The Chamber of Tax Consultants
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17th October, 2020

To,
Ministry of Corporate Affairs
Government of India

Hon'ble Madam,

The Ministry or Corporate Affairs **(MCA)** had come out with a consultation paper on enhancement of Audit Independence and Accountability in February 2020 seeking comments from various stakeholders on " how to enhance audit independence and accountability " and there by improve Audit Quality . One of the issue the consultation paper dealt was "how to reduce economic concentration of audit in the hands few i.e Big 4 ".

The Chamber of Tax Consultants (the Chamber) had made detailed representation to MCA on 15/03/2020 on all the issues raised in the said consultation paper. One of the aspects of the Consultation Paper & Chamber's representation was on " Joint Audit". The Chamber suggested that "More domestic firms should be promoted. Domestic firm should be incentivized to increase size of the firm. Other way joint audit as well as networking firm shall also be promoted. Further these firm shall be given equal rights in conducting audit." The Chamber also suggested that Joint Audit should be made mandatory for bigger companies having turnover of Rs. 1000 crore. At least firm should be a domestic firm. All the Audit firms must have equal say in Audit."

We understand a committee has been set up to discuss the feedback received on Consultation paper issued by MCA in February 2020. As stated above, while we dealt with concept of Joint Audit, we strongly believe that Mandatory Joint Audit is essential for large Companies to enhance Audit Independence, accountability and to improve Audit Quality, in this challenging macro-economic environment. Our suggestion for making joint audit mandatory in case of large companies are based on following rationale:

1. The Hon'ble Prime Minister of India Shri Narendra Modi during his address at a ICAI program on 1st July 2017 had mentioned that India should develop indigenous large audit firms. Thus providing for joint audit would result in reduction in concentration of audit in the hands of few firms having Foreign Control and is one of the ways to build better capabilities and improve quality naturally. This would also help in developing healthy competition.

2. ‘Joint Audit’ as a concept has been widely prevalent in India for more than 50 years, and is perceived as mechanism to reduce the risk of over-familiarity .

3. As stated above concept of joint audit was already prevalent in India. 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**, however some of the large corporate houses like Reliance , Birlas, Tatas (had joint audits for many decades till both their joint audit firms became part of the same Foreign Network) and Public Sector Undertaking (PSU) like ONGC, Indian Oil, NTPC etc and Public Sector Banks have joint audit arrangements.

4. 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 requires that a joint auditor of an insurer shall not include other associate/ affiliate firms which are under the same network or whose name or trade mark or brand is used by the firm or any of the partners of the other joint auditor.

5. 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.

6. During 2018, 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.

   As per the amended regulation, where a foreign investor wishes to specify a particular auditor/audit firm that is part of an international network, then audit of such investee companies should be carried out as joint audit and one of the auditors should not be part of the same network. This however does not seem to have moved beyond the concept papers and this has no indication of being implemented in its true spirit .

7. Issue of competition, resilience, conflict of interest and regulatory weakness was again in the spotlight as the next large audit failure after Satyam in 2009, happened

8. with IL&FS fiasco in 2018. This has led to further reduction of trust in the stakeholders. **The most critical among the issues raised is that of auditor's independence. Auditor's independence being the core and most vital element of an audit, any dent on it is unacceptable to Regulators and to the user of financial statements**.

9. **Joint audits for large Entities are seen as the potential reinforcement of auditor's independence.** Auditor's independence can be improved because each auditor of large entities will have lower economic bonding with the client, and it will be more difficult for managers to convince two auditors to remain silent on any discovered problem.

10. Joint audits will also improve audit quality amongst firms based on the four – eye principle where when two firms deliberate issues and exchange views their inherent quality and perspective also improves, at the same time it brings a critical eye on the respective work of each auditor.

11. It is expected that joint audit would enable

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

12. In India concept of joint audit is more suitable as all joint audit firms are accountable for their area of work as also for the work where they are jointly responsible. Only one need to focus on evenly scoping of work between the auditors.

13. Joint audit is expected to provide more choice and resilience. It harnesses talent pool due to cross fertilization of ideas and collaborative upliftment of audit processes. Also, audit firms will gain experiences to carry out more complex audits.

14. The Indian Accounting Standards being "principle-based" standards require more application of judgment. Joint audit would enable in having two experts' opinions converging rather than only one on sensitive issues.

15. 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.

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

17. 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 .

