# AUDITING: AN INDIC FRAMEWORK

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This article proposes fundamental changes to the auditing framework in India seeking to move away from the present Western framework, which has been blindly adopted, and lead to dysfunction in our audit profession. There is more, but only a couple of framework items, namely, marketing and constitutional status, are selected for the present article. This 'Indic Framework' has the potential to drive changes globally starting with India.

The Supreme Court has directed on 23rd February 2018, in a landmark judgement against the multinational audit firms operating in India, in the Sukumaran Case, that GoI should come up with a new statutory framework. Identifying the root causes of the problem sets the stage for a new framework. The auditor needs to be constitutionally provided with a judges' standing, in a fundamentally re-thought new-framework, in so far as it concerns his role as an auditor.

Can the auditing system work if the framework itself is broken and dysfunctional? Then why wonder as to how come the auditing world has been raining scams and will continue to rain scams? All we need to do is stop blindly following a defective framework unthinkingly, because it comes from the West, or because some global firms, powerful lobbies and governments support it.

## THE AUDITOR AND THE JUDGE - MARKETING

For those who do not have a clear picture that an auditor is seriously disrespected by the very framework of the laws, and his position is compromised. The present western audit framework is unsuitable for the quasi-judicial function of independent financial statement auditing, should clearly visualise the following comparable scenarios, and then introspect, if an auditor can still be independent, ethical and respect worthy, no matter how honest he may actually be.

1 Imagine a judge pleading before the potential litigants in his court –O Dear Potential Litigant in my Court, please give me your case to stand in judgement over? please??! And the judge gets praised as to what a fabulous marketing angel he is?!

2 Imagine a judge doing his brand marketing exercise with a potential litigant in his court – I will give you my name on my Order in your case, and, what a great name will be associated with the Order? You simply cannot compare my name with any other? O Please, how can you go to a smaller judge?!!

3 The judge then opens up his marketing presentation and reveals high quality marketing collaterals, which leave his litigants in a swoon – they can't think of going to another "ordinary judge"... It would be infra dig in my cocktail circuits to do that…hmmm..

4 Imagine a judge entering a remuneration contract with a potential litigant in his court – these are my fees / salary / consulting charges for issuing an order after I stand in judgement on your litigation in my court!

5 Imagine a judge offering a bargain basement "pricing offer" to a potential litigant in his court – I will undercut all the other judges, I will give you 25 percent cut in my fees, you must appoint me!!

6 Imagine a judge sending snazzy update-newsletters to the potential litigants in his own court, containing scenarios of 'advance rulings' on what he would do as a judge in various latest-situations, and telling the potential litigant. "Look at this, you will not have problems, if your case gets heard in my court"!!

7 Imagine a judge telling the potential litigants: this is not about me or who I am – this is not a service of my

personal skill and ability, it is not a conscience matter – it is all about the vast empire of the Big N business of which I am partner and we have worldwide strengths. What does it matter what is my capacity – after all it is not me, it is ABCD, the largest "global judgment network" that is doing your work. How can a lowly single honest judge be compared to ME?!! I am the most honest of all judges ever!

8 Imagine a judge telling fellow judges in the courts, you guys are incompetent and lack the capacity – you don't employ as many people as I, you don't train them as well as I do, you don't pay them as well as I do. You are all nothing compared to what I AM. LoL. Litigants are not fools to select me. ROFL.

9 Our judges network offers just about every other service, doctoring, laundry, housekeeping, construction, what not? You name it, we have it! Obviously, that makes us best judges. Don't waste your time with others! We come to ement delivered right there – don't be ridiculous, you don't have to come to the Courts anymore. You're the boss! And, ofcourse we are truly the best in our global-village world - quality in everything we do, always one step ahead. Cheers!

## CONSTITUTIONAL AUTHORITY

While the Judge enjoys constitutional authority, the Auditor enjoys none. The case for the need to make this change is identified here. There is indeed a very strong case for this.

The Auditor renders a very skillful job of delivering an opinion on the true and fair view of the financial statements of the audited entity. There are multiple points in the conduct of an audit where application of mind, involves very experienced and deep judgment. On the one hand, there are the 'facts' of the case. On the other hand, there are the laws and standards and 'regulations'. An application of the regulations to the facts, gives rise to numerous onerous interpretations involving complex issues of law, probability, precedence, intent, all supported by independence and ethics. This gives rise to multiple set of interpretations and understandings of the same facts and regulations. This is where judgment comes in. While the auditee's management may argue along one line, the independent directors, the promoter directors, the audit engagement teams – at corporate office, and at other locations - and the consulted subject matter experts, may all choose different lines. This is often the case. Based on all this, the auditor (signing the financial statements) has to make a final judgment call and his 'order' is contained in his Auditors Report. It has been repeatedly said especially recently that an auditor's signature is relied upon by the whole nation, meaning to say that the role of the auditor is crucial. Sadly, in all this, the company treats an auditor, who plays such a crucial quasi-judicial role, like any other 'vendor': commercially and there ends the matter.

