignation of my firm.

Signature of the authorized signatory

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While Shroff himself said in the TV interview that it was going back to the previous auditor, a news report even said quoting a brokerage analyst that the audit mandate has passed on from KPMG Mauritius to KPMG Global. But, with the company not having said this in any official communication, investors could not be sure what to believe.

On October 22, a week after the debacle, NSE asked the company to give details of auditors as required by the Sebi circular.

A KPMG spokesperson directed queries to KPMG Mauritius and UPL. KPMG Mauritius is yet to respond to the request for comments.

A UPL spokesperson did not answer specific queries raised by ET Prime on why the disclosures were not in the required format and details of the new auditor. “The company, with its responses, has filed its statements to the stock exchanges. Also, S&P, a credit rating agency, published a bulletin on the same matter. The said documents address all your queries,” the spokesperson said in an e-mail response.

She also forwarded a rating bulletin by S&P Global titled “UPL Corp’s change in auditor does not signal increased governance risk”, apart from the clarifications given to exchanges already mentioned earlier.

The S&P bulletin mentioned another name, Crowe ATA, as the new auditor. Though the bulletin played down governance concerns, its outlook was negative.

“Despite the change, UPL is on track to announce its second-quarter results for fiscal 2021 (year ending March 31, 2021) on October 30, 2020. Crowe ATA was the auditor of UPL before KPMG Mauritius got on board. We therefore expect the transition to be smooth, considering Crowe ATA's previous knowledge of UPL as well as the agrochemical industry,” the S&P Global bulletin said.

Curiously, Crowe ATA's name did not figure in any of UPL's official communication to the exchanges till October 23. Also, the S&P bulletin is not available to all investors, adding to the information asymmetry in the market.

In the bulletin, S&P’s Singapore-based analysts Shawn Park and Neel Gopalakrishnan said, “A sudden change in the auditor is generally perceived negatively by market participants and could dampen investor sentiment toward UPL and its governance. However, the company has confirmed that the change in auditor is unrelated to any accounting or operational issues at UPL. Any accounting implications post the change in auditor could be a credit factor. UPL’s liquidity is sound.

“The company raised funds through a bond issue in June 2020. It, therefore, has no immediate funding needs, and has time to re-establish confidence with investors.

“Our negative outlook on UPL reflects our view of a one-in-three likelihood that UPL Ltd.'s consolidated ratio of funds from operations to debt will not maintain its trajectory towards 25% by fiscal 2022, as it deleverages after the acquisition of Arysta Lifesciences Inc. in 2019. We expect the agricultural sector to remain resilient despite a slowdown in the global economy and trade. However, any indications that the deleveraging is not proceeding as expected would prompt us to review our view on the rating.”

While not everyone seems to have fumbled with disclosures around auditor resignation like UPL, data shows that the exchanges and Sebi need to monitor disclosures more closely.

"Sometimes, the managements want that the qualified items are minimal or they don't want them at all. These are issues that often lead to [auditor] resignations mid-term."

— S Ravi, former BSE chairman and managing partner at Ravi, Rajan & Co.

### “Preoccupation” and “commercial” reasons

An analysis of data from Prime Infobase show that of the 33 cases of mid-term resignations reported in 2020, the top reason turned out to be “commercial”, with nine instances, followed by “preoccupation” at eight. Alignment with group companies/subsidiaries (3), disqualification (2), merger (2), conflict of interest (1), and demise (1) were among other reasons cited by auditors for their resignations.

## Auditors mid-term cessations from NSE-listed companies

From January 1, 2020 to October 20, 2020

KPMG
  PwC
  EY
  Deloitte

Date	Company	Auditors Name	Cessation Reason
<b>■ September-2020</b>			
28	Jet Airways (India)	D T S & Associates	Commercial
16	Advani Hotels & Resorts (India)	Amar Bafna & Associates	Restructuring/merger
16	Alok Industries	N B S & Co	Resolution plan
16	Alok Industries	Shah Gupta & Co	Resolution plan
14	Gufic Biosciences	S H R & Co	Commercial
8	Euro Multivision	Rasesh Shah & Associates	Preoccupation
7	Zuari Global	Walker Chandio & Co LLP	Commercial
<b>■ August 2020</b>			
29	Kaushalya Infrastructure	Monu Jain & Company	Preoccupation

Development Corp.

