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SEBI'S POLICY PROPOSALS TO CURB ABRUPT RESIGNATIONS OF AUDITORS FROM LISTED COMPANIES

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Background

The Securities and Exchange Board of India (SEBI) has observed that many statutory auditors of listed companies have abruptly resigned without completing their assignment for the year. Many a times, these resignations were sudden and the reasons were often vague, ranging from "pre-occupation" to "lack of adequate information from the company". For example, in June 2019, Price Waterhouse & Co. resigned as the auditor of Reliance Capital and Reliance Home Finance, stating that they did not receive substantive responses to their queries. Similarly, last year Deloitte Haskins & Sells quit as the auditor to Manpasand Beverages, due to lack of cooperation by the company on sharing data with the auditors.

Taking note of such resignations, whereby auditors have resigned without assigning detailed reasons, SEBI has proposed to tighten disclosure norms with respect to resignations of statutory auditors and has issued a 'Consultative Paper on Policy Proposals with respect to Resignation of Statutory Auditors from Listed Companies' dated 18 July 2019 (Paper), with an aim to address situations where an auditor decides to resign before fulfilling its responsibilities for the audit period it is appointed for, leaving investors and stakeholders devoid of reliable financial information about the listed companies and their unlisted material subsidiaries.

The Paper states "*resignation of an auditor due to reasons such as pre-occupation before completion of the audit of the financial results for the year seriously hampers the investor confidence and leaves the investors with lack of reliable information for taking their financial decisions.*"

Key changes proposed

Enhancing responsible behaviour of auditors and strengthening disclosures to investors by the auditors

- Placing conditions on auditors prior to their resignation

  As resignation of auditors before fulfilling their responsibilities hampers investor confidence and leaves investors lacking reliable information for taking their financial decisions, SEBI has proposed that if the auditor of a listed entity/material unlisted subsidiary of the listed entity proposes to resign,

  - after signing the audit report for all the quarters (limited review/ audit) of a financial year, except the last quarter, then the auditor shall finalise the audit report for the said financial year before such resignation, and

  - in all other cases, the auditor shall issue limited review/audit report for the quarter in which the auditor resigns from the listed company.

  With respect to the material unlisted subsidiaries, the auditor shall issue the limited review/audit report for that financial year or quarter, as applicable, before such resignation.

  Further, if the reason for the auditor's resignation is that the listed entity or a material unlisted subsidiary of a listed company is not providing information, the auditor shall provide an appropriate disclaimer in its audit report, in accordance with Standard of Auditing suggested by the Institute of Chartered Accountants of India.

  SEBI has suggested relevant amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations), to effect the above.

- Prescribing a format of resignation

  The resignation letter shall include detailed reasons for resignation and in case of any concerns, efforts made by the auditor prior to resignation. If the resignation is due to information not being made available to the auditor, further details shall be provided including whether the auditor could have performed alternative procedures to obtain appropriate evidence for the purposes of the audit/limited review.

Increased disclosures to investors and strengthening the role of the audit committee

SEBI has, in the Paper, proposed that in case of resignation of the Auditor, the listed entity shall disclose the resignation letter of the auditor to the stock exchanges (in case of material unlisted subsidiary, the subsidiary shall disclose the resignation letter to the listed entity and the listed entity shall disclose the same to the stock exchanges).

Further, SEBI has observed that while the Listing Regulations lay down the broad role of the audit committee, there is no specific procedure to be followed by the auditor or the audit committee, when there are significant concerns leading to the auditor's resignation.

SEBI proposes to issue a circular or amend the Listing Regulations to lay down the procedure in such cases, as follows -

- Auditors shall approach the chairperson of the audit committee directly and immediately in case of any concerns with the management;

- In cases where resignation is due to non-receipt of information from the management, the auditor shall inform the audit committee about the details of information/explanation sought;

- The audit committee shall thereafter deliberate on the matter and apprise its views to the management and auditor.

The listed entity shall be required to submit the views of the audit committee and its board to the stock exchanges along with the aforementioned resignation letter of the statutory auditor.

SEBI has invited comments on the Paper by 8 August 2019.

Comment

The proposed amendments are designed to promote higher accountability of auditors and enhance investor protection. While steps are included to discourage auditors from jumping ship in the middle of their term, safeguards are also put in place by ensuring that the auditors not only list out detailed reasons for such resignation but also list out efforts made by them prior to the resignation. The Paper also proposes that the statutory auditors confirm in the resignation letter that there are no material reasons for resignation other than those mentioned in the said resignation letter, ensuring that the investors and stakeholders are made aware of all information required to make informed decisions. Clarifying the role of the audit committee is also a step in the right direction in this regard.

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