WHITE PAPER ON MULTINATIONAL ACCOUNTING FIRMS OPERATING IN INDIA

Prepared and published in public interest to inform the stakeholders in the Indian economy and the Indian public

In the context of the state of the accounting profession of India whose collective interests approximate to national interests.

And in the context of the stealthy entry of Multinational Accounting Firms [MAFs] into India through their global financial nexus

And in the context of the failure of the Government to extend the benefit of the policy of calibrated opening to the Indian CA profession

And in the context of such illegitimate presence and even more illegitimate activities of the MAFs in India way ahead of the WTO schedule in GATS, negotiations on which have hardly begun with nations exchanging just wish lists in the year 2003

And in the background of the current poor perceptions about the MAFs in the West which are widely at variance with the red carpet reception to the MAFs in India

Compiled and edited by

The Group On White Paper on Multinational Accounting Firms

Constituted By

THE CHARTERED ACCOUNTANTS'
ACTION COMMITTEE
FOR LEVEL PLAYING FIELD

IV FLOOR, ROSY TOWERS
8, UTTAMAR GANDHI SALAI
NUNGAMBAKKAM
CHENNAI-600034.

INDEX

CHAPTERS	PAGE NO.
CHAPTER 1:	**1**
WHY THIS WHITE PAPER	
CHAPTER II:	**10**
GLOBAL FINANCIAL ARCHITECTURE - EVOLUTION OF THE COMPLEX FINANCIAL SYSTEM, THE EMERGENCE OF THE FINANCIAL PROFESSIONAL AND POWERFUL MAFs	
CHAPTER III :	**22**
MAFs: THEIR HISTORY, EVOLUTION, OWNERSHIP AND THEIR PRESENT STATE IN BRIEF	
CHAPTER IV:	**25**
THE EVOLUTION AND STRUCTURE OF THE INDIAN CA PROFESSION, ITS REGULATORY MECHANISM AND CONTROL.	
CHAPTER V:	**30**
THE ENTRY OF MAFs IN INDIA AFTER THE ONSET OF LIBERALISATION AND GLOBALISATION, AND ITS CONSEQUENCES TO THE PROFESSION AND THE NATION	
CHAPTER VI:	**43**
THE ISSUE OF LEVEL PLAYING FIELD FOR INDIAN CAs, IN THE CONTEXT OF THE STRUCTURE OF THE INDIAN CA FIRMS, THE BILATERAL RECIPROCITY AND FURTHER IN THE CONTEXT OF THE MULTILATERAL GATS	
CHAPTER VII:	**51**
THE PHILOSOPHY, CHARACTER, WORLD VIEW, GOALS OF MAFs: THEIR STRATEGIES AND METHODS; THE APPREHENSIONS ABOUT THEM; THEIR GENERAL IMAGE IN THE WEST	
CHAPTER VIII:	**96**
THE TRACK RECORD INDIVIDUAL MAFs -- A CONTINUING STORY OF COMPLICITY IN CORPORATE WRONGS TO ASSISTING AND PLANNING WRONGS:	
CHAPTER IX:	**125**
MAFs IN INDIA AND THE INDIAN CA PROFESSION -- A STUDY IN CONTRAST	
CHAPTER X:	**131**
AN ILLUSTRATION OF THE PUBLIC OUTCRY AGAISNT THE MAFs IN THE WEST, AS CONTRASTED WITH HOW THEY ARE CELEBRATED IN INDIA.	
CHAPTER XI:	**134**
THE ROLE OF THE GOVERNMENT, MEDIA, CORPORATES, AND ICAI AND HOW IT HAS AFFECTED THE INDIAN CA PROFESSION	
CHAPTER XII:	**137**
WHAT SHOULD THE INDIAN CAs DO?	
A FINAL WORD	**140**

CHAPTER 1

WHY THIS WHITE PAPER

This "White Paper On The Multinational Accounting Firms" is being brought out by the Chartered Accountants Action Committee for Level Playing Field [CAAC] in public interest to inform the Indian business, Indian finance sector, Indian Government, Indian policy makers, Indian professionals and also the general public about the correct facts about the Multinational Accounting Firms [MAFs] and about the state of the Indian accounting profession. The 'why' of this White Paper is explained in brief at the out set as a key to this document.

Wide difference between the perceived image of MAFs in India and the facts about them

There is wide difference between how the MAFs are perceived today say in the West, on the experience from where they rest their claim to operate in the rest of the world, and in India. In the west they are treated more as a necessity and inevitability at home, nevertheless as a tool to serve the Western agenda in the rest of the world. In brief there is a difference between the perception about them in India and the reality. There are many reasons, including the historical, colonial hang over, for such high perceptions about things and institutions from the West in India. But the most important reason for such difference between the perception about the MAFs in India and the reality, which is the perception about them in the West, is the lack of knowledge about the MAFs in India, particularly among the main players in the Indian economy and in the Government and even in the media.

How the image of the MAFs in India is totally divorced from the reality may be demonstrated by just two contrasting events, both happened even as this White Paper was being prepared. The first event was the recent [7.June 2003] Ernst &Young International Entrepreneur Award was given to the IT icon of India, the Chairman of Infosys, Mr Narayana Murthy. It was a media hyped event which gave high visibility to E&Y. It was just a week earlier that the Securities Exchange Commission of US recommended suspending E&Y from accepting new audit work. If the award were to be given in the US to some one, it would have been embarrassing for the recipient. But in India it is touted as an honour. Actually considering the relative merit of E&Y and the recipient Infosys Chairman Narayana Murthy, it is an honour from him to E&Y. But, that is not how it is perceived in India or promoted in India. A week after E&Y gave the award to Mr Narayana Murthy, the Guardian newspaper published the following report of about E&Y camouflaging a huge fee it received from the bankrupt Health South in US for toilet inspection as audit fee:

"Accountancy is dirty work, but who would have thought Ernst & Young could earn £2.4m for inspecting toilets? The Wall Street Journal has found that the firm was paid the money for what was coyly termed "pristine audits" between 2000 and 2002 by Health South, the disgraced US health company - which the accountants classified as "audit-related fees" but actually paid for scores of junior E&Y accountants to visit Health South's clinics to check toilets for stains. In fact, Health South only paid Ernst & Young $3.3m to audit its accounts, compared with $4m to check the lavatories. A variety of Health South executives have pleaded guilty to accounting fraud in a $2.5bn scandal - so it's a shame E&Y didn't spend less time looking up the U-bend"

Comparing the extent of fee paid for inspecting toilets with the fee paid for audit, it is obvious that the main work done by E&Y for Health South was toilet inspection, and they also

audited the accounts of the company. That is, they also do audit work! A week later the Hong Kong police arrested a partner of E&Y for fraud. This was the second event, both within a week of each other. These are not just anecdotal isolates. This is the trend, repeated. According to the study by CAAC explained in detail later E&Y has paid fines aggregating to over $3.7 billions and is involved in many cases of fraud and abetment. This MAF is conferring in its name for the International Entrepreneur of the year Award to the most acclaimed Indian businessman, known for his ethics and corporate governance. First this Award is not given to make Mr Narayana Murthy known to India or even to the world. It is the other way round. Again had only the Indian public and the Indian corporates been aware of the true facts about the firm or had Mr Narayana Murthy been aware of the track record of E&Y it would be doubtful whether he would have considered it a real honour to receive the award in the name of such an organisation. In the process it is E&Y which has increased its brand value by giving the award to a globally established icon like Mr Murthy. While the E&Y was being ridiculed and humiliated in the media abroad, here in India the award given in its name was being regarded as an honour.