18. Joint audit thus does offer benefits in terms of Macro-economic policy, Independence and Quality and can lead to increase in effectiveness of audit. In addition, keeping the audit market healthy, less dependent on few firms which are foreign controlled and less polarised is critical for 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 and making them global players in a world where India will have a larger role to play is important in the near , medium & long term.

19. 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. Already in UK thanks to the Actions taken by the Regulators there , the number 5 firm has become the auditor of the larger number of listed Companies compared to the Big 4. Albeit these may be the smaller listed Companies but the concentration risk is being addressed.

20. Auditor independence issues are directly addressed by 'multiplicity' of auditors as compared to 'singularity'. Every monoculture is bound to result in consequences that are undesirable ab initio and pose serious threat in the long term. Where auditor's independence is protected and preserved, it shall pave way for audit quality enhancement. Also, the increase of more watchful eyes may act as deterrent of frauds and error.

21. The increasing number of corporate failures and fingers being pointed towards audit quality issues owing to conflict of interest, joint audit arrangements should turn out to be one of the resilient guards we are looking to mitigate such incidents and may emerge as the 'White Knight' for auditor's independence.

22. The empirical findings suggest that companies adopting 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[1].

23. Some Vested interests have raised the bogey of higher costs in case of joint audits , which is not borne out by the facts in Corporate India where Joint Audits have not resulted in huge costs increase but more in sharing the total fees by few firms instead of one firm garnering the whole fees. And even if there is a marginal increase the same is offset much more by the benefits mentioned above.

24. Global clues:

(i) France has mandated joint audit since 1966. Similar provisions are also in place in countries such as Morocco, Kuwait, Congo, and the Ivory Coast.

Also, auditing by two independent auditors is mandatory in Saudi Arabia, Algeria, and Tunisia.

(ii) In Belgium, and South Africa and a handful of other African jurisdictions joint Audits are mandated for companies in the financial services sector.

(iii) France continues to use joint audit focusing on benefits of a sustainable and less concentrated French audit market, which balances any questions regarding increased cost or debates about audit quality.

(iv) It is believed that the mandatory requirements in France have helped to ensure greater representation of more firms in the audits of the largest companies. 13

other non-Big Four firms are involved in the audit of the top 100 French listed companies, compared with only one involved in the FTSE-100 in the UK.

(v) The French experience show cases 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.

Future of Audit – UK Recommendations

(vi) The debacle of Carillion, BHS and series of audit failures forced the UK Legislation to review its existing regulations and the effectiveness of audit. Post the audit catastrophe of Carillion and BHS, the Business, Energy and Industrial Strategy Committee of the House of Commons (UK) in its report 'Future of Audit' (Nineteenth Report of Session 2017–19), noted that **the Big Four dominate the FTSE 100 and FTSE 250 UK audit markets**. The obstacles facing other firms (challenger firms) have led to a lack of competition and choice for some of most important companies when they change auditors. They recommended joint audit as one of the measures to reform the UK audit industry last year.

(vii) The committee envisaged that choice would all but disappear if one of the Big Four failed. The committee felt that this precarious situation must be addressed before it is too late and to improve resilience and choice, the challengers firm needed to gain a secure foothold in FTSE 350 audits .and there by recommended a segmented market cap and the use of joint audits, on a pilot basis, for the most complex audits to enable the challengers firms to step up.

(viii) In the study carried out by Biscogno and De Luca (2016) to investigate the effect of joint audits on the quality of the firm's financial statements in the

case of Italy, they confirmed that the joint audit system does positively affect the reliability of firms' financial statements.

(ix) The European Commission Green Paper (2010) highlighted concerns regarding high audit market concentration and suggested the introduction of mandatory joint audit in the European Union (EU). This proposal was motivated by the recognition that the Big 4 firms dominated the audit market in the EU.

(x) The less concentration of the French audit market, compared to other European countries, is often viewed as a direct and desirable outcome and consequence of the joint audit rules and regulations.

The Auditing standard on similar lines 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.

Joint audits are not a ready remedy. Implementation of joint audit might be 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 or borrowings more than INR 1000 crores

In conclusion, we strongly and earnestly suggest the Joint Audits should be made mandatory for large entities.

Thanking You,

Sincerely,

For **The Chamber of Tax Consultants**

Sd/-	Sd/-	Sd/-
Anish M. Thacker	**Mahendra Sanghvi**	**Apurva Shah**
President	**Chairman**	**Co-Chairman**

Law & Representation Committee

CC : Hon'ble Prime Minister Shri Narendra Modiji

Mr. Anurag Thakur, Minster of State for Finance