14	Castex Technologies	Raj Gupta & Co	Preoccupation
14	Commercial Engineers & Body Builders Co.	B S R & Co LLP	Alignment with group /subsidiary auditors
14	Jmt Auto	Raj Gupta & Co	Preoccupation
14	Metalyt Forgings	Raj Gupta & Co	Preoccupation
14	Repro India	B S R & Co LLP	Commercial
14	Rollainers	Raj Gupta & Co	Preoccupation
13	GVK Power & Infrastructure	Price Waterhouse	Management non-cooperation
13	Intrasoft Technologies	Walker Chandio & Co LLP	Commercial
13	Nelco	Price Waterhouse	Preoccupation
12	Tribhovandas Bhimji Zaveri	S R B C & Co LLP	Commercial
11	Fairchem Speciality Co Chartered	Price Waterhouse & Accountants LLP	Alignment with group/ subsidiary auditors
10	Kama Holdings	Luthra & Luthra	Management non-cooperation
6	Dcm Nouvelle	B S R & Co LLP	Commercial
3	Coffee Day Enterprises	Sundaresha & Associates	Disqualification by ICAI
3	Integra Garments & Textiles	C S Chaubey & Co	Restructuring/merger
<b>■ July 2020</b>			
31	Windsor Machines	Niraj D Adatia & Associates	Commercial
24	Suumaya Lifestyle	Chahan Vora & Associates	No reason stated
17	Coffee Day Enterprises	B S R & Associates LLP	Commercial
17	Clariant Chemicals (India)	Price Waterhouse	Conflict of Interest
<b>■ May 2020</b>			
29	Equitas Holdings	S R Batliboi & Associates LLP	Alignment with group/ subsidiary auditors
<b>■ April 2020</b>			
1	Pae	R C Vakharia & Co	Demise
<b>■ March 2020</b>			
19	Sintex Plastics	Chanda Ram & Associates	Disqualified under Companies Act
14	Rpp Infra Projects	Sundaram & Narayanan	Preoccupation
10	Kshitij Polyline	R M Ajgaonkar & Associates	No reason stated
<b>■ February 2020</b>			
4	Digjam	Deloitte Haskins & Sells LLP	Management non-cooperation

Note: While companies may have different financial years/accounting periods, for standardisation purposes, an 'April-March' financial year has been considered for all companies.

Data for a company prior to its listing on NSE is not available.

Source: [primeinfobase.com](http://primeinfobase.com)

 ETPrime

Audit majors say the Covid-19 pandemic has messed up with cost structures, leading to



high number of cases of audit firms quitting due to “commercial reasons”.

A KPMG spokesperson, without referring to any specific case, says, “Given the changes in the business and regulatory environment, including due to Covid-19 and the new CARO (Companies Auditor's Report Order) 2020, auditors need to perform enhanced procedures in many areas.”

According to him, this has resulted in an increase in audit efforts and costs. While most companies appreciate this, and have agreed to increased audit fees, some companies may not be in a position to compensate the auditor due to their own business situation. “In such cases, an auditor may resign, since performing the audit at the fees offered by the company may not be commercially viable for the auditor,” he says.

KPMG network firms have resigned from four companies this year. In three, they cited commercial reasons, according to Prime Database.

S Ravi, former BSE chairman and managing partner at audit firm Ravi, Rajan & Co., whose clientele includes several listed companies, tells ET Prime that the pandemic has not impacted audit work much. “Most of the results are being completed in time. Things are getting done through secure transmission networks.”

But, Ravi adds, deficiencies and quality issues like lack of third-party confirmation, or lack of confirmation or documentation on large heads, are among the key reasons for auditors to resign. “The risk is too high in these cases.”

He says every audit firm has a checklist. “Though we have not had a situation to resign till date, we take the compliance of these checklist items seriously and ensure that it is strictly followed. Some of the items include high debtors, related-party transactions, etc. Items of qualification and emphasis also lead to differences with the management. Sometimes, the managements want that the qualified items are minimal or they don't want them at all. These are issues that often lead to [auditor] resignations mid-term.”

### **Reported cases of non-cooperation**

This year, only in three cases auditors expressly cited “non-cooperation of the management” as the reason for their resignations.

The list includes Digjam, whose auditor, Deloitte, resigned in March. The company had gone into insolvency resolution and the management was unable to share appropriate audit evidence to ascertain realisable values of assets and inventories, the auditors had informed in a detailed letter.

In August, GVK Power and Infrastructure and its subsidiary [GVK Airports](#) reported that Price Waterhouse Chartered Accountants LLP, which was the auditor, resigned. Though the auditor did not provide details in a Sebi-prescribed format, it said in its resignation that it had sent several letters to the company in July-August, seeking information relating to the audit, which were not addressed.

“In view of the various recent events in relation to the company's subsidiary, Mumbai International Airports Limited (MIAL), we have assessed the appropriateness of our continuance as statutory auditors of the company in terms of Standard on Quality Control r (SQC r), quality control for firms that perform audits and reviews of historical financial information and other assurance and related-services engagements, and accordingly wish to communicate our intention to resign as statutory auditors of the company.”