This is just an illustration. Nothing could be more demonstrative of the wide divergence in the perceptions about the MAFs in the West and in India.

Based on the perceived images, the Indian establishment places blind trust in MAFs

Because of the inadequate awareness about the MAFs and about the true facts about them the Indian business, particularly the corporate and the finance sectors, and also the Government and policy makers, implicitly trust the MAFs and their professed and advertised competence and ethical standards. The elite public also tends to believe the assessment of the Indian establishment about them. There is also some kind of unverified and un-assessed aura about them, which prevents proper assessment about them.

Merciless scrutiny in the West Versus the Red carpet welcome in India

It is a contrast. The MAFs are subjected to merciless scrutiny in the West both by law enforcement agencies and are subjected to fines and sentence of suspensions of practice and even in non-western world they are being called to account for their misdeeds, like in Hong Kong where a partner of Ernest & Young was arrested on 10 June 2003 for professional delinquency. In India they are being red-carpet welcome. They are being consulted by the Government. They are engaged by the Planning Commission, Divestment Ministry and different state Governments at extortionate cost. The Public Sector financial institutions and banks engage them for their reconstruction work. They engage them to secure certificates from them as to how well they are working or managing their business. Where the domestic financial institutions monitor some of the corporates assisted by the DFIs they stipulate that such assisted corporates must engage the MAFs for certifying their quarterly income statements. And the MAFs do this work at prohibitive cost. In the process the MAFs have trespassed beyond their permitted 'raison detre' of consultancy and have infiltrated into attestation and audit functions. In some cases of late they are also doing statutory audit functions indirectly through their surrogates. Thus they command a value based on their brand in the Western countries. But the scrutiny which goes on in other countries about them does not take place here. Because there is very little knowledge in the Indian system about them and about how they are viewed outside.

CAAC's concern about the lack of correct knowledge and understanding about the MAFs; and the need to inform all stakeholders manifests in the idea of this White Paper

It is in these circumstances that the CAAC, concerned at the prejudice to interests of Indian Chartered Accountants, the main stakeholder in the accounting profession in India, whose collective interest converges with national interest, considered it necessary in the larger national interest to inform them about the correct facts about the MAFs through this White Paper. The CAAC considers it all the more necessary to inform them as the main stakeholders do not have the correct or adequate information about the true facts about the Multinational Accounting Firms operating in India.

The intent and content of the White Paper - a preview

Thus, the main intent and purpose of the White Paper is to inform the Indian stake holders about the correct facts about the MAFs, whose services they engage and trust, so they can make intelligent assessment and judgement about them even as they engage them as prohibitively high cost. The White Paper also intends to make the Indian accountancy profession, the Indian business and also other stakeholders aware of how MAFs made surreptitious entry into India using the foreign exchange crisis in India and taking advantage of many incoherent policy decisions mindlessly adopted under the pressure of the IMF and the World Bank to tackle the crisis at that time. It also endeavours to inform how their presence in India is illegitimate since the Institute of Chartered Accountants of India [ICAI] was kept in dark in the decision to let in the MAFs to do consultancy in India by licences issued by the Reserve Bank of India. This incidentally resulted in opening up of the accounting profession without any reciprocal advantage to the Indian accounting profession and also ahead of the WTO schedule for multi-lateral agreement for trans-country accounting services, for which the member-countries have started filing position papers only now, i.e., in the year 2003.

How India's negotiating capacity in WTO is eroded

The White paper strives to explain how this has eroded the negotiating capacity of India in the WTO as opening the vital profession of accounting services means that the negotiators have played the last card first without anything further to give to get something in return in the negotiations.

What are the consequences of their illegitimate presence

The White Paper also seeks to inform them about the consequences of such illegitimate presence both for the Indian accounting profession as well as for the Indian business.

How the Indian accounting profession was not alert enough

The White Paper also endeavours to emphasise how by not being alert the Indian accountancy profession has virtually handed over the business consultancy market in India to the MAFs, without any reciprocal access to the Indian professionals abroad. And how, with the result, the accounting profession in India today does not have the advantage of either bilateral reciprocity through bilateral negotiations or Most Favoured Nation Treatment (MFN) under multilateral negotiations in the WTO.

How the MAFs have infiltrated into areas other than consultancy

The White Paper is also intended to bring home to the Indian accountants how the MAFs, who have illegitimately entered the Indian consultancy market, are not limiting their raison d'etre to the consultancy work only and how they are in the process of illegally and surreptitiously taking over the attestation and audit functions of the profession in India.

How the professional opportunities emerging from globalisation has been monopolised by MAFs

The White Paper also brings out the fact that how the new and high end professional opportunities attendant upon globalisation have been largely monopolised by the MAFs, thus leaving the Indian CA firms to fight for low end services.

How the Indian CA firms are weakened at home and deprived of the chance of becoming a global power

This White Paper is also presented with a view to make the system and the establishment including the media and the opinion makers aware of how the Indian accounting professionals, who constitute the third largest army of trained and skilled professional of their type in the world, being next only in numbers to US and UK, are denied level playing field and weakened in their own country and how they are denied the opportunity to become a global force building on their national strength.

How the Indian establishment is ignorant of the true facts about the MAFs

The White Paper also seeks to inform the general public and the different segments of the Indian establishment the little known facts about the MAFs as without the knowledge of such vital facts about the MAFs how the Indian business establishment and also the bureaucratic establishment have been according them red carpet welcome while they suffer from the ignominy of an acute lack of credibility in the western countries.

The White Paper, described in nutshell

Presents the MAFs as they are actually perceived in the West;

Captures how the MAFs are global only in their brand and how they diffuse themselves to evade local laws and are virtually not subject to supervision by any body or authority as they claim that their different country operations are unrelated to one another;

Exposes how the ownership of the MAFs are unknown and are buried in secret tax havens of the world and how a profession which requires all transparency is, by intent and design, not only opaque but also secretive; and

Discovers for the Indian audience, business and political, bureaucratic as well as professional, how the MAFs hide unbelievable misdeeds behind the veil of secrecy and of their brand power and lobbying power, the nexus of the MAFs with other multilateral agencies in the global financial architecture.

This White Paper, thus, is presented to the different stake holders in the Indian economy and to the general public of India in the larger national interest and also in the general interest of international business in India.

The back ground: The globalisation and liberalisation programme in India and the emergence of lack of level playing field, even a hostile playing field, for Indian CA firms

It is necessary at this stage to capture the background to the entry of MAFs in India. The entry of MAFs in India was occasioned by the opening of the Indian economy in the early 1990s. The globalisation and liberalisation programme of the Government of India undertaken largely on the persuasion of the IMF and the World Bank based on the principle of Washington consensus was the route through which the MAFs entered India. The history and mode of their entry and the consequences of their entry will constitute the heart of this White Paper.

The un-debated transition from socialism to market capitalism in India

India is one of the large nations, which initially launched a listless, ill-defined and ill-directed liberalisation and globalisation programme in early 1990s without adequate homework.

Globalisation, in itself, is an ill-defined idea. Even though it apparently intends to institutionalise a rule based world economy, trade and investment without barriers, it has so far been only the rule made by the mighty. This is how many leading commentators on globalisation, who are themselves great votaries of the idea, have critiqued the concept. Yet to day this ill defined and even more ill-executed idea of globalisation deeply influences our micro and macro economic thinking, working and in fact the collective Indian psyche. It was only after about five years coinciding with the popular outcry against the frauds seen in the Enron power project which was projected as the manifestation of the liberalisation and globalisation programme of the Indian establishment, that a feeble debate has started about the content and quality of the liberalisation and globalisation agenda of the Governments in India.