This ostrich-like stance of the western rules of auditing that is the basis of our present laws, defies the facts of the situation, that in so far as the audit is concerned, the auditor performs a quasi-judicial function based on exercise of both personal skill and judgment, involving a conscience-based duty, delivering grass-root governance to the entire economy in the form of assurance arising from his integrity, and therefore the present structure is far from salubrious, just as making a judge subservient to the litigants, denying him the standing, denying him the privileges, and the financial independence, will all compromise and throw into jeopardy the legal system.

The very same outdated framework of laws, which fails to protect the standing and role of an auditor, however, expects that the auditor should be independent of the auditee, without providing any support for it. The auditor can be (and often is in present times) hauled-up for misconduct for taking a stand in his audit opinion, which need not match with those on the other side of the disciplinary process.

The disciplinary process is often vitiated because decision-makers do not have a clue and/or have never conducted a financial statement audit. Finding competent decision-makers to man the disciplinary-process is akin to finding a needle in a haystack. An auditor can be sued for defamation if he resigns for making explicit disclosures; and really speaking it is not at all the auditor's deliverable to make public statements other than those he is formally reporting on. Vested interests in our business world weaponize these legal provisions against the auditor and the auditing firm in pursuit of their own goals, complicated by incompetence of those who are given the powers to indict an auditor. Even a casual glance shows that the classic systemic-failure of a 'judge becoming subservient to the litigants', referred to above, has become the reality. This has jeopardised the audit process – creating a dangerous environmentthat is now hanging by a thread – one in which the big fish escape and nameless small issues gain a place of importance.

The biggest loser of course is the investor, and our capital markets. Ask well-experienced auditors, and they will uniformly agree on these forces at work. As a further consequence of our present defective foundation, the audit process over the years has turned into an extreme-documentation-exercise rather than remain as one that is focused on application of responsible professional judgement. The better auditor is the better file-maker: one who is best able to fend off or absorb professional liability. This in turn has created a secondary wave of risks-and-failures. A cottage industry has emerged of 'auditor shopping': good-documentation by presentation-savvyauditors is exploited by corporates, as a substitute for good auditing. It is all too obvious that the process when tested in situations will continue to fail, as it is inherently fraught with inadequacies. No amount of SOX and governance rules, fresh auditing standards, tweaks to listing rules, independent director training, higher regulatory authorities, can fix the problem, and having tried it for a few years, we see that audit failures still continue to happen. Why? Because the root cause of the failure, namely the lack of standing and authority of an auditor as a constitutional authority similar to a judge, has failed to be recognised.

It is essential to empower the auditor and not keep him as a pawn in a commercial game. By keeping the auditor as a pawn, all rules have already been compromised by interests whose objective is that. Have we not said always that auditing is a noble profession? Should there not be a framework to support it? Any disagreements of stake-holders on an audit opinion, should vest as in the case of the order of a judge, against the merits of the order itself, through an appeal to a senior auditor on its content, rather than viciously crucify the auditor personally and labeling him as guilty of misconduct, effectively destroying honest professionals (even a single finding of guilt suffices in today's evaluation structure), professional firms, and finally de-railing the profession.

## GRASS ROOTS "GOOD GOVERNANCE" IN NATIONAL INTEREST

On a national scale, the court system, interfaces with less than one percent of the population. The legal system kicks in only when there is a complaint on a dispute. On the other hand, nearly one hundred percent of the population is directly or indirectly, subjected to an audit. Every business, and every charity, is audited. The financial statement audit is nearly omnipresent and is a substratum of the nation's economy. The objective of our times is to bring in good-*niti* – ethics, integrity, and *good governance*. Indeed this objective that is to be fulfilled is in the motto– *satyamevajayate*. By re-positioning the status of an auditor, the reach of integrity and good governance in society will be almost pushed to one hundred percent.

This shows how vastly favourable the impact on the population will be by a reform of this nature – in fact so complete will be the roll out of the process of bringing an undercurrent to all our affairs, that such a change will completely clean up the country's everyday standards of ethics at the grass root level. One can safely say that this is in our national interest. *Kautiliya* believed that "greed clouds the mind" implying that a greedy person could not figure out the consequences of his/her actions. It is therefore essential that a premium is placed on probity, and, the audit profession be rescued from the bad framework which blindly ape the west, and the chartered accountant is given a constitutional position similar to a judge in so far as his function as an independent auditor of financial statements goes. ■