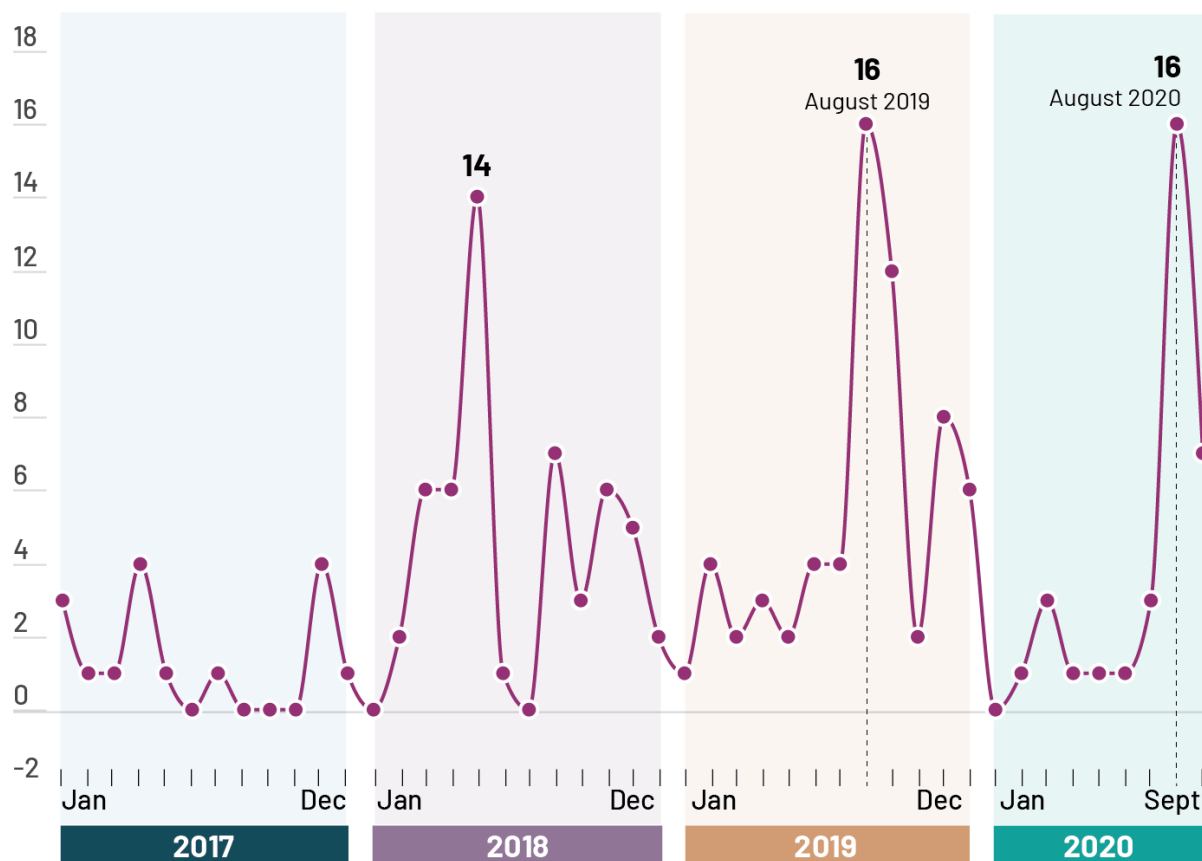
The CBI had registered a case against MIAL for alleged irregularities, including siphoning of funds. The Adani group has since taken over.

Kama Holdings was the third case where lack of information from the company was expressly reported. “The time gap between the receipt of the company’s material subsidiary’s audited financial statements/reviewed financial results and the company’s audit committee meetings is very meagre, resulting in insufficient time available for audit of the consolidated financial statements/review the consolidated financial results,” audit firm Luthra and Luthra said in a letter dated August 10.

### **The August rush to jump the ship**

Curiously, August saw the highest number of resignations in 2020 at 16, accounting for nearly half of the cases this year so far. Even within this, the first half of August saw 15 auditors bidding adieu. The 45-day criterion prescribed by Sebi — which could mean additional compliance burden if the resignations happened after August 15 — could be behind the rush.

## Month-wise number of auditor cessations in NSE-listed companies



Note: Data for a company prior to its listing on NSE is not available.

Source: [Primeinfobase.com](http://Primeinfobase.com)

ETPrime

“If the auditor resigns after 45 days from the end of a quarter of a financial year, then the auditor shall, before such resignation, issue the limited review/ audit report for such quarter as well as the next quarter,” the Sebi circular had said.

In 2019, too, a record number of resignations (16) came in August, followed by September (12). This year’s the September tally is slightly lower, at 7.

Irrespective of the reasons the auditors might give, the bunching of resignations just ahead of finalising annual accounts tell their own story.

“Lot of things are situational also. It is possible that the company was good for the past few years and due to the economic downturn, it has started behaving differently. Then you might take a call to leave, but considering past relationship, you might give a different reason to leave,” Ravi says.