In fact the tilt in Indian thinking and in the Indian economic policies towards globalisation in early 1990s was not a deliberated national decision. It was compelled and driven by the foreign exchange crisis that almost turned the country bankrupt in early 1991. Panic reaction to this crisis resulted in a de-focussed liberalisation and thoughtless globalisation, both undertaken without proper home work and debate and understanding. Just as the nation was blindly led into the socialist mess in mid 1950s, it was led into another mess in the name of un-calibrated globalisation and thoughtless liberalisation. In fact even before different countries of the world began to understand the concept and structure of globalisation, India had begun to put into practice the ideas and theories of globalisation as the west commended. Actually even before the WTO came into being and began to lay down multilateral rules for trading, investment etc., we in India began implementing them and in the process virtually experimenting on India in years what the West experienced in decades and even centuries. Elites and intellectuals of India, who were socialists till socialism collapsed in the world and even headed the South Commission that rejected the idea of free market, overnight defected to the West-centric and IMF-World Bank prescribed model as the inevitable roadmap to develop India. Thus un-calibrated and ill-defined globalisation and liberalisation process set in motion in India from around 1991.

The Indian socialist regime [1955-1991] and its assumptions

This was a u-turn for a country which was for over three decades from 1955 following the so-called socialist model of state-dominated economy with the commanding heights of the economy left to be handled by the State, which also decided what and how much the private operators should handle, subject, of course to licensing. In fact, when the country accepted this socialist model in 1950s itself, it was without any debate as to the suitability of the socialist model to the Indian ways of thinking and living. The socialist psyche was so much internalised in politics that in the late 1960s and early 1970s any one who disagreed with the socialist model was labelled as anti-poor and pro-rich, pro-America and even as CIA agents! Those who differed from socialist ideas were ostracised as political untouchables. With the result every political party was compelled to file an undertaking expressing faith in the ideology of socialism, to be registered as a political party eligible to contest elections. (This rule prevails even today!!). In fact even the Constitution of India was amended [in 1976] to define India as a socialist state. This definition is still very much an effective part of the preamble to the Constitution. Different provisions of the constitution were repeatedly amended to institutionalise and implement socialist and state dominated economy in India. There are over 90 amendments to the constitution till today, most of them intended to give constitutional affirmation or sanction for economic measures taken to implement socialist programmes. Even the property rights listed as un-abridgeable

fundamental rights were deleted and relegated to the status of mere legal rights. The effect of this is to facilitate even expropriation of property with or without adequate compensation. That is today the Government can in theory and lawfully expropriate the properties of any one in the country, including those who have invested their monies from abroad. These laws, the judgements of courts based on such laws and approving such laws are still in force. They constitute the laws on economic relationship between the Indian state and its citizens. Thus the largest segment of the organised economy in India was handled by the state and state run corporations. The state was the largest dispenser of economic opportunities and it is not very different even today, despite more than a decade of privatisation and globalisation.

The U-turn to liberalisation and globalisation in early 1990s

However with the onset of globalisation policies of the Government, establishment assumptions of the Indian state about the national economy have changed almost completely. Today contrary to any one dissenting against socialism being labelled as anti-poor, pro-rich and pro-US and even as CIA agents, and any one who dissents against either the principles of globalisation or against the pace of it, is instantly designated as protectionist, anti-modern and anti-development.

In fact, the sequence of liberalisation and globalisation began at the wrong end, with the later preceding the former in most areas. Since the establishment thinkers and bureaucrats determined the strategy and sequence of the economic transition without any participation of the stakeholders, there was very little awareness about the content and consequences of the liberalisation and globalisation programmes even among the informed minds of India. Even the high end industry in India which could be trusted to understand global developments and trends was not sufficiently informed about the impact and consequences of the emerging global regime. Thus without any home work the nation entered the global economic game, presuming that globalisation would promote global investment and global trade and technology in this country. But in practice global trade merely plays a subsidiary role to global finance and in volume it is miniscule. In fact the very architecture and drive of globalisation is global finance.(This aspect has been dealt with elaborately elsewhere in this White Paper) Investment banks, commercial banks, merchant banks, rating agencies and financial professionals constitute the closely knitted centrifugal driving forces of global finance. That is how the opening of any economy is co-extensive with the entry of these centrifugal forces together. In fact the Washington Consensus, which became the foundation for what later became globalisation, was a formula designed by the players in global finance essentially led by the US Treasury and the IMF and World Bank. It is widely acknowledged that there is a symbiotic relationship among these forces. For example if the disinvestment programmes are deferred in India, that would affect the role and income of the MAFs in India. Therefore promptly the rating agencies will reduce the rating of India on the ground that because of the deferment of the divestment programme the confidence of the foreign investors has diminished in the Indian economy. So it is widely apprehended that the diverse centrifugal forces, which drive the process of globalisation, almost work in collusive cohesion. It is by such collusive convergence of efforts that the MAFs entered India by exploiting the 1991 economic crisis, and forcing the Government to open the gates to them through the RBI.

The conception and birth of the CA Action Committee for Level Playing Field and the evolution of the idea of the White Paper

Due to the colonial hangover in India, almost everything that the West commends is readily accepted, un-scrutinised and untested at the elitist and intellectual level in the Indian establishment. The result is that the experience of the West is repeatedly and freely imposed on

an unsuspecting nation, which has vast diversity and differentials as compared to the largely homogenous west. This was true of the socialist experiment of 1950s as much of the free market experiment of 1990s. Thus the elites of India, including the intelligent professions like the CAs, failed to give proper intellectual lead for India at the crucial and critical moment of transition from the socialist model to the market driven model in the early 1990s, and failed just they failed in the mid 1950s when socialism was hyped about. They were just part of and promoters of the herd mentality. Therefore it was no surprise that when the Government decided on globalisation and liberalisation on the lines of the US driven western model, the elites of the country, including the confirmed advocates till the previous day of state-driven model overnight defected to the new model, without any thought or plan to calibrate the transition. In fact the intellectual hype was so intense about globalisation that any one who advocated a more calibrated and transition-friendly approach was suspect in the eyes of the modern, which meant western. Consequently it was more fashionable to ask more liberalisation and globalisation than to ask for calibrated approach to both. In this clamour for more and more, un-calibrated and un-thought liberalisation and globalisation the illicit entry of the MAFs was actually welcomed, not considered harmful to national interests or the professional interest of the Indian CAs. A more calibrated and transition-friendly approach would have produced an entirely different policy on entry of MAFs into India. In fact the Indian CA profession itself was persuaded to believe, and it also believed, that the entry of the MAFs would be beneficial to the Indian CAs.

As the Nation begins to feel the pinch, section by section of the national economy begin to resist

Gradually from around the year 1995 a change began and the Indian mind began to stop to think. There was a small but general awakening among different stakeholders in the national economy, which started with the exposure of the Enron power project in Dabhol in Maharashtra. Section by section of the Indian economy began to wake up, with some of them realising that the nation has been misled by the articulated presentation of the idea of globalisation in its West-centric formulation. Even then the Indian accounting profession did not realise that it has been caught in a quicksand. This is despite the fact that even before any other profession was opened in India the accounting profession had been opened to MAFs in India before the eyes of the Indian Chartered Accountants. It was only around the close of the last decade that some enlightened CAs began critiquing the model of one-way traffic, West-centric globalisation of the accounting profession in India and the disastrous consequences of such model.

This process slowly evolved by extensive discussions meetings and interactions among thousands of Chartered Accountants particularly in the southern part of India. The result was the birth of the Chartered Accountants Action Committee for Level Playing Field at Chennai. The first convention of the CAAC was held on September 1, 2002, when for the first time over 400 chartered accountants came together to deliberate on the issues arising on the illegitimate entry of the MAFs in India. Some committed CAs decided to pursue the national agenda implicit in the CAAC and began touring different parts of the country. They addressed over 50 meetings and conventions of CAs in over 25 locations. They also had occasion to interact with businessmen and policy makers as well as the media at different places in the country. In the process they found an amazing degree of ignorance and lack of awareness everywhere about both the state of the national accounting profession as well as the illicit entry of the MAFs. They were also surprised by the complete lack of awareness about the MAFs and their methods. The different aspects and dimensions of the movement is covered and reasonably updated in the website of the CAAC, http://www.ca-actioncommittee.org.

All empirical evidence about the impact of the entry of the MAFs on the different stake holders in the Indian economy, and the empirical evidence about the level of understanding and knowledge of the most affected stake holder, namely CA profession, also pointed to the need of a reliable material to create proper understanding about the MAFs and about the causes and consequences of their entry and about the GATS and the WTO and all other related aspects. It was therefore felt that a White Paper on the MAFs and also on the consequences of their entry into India would have to be brought out in the interests of the CA profession in India and also in the larger national interest and in the interest of transparency.

In order to create proper awareness and understanding about the issues and the causes and consequences of the entry of the MAFs a group of CAs led by Mr B.S. Raghavan, a retired civil servant, was constituted by the CA Action Committee in 2002. The core idea of the group was to gather relevant material about the MAFs and to come out with a White Paper. In fact, the initial thoughts on the White Paper emerged when the attention of the CA Action Committee was drawn to the series of articles written by Mr B.S. Raghavan on the questionable practices of MAFs in a well-known economic daily in India. Convinced that a White Paper was necessary in the larger interest of the accounting profession as well as in the national interest, CAAC felt that, in order that the preparation of the White Paper and its content should not be subject to any unintended bias, Mr. B.S. Raghavan, a professional from outside the rank of the Chartered Accountants, would be the appropriate person to head the group to prepare the White Paper. Incidentally, he is also one of the advisors of the CAAC from its conception. The other members of the group, all of them Chartered Accountants, are: Mr S. Gurumurthy, who is also a well-known investigative journalist, Mr. M.R. Venkatesh, Mr. P.S. Prabhakar & Mr R.G. Rajan. After meticulous study lasting for over 6 months the group has come out with this White Paper.

This White Paper has been divided into 12 chapters. The first chapter, the earlier one, gives the background to the formation of the CAAC and how the need and the necessity for this White Paper was perceived. The contents of the other chapters are summarised as under:

CHAPTER II

GLOBAL FINANCIAL ARCHITECTURE - EVOLUTION OF THE COMPLEX FINANCIAL SYSTEM, THE EMERGENCE OF THE FINANCIAL PROFESSIONAL AND POWERFUL MAFs

CHAPTER III

MAFs: THEIR HISTORY, EVOLUTION, OWNERSHIP AND THEIR PRESENT STATE IN BRIEF

CHAPTER IV

THE EVOLUTION AND STRUCTURE OF THE INDIAN CA PROFESSION, ITS REGULATORY MECHANISM AND CONTROL.

CHAPTER V

THE ENTRY OF MAFs IN INDIA AFTER THE ONSET OF LIBERALISATION AND GLOBALISATION, AND ITS CONSEQUENCES TO THE PROFESSION AND THE NATION

CHAPTER VI

THE ISSUE OF LEVEL PLAYING FIELD FOR INDIAN CAs, IN THE CONTEXT OF THE STRUCTURE OF THE INDIAN CA FIRMS, THE BILATERAL RECIPROCITY AND FURTHER IN THE CONTEXT OF THE MULTILATERAL GATS

CHAPTER VII

THE PHILOSOPHY, CHARACTER, WORLD VIEW, GOALS OF MAFs: THEIR STRATEGIES AND METHODS; THE APPREHENSIONS ABOUT THEM; THEIR GENERAL IMAGE IN THE WEST

CHAPTER VIII

THE TRACK RECORD INDIVIDUAL MAFs -- A CONTINUING STORY OF COMPLICITY IN CORPORATE WRONGS TO ASSISTING AND PLANNING WRONGS:

CHAPTER IX

MAFs IN INDIA AND THE INDIAN CA PROFESSION -- A STUDY IN CONTRAST

CHAPTER X

AN ILLUSTRATION OF THE PUBLIC OUTCRY AGAISNT THE MAFs IN THE WEST, AS CONTRASTED WITH HOW THEY ARE CELEBRATED IN INDIA.

CHAPTER XI

THE ROLE OF THE GOVERNMENT, MEDIA, CORPORATES, AND ICAI AND HOW IT HAS AFFECTED THE INDIAN CA PROFESSION

CHAPTER XII

WHAT SHOULD THE INDIAN CAs DO?

A FINAL WORD

CHAPTER II:

GLOBAL FINANCIAL ARCHITECTURE

EVOLUTION OF THE COMPLEX FINANCIAL SYSTEM, THE EMERGENCE OF THE FINANCIAL PROFESSIONAL AND POWERFUL MAFs

THE POWER OF VIRTUAL FINANCE

It is necessary to get a macro view of how the global financial architecture has evolved in the last few decades since 1971 and how the complex global financial system has enormously enhanced the role and power of the accounting profession particularly with the unprecedented expansion of the equity market and also the financial market and the different financial instruments evolving from time to time. The sheer size of the virtual financial market which outnumbers the real economic transactions by over 100 times gives a mind boggling influence to those who operate the financial market and those who arbiter its rules and instruments. The single most critical element of the finance led globalisation is the accounting profession. The west has attempted to keep the global finance under its control through the rules, personnel and institutions by which it is operated. Consequently they also have refused to open this sector to foreign players. This is where the accounting profession and the different functions performed by the accounting professionals emerge as the critical factor.

No country which is unfamiliar with the way the global financial maze functions can succeed in deciphering and demystifying the process of globalisation. Unless a nation is able to decipher and demystify the concept and practice of globalisation it will be difficult for that nation to handle the difficult global game. This is where the accounting profession of a nation emerges as the critical factor to decipher the concept of globalisation driven by virtual finance to enable the nation to handle it with success. It is important at this stage to analyse how central the accounting profession is to a nation in facing up to the challenge of global economic game which is driven by global finance. Therefore it is necessary to understand the structure of global finance and how it has evolved as a complex architecture and also how important it is for a nation to handle it skilfully to navigate itself.

This understanding is inevitable to bring home how critical it is for a nation, and particularly a nation like India, which is an emerging power in global economy, to develop the national accounting profession not only as the main force in the country to handle the game of global finance, but also as a global power to protect and advance the larger national interest at the global level. This historic background is necessary to appreciate how with the evolution of the present global financial order which drives the entire process of globalisation, the role of the financial professional, namely, the accounting professionals in the main, has become critical. Any country which commands a large pool of accounting professional talent will have high competitive advantage.

Given the Indian competence in the accounting profession, India should have natural advantage. But this is precisely why the MAFs intervened as India opened up and have virtually denied that advantage to Indian accounting profession. This calls for an understanding as to how the accounting profession is intimately connected to the global financial architecture and how the importance and criticality of the accounting

profession which not merely supplies a large pool of financial professional to manage this global financial architecture, but also undertakes attestation and certification work on behalf of the investors, has increased enormously in the last three decades. This is demonstrated by the fact that the MAFs in particular and the accounting profession in general, as we will see later, emerged as financial consultants to both business and the state, from around the time that the global financial game changed its emphasis to virtual finance. This also resulted in the MAFs getting on the ladder of consultancy as the core of their profession, with audit and accounts as the marginal areas. This development was swift and the change was total.

THE EVOLUTION

This requires some historic reference to the developments in the global financial architecture since World War II. The post War reconstruction of the world through the Breton Woods conference in 1948 postulated that money being basically a de-stabiliser should be kept under watch and check. This led to the formation of the World Bank and the IMF and the creation of a global financial system in which each participating Government guaranteed to exchange its own currency on demand for US Dollars at a fixed rate. In turn the US Government guaranteed to exchange Dollars on demand gold at a rate of at a rate of 35 USD per ounce of gold. This effectively placed all the currencies on indirect gold standard, backed by the US gold reserves. Governments thus came to accept US Dollars as gold deposit certificates and chose to hold their international foreign exchange reserves in Dollars rather in gold. This worked well for over two decades. There was hardly a financial crisis during this period. This was the most stable period in the global economy.

But this arrangement was based on the assumption that the US economy would always remain strong enough to support the dollar. But the cost of the cold war and the involvement of the US Vietnam war considerably weakened the faith of the rest of the world in the dollar as the reference point of global finance. A situation was developing in which there could be a run on the dollar with countries and investors holding dollars surrendering the dollar and asking for gold in return. To pre-empt such a danger the US President, Richard Nixon, removed the convertibility of the Dollar to gold in August 1971. This completely debased the very structure of global finance conceived by Breton woods meet. After these developments, the Gold-Dollar parity of 35 Dollars to an ounce of gold, shot through the roof to end at over 300 Dollars to an ounce of gold within the next few years. It meant that the investment in dollars which the world had made became worth only 10% of their original value. In the process the world had inevitably got hooked to the dollar as the global currency by virtue of the rules adopted earlier. With the fixed exchange rate gone, floating exchange mechanism replaced the old structure. With the result the global financial architecture slipped into the very danger of destabilising money mechanism which the Breton woods philosophy and structure endeavoured to avoid and in fact succeeded in avoiding for over two decades.

THE DOLLAR GAME

Thus began the dollar game. It requires some understanding of this game to more fully appreciate the global financial architecture as it operates today. After the currencies were floated against one another with no single reference point, the US began to manipulate the new financial floating exchange architecture to ensure that the dollar reserves, which had

accumulated in the hands of the world, were brought under control. Thus was born what was known as the petro-dollars. By using its political clout with the OPEC, the global oil cartel which had its blessings, the US persuaded them to a disproportionate increase the prices of the Crude. This was known as the first oil shock in the 70's. As against the cost of production of a barrel of crude approximately at 3 USD in Saudi Arabia, the international selling price was about 25 USD. This sucked the extra Dollars stocks in over a hundred countries into the hands of these 10 OPEC members. The dollars thus sucked by the OPEC countries could not be invested anywhere except the US, as no other country could absorb that investment. So the petro dollars were invested into the US treasury and other bonds by these OPEC members as long-term investments at sometimes less than 1% per annum. This investment continued to fuel the growth of US. This export of dollars to finance its imports and sucking it back into the US economy through treasury bonds and later also through equity market was made possible because of the inevitable need for a global currency to conduct global trade, a position which the dollar could only fill because of the historical advantage the US enjoyed.

With declining savings and excessive consumer borrowings, the US is being forced to borrow more and more in the global market to sustain its economy. The excessive consumption by US which incidentally drives the global economy today is causing huge trade deficit which at present is over $550 billions. [The figure forecast for the year 2003 is $587 billions] If the US does not consume then the world goes into a recession. Thus by its capacity for consumption, the US has emerged as the engine for the world's economy. To this extent American consumption translates into economic drive of the world as much as a reduction in American consumption would translate into a global recession. But with the family savings in the US virtually confined to the Asians and Hispanics, and the rest of the Americans borrowing heavily for their consumption, the US in turn borrows heavily in the global market to fund its consumption. This leads to the US being the largest investment destination for the rest of the world which accumulates dollars by selling goods and services to the US. But this investment by the rest of the world into US does not result in creation of production capacities like how FDI in other countries does, but it largely finances local consumption.

Thus significant amount of savings of the rest of the world in the form of their foreign exchange reserve are invested into the US. Thus the savings of the rest of the world, from countries like China, Japan and even India, whether in the form of FDI or loan is once again directed into the US. Thus the US has emerged as the single largest debtor nation of the world. It continues to borrow at over 75 Billions every month. **At approximately 5 Trillion Dollars the US Debts far exceeds the combined debts of all other nations put together.** Mr. Alan Greenspan, the Federal Reserve Chief has expressed his discomfort in no uncertain terms on this level borrowing of America. The best example of how the global finance translates into the exporters to the US funding the US consumption is like the shop keepers financing their customers to buy from their shops. If they do not, the sale in the shop will stop. If they did, they are merely funding the consumption of their clients.

This is how the world is caught in this dollar game. A collapse of the US economy or the Dollar could mean the collapse of the world economy itself. That explains why countries like Japan keep financing the US and thereby maintaining their exports to the US to sustain their own economy. This is true of most nations

outside Europe. . The emergence of the Euro as an alternative medium of global finance and shift of the global finance to the Euro pole is a distinct possibility in future. But as the situation stands at present, the dollar game still continues. Even though the reference to the US may appear to be superfluous considering the scope of this White Paper, since the global financial order is today powered by the US consumption and as a result the dollar has emerged as the principal arbiter of the global financial and trade order, it is considered necessary to make a reference to the US consumption through borrowing from outside US as a relevant phenomenon which should be integrated in understanding how the global financial order operates, particularly from around 1971.

GLOBAL TRADE AND CURRENCY TRADE

The emergence of floating exchange rates resulted in the emergence of global currency trade and the expansion of it into derivatives market. The derivative trading which used to be in the region of $18 billion a day in 1978 rose to over $1 trillion a day in 1990 and to nearly $2 trillions a day to day. As against this, the actual trade in goods and services for a whole year now is about $7 trillions.

The global trade in goods and services is about USD 20-25 billions per day. But the global financial transactions, through actual money transactions and money instruments including derivatives, amounted to over USD 2.0 trillions a day. This has led to a complete disconnect between the global financial system and the global production mechanism. The production sector has been rendered less relevant and marginalized, has to reckon with this global financial order. Global trade heavily depends on this financial system as the engine, which in turn by its very nature causes currency instability upsetting the apple cart of free trade. With the result during the last decade alone there has been over 70 financial crisis in the world which has set many nations growth back by decades, and some, in South America, beyond repair.

The rationale of the global financial system is that virtual money in the form of market capitalisation of the stock markets in OECD nations is attracting the actual money of the rest of the world. The US leads in exchanging its virtual money for the actual money invested by the rest of the world. The rest of the world including Japan is inevitably a party to this game as the fundamental basis of this game is the US consumption which supports the pre-eminence of the US as the chief drive of the global economy.

The transaction between virtual money and actual money is facilitated by the medium of the derivative market. Similarly the transaction between the trade and production on the one hand and finance on the other is mediated by derivatives. This derivative market is controlled by the financial institutions conceived and evolved in the West which has become the global financial architecture. This global financial architecture is controlled and operated by banks, and investment banks, mutual funds and other financial intermediaries, manned in the main by accounting talent developed by the western countries and the MAFs controlled by them. The money managers who carry out these transactions stake their reputation and careers on making that money grow at a rate greater than the prevailing market rate and that of their nearest competitors. This growth depends on the ability to ceaselessly increase the value of the financial "assets" that is being traded. The process tends to feed on itself. As the price of "assets" rises, more speculators are sucked into these transactions and the prices of these "assets" continue to increase attracting more people - till of course the bubble bursts, when because of its

size and devastating effects other financial institutions shall rush to prevent the "contagion effect". It is always a win-win situation for these speculators. When they succeed, they make their money and when they lose, they lose others' money.

The fact is that many major corporations, banks and even some Governments have became major players in the derivative players in this speculative game. The profits from the derivatives are far in excess of the profits from operations and in some cases, a convenient method to camouflage the loss from operations. In fact, certain global banks have become huge speculators themselves by focusing on this and marginalizing their traditional operations. These speculators constantly invent and innovate for newer and newer instruments. The reach of these "financial gamblers" is not restricted to any specific commodity or stock markets alone. These speculators who thrive on volatility on which speculation depends do not favour fixed exchange rates.

Allen Metzler, one of the world's leading authorities on Central banks and monetary policies estimated in 1993 that if the world's central bankers agreed among themselves to a coordinated action to protect a currency from a speculative attack they may able to muster 14 billion USD, a mere drop as compared to the staggering amount of 800 billion plus USD then (today this exceeds USD 2 trillion per day) that the speculators trade daily. In fact fair value of currencies [as determined by purchasing power parity and relative movements in productivity] 'has tended to exert a very feeble influence in foreign exchange' according to the head of global research at State Street, the Boston based investment bank [Business Standard, June 5, 2003] Thus it is not the real value of the currency but their speculative value that prevails, as 'the gravitational pull exerted by the real value is extremely weak. This phenomenon which developed subsequently has totally altered the functional basis of the global economy which revolves more around speculation, than around production or productivity or the real economy.

Mr. Akio Morita, the founder- chairman of Sony Corporation pointed out in a letter to the group 7 leaders when they met at Tokyo in the year 1993 that while the business and Governments of different countries have control over manufacturing and trading efficiency of their national economy, they have no control over the value of their national currencies determined in relation to other countries. As a hypothetical example he said that even though for instance the Japanese economy might grow in physical terms by 10%, if the value of the Yen falls by 12%, the net effect would be that the economy fell by 2% and not grown by 10%. He said that the speculative derivative trade has completely overtaken the global economy and has emerged as its chief drive. He hinted that the solution lies in creating a single global currency under unified global governance, which might be the only viable way but conceded that it was wishful thinking.

The currency trading left the nations at the mercy of the speculative money that moves around in the world in split-seconds from country to country and currency to currency leaving behind a trail of financial instability that can be cured only by a fresh bout of financial engineering. The IMF-World Bank combine immediately step in for a bail out package with a set of conditions that would favour this system. In fact over the past two decades there have been at-least twenty countries that have faced this major financial instability, the notable one being the East Asian Financial crisis. Floating currencies and derivatives and speculation, are the root causes of this mess. But this mess is a reality today and it cannot be wished away. A

nation has to handle it if it has to handle the process of globalisation successfully. How long this process is sustainable is a matter of speculation. But so long as a nation participates or it is compelled to participate in the process of globalisation, it has to develop the skill to handle this unruly horse called the world of finance, which is nothing but a world of speculative derivatives, or in other words, the world of speculation. This destabilising force of money is precisely what Maynard Keynes wanted kept under check by instituting the IMF and the World Bank as originally conceived, but this is what the world economic leadership failed to do landing the world in unending instability. But a country which wants to handle globalisation and global forces successfully will have to develop its own skill and the competence to handle this unruly horse. This is where the national profession of accountancy becomes the most critical factor.

THE EMERGENCE OF THE FINANCE PROFESSIONAL

This entire space of trans-national financial transactions, instruments, institutions, systems-procedures, relations, disputes arbitration between the participants in the financial trade, and the entire range of financial services, are the home terrain of professional accountants.

From what Akio Morita said, it is evident that not technology, not production, not efficiency, but the speculative currency movement in the form of e-transfers and derivatives, which decisively influences the global and therefore the national economies. This is where the ever expanding and highly influential role of the finance-accounting-audit- profession comes in. It is the accountants who handle this enormously powerful money machine, by creating and modifying the different, new financial instruments, forecast the movement of values of the stocks and other financial instruments operate the entire financial market, which is the most decisive influence on the global and national economies. Thus the Multinational finance-accounting-audit firms, the MAFs, have developed enormous clout in the global financial market and with the global banks and other financial institutions.

This is the background for the emergence of speculative finance as the chief arbiter of global trade and production. Countries which have developed the institutions and skills to handle this speculative derivatives and the mechanism to generate virtual money are able to control the levers of globalisation. The institutions and skills to handle this financial architecture are the sine qua non for handling the process of globalisation. The accounting profession generates and supplies the skill needed to handle this global financial architecture. This is where the real control is. That is the capacity to control and handle the global financial architecture. This is where the financial professional has emerged as the principal player in the entire process of globalisation. Unless a nation develops the skill to handle the difficult and destabilising influence of derivatives and the financial institutions and the ever-growing new financial instruments and products, it will never be able to handle successfully the forces of globalisation. The professional who handle this high skill area are the mainly the CAs. That is why the US which has emerged the principal financial engine of the world thank to the historic advantage that the dollar has come to command has about 400000 CPAs, which translates to 1.75 CPAs per thousand population which is approximately equal to the number of doctors per thousand population. From this one comparison one can understand the critical importance that this financial profession commands.

Being third only in the number of accounting professional population, with the US first and the UK next and fast emerging to become number two overtaking the UK, and with its large pool of highly skilled and equally competent army of chartered accountants the Indian Accounting profession has the potential to emerge as a global player to handle this critical area of global finance. The professional CA firms are the intermediators in this critical area of global finance and the globally linked national finance as it is they who interface the different actors in the game to this world of finance. But to emerge as the global power, the Indian CAs must emerge as a power at the national level. A profession which has lost out in its own terrain cannot emerge at the global level. This is the crux of the issue. The way the Indian system has shaped the regime for the accounting profession in India does not seem to factor in the potential of the Indian CAs to emerge as a global player and to exploit the potential. This is a loss to India as well as to the world. Take the Indian medical profession. The way the Indian medical professionals have emerged as national players in the western countries, the accounting professionals can never become, as the accounting professionals do not directly deal with the people; they deal with the financial and corporate system which are accessed by the MAFs through the nexus explained herein. So unless a proper regime is put in place the potentialities of the Indian accounting profession cannot be exploited to the advantage of the nation and to the world at large.

THE NEXUS

As the world of finance is structured to day, there is a nexus which preserves the lead of the developed nations, particularly the west, over the rest. The attempt to stifle the Indian CA profession within India is calculated to de-risk the possibility of the competent Indian CA profession from gaining knowledge and experience in the liberalised Indian economy and becoming a challenge to the MAFs at the global level and instead it remains as the workhorse of the MAFs rather than CAs becoming and being their own masters. The nexus which maintains the lead of the west over the rest ensures that this process which de-risks the West against the competition from the Indian CAs is continued. Let us see how the nexus works.

Financial analysts, bankers, merchant bankers, fund managers, economists, rating agencies, consultants, stock and currency traders, and multilateral funding agencies are aligned with one another in this global trading mechanism with a global reach. But they need an associate, and a pliable one at that, to certify and sanctify their deeds. So, they appoint the MAF-- one amongst the big four-- with whom they have developed a level of comfort and who have also with a global reach. This is intended to give them what is a deliberately cultivated credibility to cover up all acts of their omissions and commissions. Transactions are legitimised through audits by these firms and the audited figures are used for furthering the interests of this alliance. The auditors would ratify projections as well as actual workings of their partners or their respective clients to ensure that the International Banks, lending agencies and others would do business with the hapless victim. Any financial slip-up could be sanctified during audits, if audited by these firms. Appointments of auditors are on quid pro quo basis with their alliance partners and they in turn do everything to keep their partners satisfied.

In this nexus, others follow the entry of one. As global finance is generally incomprehensible for normal investors and businessmen, particularly in countries like India which have not been familiar with this game having not played this game for decades because of the controlled

economy, they look up to the 'recommended' auditors, with a Brand image, 'for assurance' little realising that they are a party to this global loot. Mere figures so attested by the auditors do become "audited" and the morally indefensible transactions attain the aura of legitimacy. How can, then, their ethics and morals, be not equally suspect?

Signal service has been rendered by Unison a public service union representing over 1.3 millions members from different services and the largest trade union in UK by bringing out how the Big Five [now four] accounting firms influence and profit from privatisation policy. The summary of the report of Unison based on the research work and advice of the Health Policy and Health Services Research Unit at University of London, states as under:

"UNISON, the public service union, has produced this report to expose the vested interests of the five largest accountancy firms that now profit from the industry that has grown up around the private finance initiative (PFI) and public private partnerships (PPPs).

The government has used two reports to defend PFI, the Andersen Report (Value for Money Drivers in the Private Finance Initiative, January 2000) and the PricewaterhouseCoopers Report (Public Private Partnerships: A clearer View, October 2001). The reports lack hard evidence and UNISON's investigation has revealed that both Andersen, PwC and the other three major accountancy firms are themselves beneficiaries of PFI policies and may find it hard to be impartial.

The Big Five accountancy firms act as auditors to both private and public sectors but increasingly have developed into management consultancy which now provides half of their profits. This has raised concerns as to whether auditors who also sell other services to their clients can remain independent.

Much of the consultancy work is on privatization. At the same time, the Big Five have been at the heart of government policy development on privatization acting as secondees to government departments; developing the value for money tests used for PFI projects; and producing reports for the government on the benefits of PFI and PPPs.

Public alarm is growing at the potential conflicts of interest of the different roles taken on by the Big Five. When UNISON examined PFI schemes where the Big Five acted as financial advisers, we found that in 45 cases the advisor to the public sector was also the auditor to atleast one of the consortium members or bidders on the project."

The UNISON has also produced another report 'How the Big Four accountancy firms have PFI [Private Finance Initiative] under their thumbs' exposing the nexus between the world of finance and the big four accounting firms. These the two reports relevant for understanding the dubious role of the Big Four in manipulating divestment and privatisation policies will bring out the hidden hand that operates the apparent policies of the Governments formulated in public interest. These reports also bring out the nexus between the world of finance comprising the investment bankers who promote the Private Finance Initiative [PFI] and Public Private Partnerships [PPPs] for promoting privatisation.

Now let us see how this global financial architecture is operated by the financial intermediaries in un-stated joint venture with MAFs, which monopolise the entire space at the global level in strategic association with global financial intermediaries. And how they have structured their operations to continue their nexus with global finance and in the process compromise their professional character to the detriment of the investors and the general

economy of different countries. Also how considering that if there is any one country which can challenge their superiority it is India and the only professionals who can do it are the Indian CAs, they de-risk themselves by ensuring that there is no Indian challenge to their superiority. In addition, how they hide behind a highly skilled brand building exercise and conceal the enormous slip in their standards and quality, ethics and morality. Let us also see how the Indian CA profession which has not been allowed to grow out of its controlled economy mind-set because of denial of opportunities to handle the process of liberalisation and globalisation since 1991, and the unrestricted entry of the MAFs elbowing out the Indian CAs altogether.

How international financial interests prevent national alternatives and how the national will successfully innovate alternatives - the Yugoslavian example

In the context of how the global financial interests led by the IMF and the World Bank, which are the principal promoters of the western financial models, institutions, rules and instruments, which need the MAFs as the tools to work with, it is important at this stage to look at the Yugoslavian example to compare how the global forces work to dominate nations and how national will resists such domination. This reference to Yugoslavia may, on a superficial examination, seem a little out of place in the context of this document, but it is intrinsically linked to the psychology which rationalises and welcomes the presence of the MAFs as superior problem solvers for the non-western nations.

The illustration at hand was the financial crisis which over took Yugoslavia in early 1990s. The hyper inflation which overtook Yugoslavia topped 3 million percent in the year 1993-yes, three million percent, higher than the historic inflation recorded in Germany after the World War I. The highly nationalist Yugoslavian Government, on the advice of a Yugoslavian economist Dragoslav Avromovic, preferred to reject the IMF-World Bank commended restructuring package and decided to follow an innovative national strategy to tackle the crisis, an unprecedented one in world economic history. The national alternative proposed by Dragoslav was to issue a new Super-Dinar firmly linked to the Deutsche Mark currency stock with the Government as the foreign exchange reserves and made fully convertible, to circulate side by side with the existing Yugoslav Dinar to take care of the external sector stability and an internal structural adjustment programme based on national resources and consistent with national situation. The results were remarkable. The inflation came down to nil, repeat nil, in the first week of the introduction of the Super-Dinar. Further, instead of flight of capital through the Super-Dinar, the foreign exchange reserves increased by 60% in the first three months, with people rushing to convert their foreign currency accounts in terms of the new Super-Dinar. The International Commission on Peace and Food referred to this remarkable achievement as the alternative strategy in Yugoslavia, which is reproduced.

Alternative Strategy in Yugoslavia

The extreme damage wrought by the economic reform program in these countries over the past half decade necessitates an urgent Deutsche Mark search for more viable alternatives, a search that has been retarded until now by the widely held view that none exists. Very recent events in Yugoslavia suggest that even in the limited area of economic stabilization and adjustments, an alternative strategy can be more successful. Although the long term impact of the Yugoslav experiment is as yet unknown, its remarkably positive initial results merit serious consideration.

The economic disorder that accompanied recent political developments in Yugoslavia resulted in an explosive increase in prices of more than 100 percent per month in 1992. Despite efforts to control monetary expansion, hyperinflation exceeded three million percent in 1993--far higher than the inflation rate reached in Germany following World War I and, quite probably, the highest rate in recorded history. The price spiral was accompanied by a steep fall in real purchasing power by as much as 75 percent. The budget deficit increased rapidly as the value of Government tax revenues fell further and further behind the rising cost in current terms of its expenditures, due to the time lag between tax declaration, collection and expenditure in a period of very rapid price increases.

In January 1994, the Government embarked on a comprehensive monetary reconstruction program to achieve price and exchange rate stability; to remove administrative controls over production, investment, prices, salaries, and interest rates; to re-establish the role of the central bank in monetary stability; to reorganize public finances through an efficient tax system, including more efficient tax collection and better coverage of the large "gray" economy; to reduce Government administrative and defence expenditure to the maximum possible extent; to maintain price supports for important agricultural commodities as an incentive for production; to stimulate economic activities of private, cooperative and public sector enterprises through equal access to credit and Government facilities; and to encourage the take-over of sick firms by stronger, more efficient companies. At the same time, the program was intended to mitigate the harsher effects of shock therapy programs on the working class and fixed incomes pensioners by providing free scope for collective bargaining, enforcement of a minimum wage policy and a social safety net for the unemployed.

It was recognized from the outset that stability of the currency was an absolute precondition for the success of the reform program, which depended in turn on the firmness and consistency with which the program was implemented. The central element of the program was the introduction of a new currency, the 'super-dinar', in parallel to the existing currency, but without demonetizing or confiscating it. Inspired by an experiment in the Soviet Union during the 1920s, the value of the new currency was tied to that of the Deutsche Mark and made fully convertible without restriction. Based on the country's very limited foreign currency reserves, new issues of the currency were to be utilized primarily to inject real purchasing power into the economy, revive demand and stimulate production, while covering the Government's budget deficit during an initial six month period needed for sufficient recovery. In this way the foreign currency and gold reserves were used as a buffer to moderate contraction of the money supply and avoid the shock usually accompanying such efforts. Issuing of old dinars was stopped, but it remained in circulation as legal tender. An interest rate of six percent was established for the super-dinar--the first real, positive interest rate in years--to make holding the new currency an attractive alternative to hoarding goods or foreign exchange. It had been widely anticipated by foreign experts that this strategy would result in an immediate run on the country's foreign reserves and thereby a collapse of the new currency's foundation.

Contrary to expectations, the initial months of the program have yielded spectacular results. Inflation fell to zero percent in the first week after issuance of the new currency and remained below one percent during the first five months.

Instead of a massive outflow of foreign currency through conversion of super-dinars, people have rushed to cash in their foreign currency, resulting in a 60 percent increase in the nation's reserves during the first three months. One of the most significant features of the program has been its fair distribution of benefits and low social cost to the population. In contrast with the widespread outrage felt by Russian citizens over repeated episodes of demonetization and confiscation of household savings, the Yugoslav people have enthusiastically accepted the new currency as representative of a new deal for the poor and the working class. In addition, instead of the severe contraction of output experienced elsewhere, production rose by more than 100 percent during the first five months, stimulating an increase in employment and demand for new investment. Real tax revenues have increased significantly.

The astonishing initial success of the program can be attributed to its balance and comprehensiveness and to the following specific features: the Government's recognition that stabilization was absolutely essential to economic recovery; the widespread public support for the program, which was in large part due to the efforts to protect weaker sections from its harshest effects; the simultaneous relaxation of controls on industry; support for a natural rather than a forced process of privatization, based on the specific circumstances of each firm rather than on ideology; continued price supports for agriculture and a minimum wage for labor, which are crucial for maintaining food supplies and social stability; and rejection of import liberalization in order to protect domestic manufacturing against a major shock during the initial period of recovery. ***Possibly the greatest strength of the Yugoslav program is that it was of necessity conceived by people within the country rather than by foreign experts, and depended entirely on domestic resources and capabilities for its accomplishment, rather than on pleas for foreign assistance. Self-reliance released the creativity, generated the determination and mobilized all available resources to make the transition successful.***

It is too early to predict the eventual outcome in Yugoslavia, subject as it is to extraordinary external constraints on public policy. However, the initial evidence is sufficient to demonstrate that alternative approaches can and must be fashioned which are more comprehensive in scope, more balanced in implementation, more pragmatic in conception and less influenced by extreme ideological viewpoints. It is likely that further study of the Yugoslav model will reveal important applications not only for countries suffering from hyperinflation or the effects of radical transition, but for those carrying out more modest programs of economic reform.

The most crucial observation in the report is: Possibly the greatest strength of the Yugoslav program is that it was of necessity conceived by people within the country rather than by foreign experts, and depended entirely on domestic resources and capabilities for its accomplishment, rather than on pleas for foreign assistance. Self-reliance released the creativity, generated the determination and mobilized all available resources to make the transition successful. Contrast this with the so-called shock treatment in Russia in the form of a structural adjustment programme twice conceived by the external world financial experts for Russia. This led to widespread chaos, confiscation of local savings and currencies and external crisis, leaving behind a weakened economy. The Yugoslavian Government rejected this very advice. A tail piece: the formula Dragslov suggested to Yugoslavia was the formula which a Russian economist had suggested to Russia but rejected by the Russian

Government which went along with the external financial experts' advice. This is a demonstration of what local minds knowing local situations, assessing local resources and understanding local psychology can do.

But none of the World Bank or IMF publications would even whisper about this great alternative success. None of the western economic journals would talk about it loudly. For it is not according to their prescription. It is actually in defiance of them. How could any one solve national problems without solution prescribed by the West. So this great and successful experiment is comparatively unknown in world economic circles. The information about this extraordinary instance of a national alternative succeeding in the face of a global presumption that only the Western economic institutions hold key to the solutions of global and national problems is so scanty, that the authors of this White Paper had to seek the details from a global financial consultant, Garry Jacobs, who sent the above information. This is the letter Garry Jacobs wrote to one of the members of the CAAC group on this White Paper :

"I enclose an excerpt from the report of the International Commission on Peace and Food in which we have cited Dragoslav Avramovic's work in Yugoslavia. Drag was a contributor to the report. The full text of the report is available at icpd.org, but this excerpt is the only reference to Yugoslavia. I do not believe I have any further papers back in California, but if you are looking for more I will ask my office to search. Unfortunately, Drag passed away two years ago so he is not available to consult and there was relatively little international coverage of his remarkable achievement at the time for political reasons. Perhaps you will find more recent references to it on the web.

Regards

Garry"

Garry Jacobs's words, 'there is very little coverage of his [Drag's] remarkable achievement at the time for political reasons' are significant in more than one way. It is important to the Indian nation when it has to assess the advice given to it from outside the country - it can follow the Russian example or the Yugoslavian example. It is as much relevant to the Indian CA community.

CHAPTER III

MAFs: THEIR HISTORY, EVOLUTION, OWNERSHIP AND THEIR PRESENT STATE IN BRIEF

The growth in the power and influence and in the volume of business of the MAFs is directly relatable to the developments in global finance since 1971. The unprecedented growth of money, particularly virtual money in the form of market capitalisation and in the form of derivative build-up, from $18 billion dollars a day to nearly $ 2 trillions a day now, necessarily brought about a nexus between the world of finance and the accounting profession. The global scale of operations also necessitated a global size accounting firms. So the growth of the MAFs was aligned to the growth of the global finance as the principal determinant of the global trade and investment. Now let us examine, in this back ground, the history of the four MAFs, now known as the BIG FOUR., namely, KPMG, ERNST & YOUNG, DELOITTE, TOUCHE & TOHMATSU, and PRICEWATERHOUSE COOPERS. What was once Big 6, became Big 5 with Pricewaterhouse and Coopers and Lybrand merging into Price Water house Coopers, and later with the collapse of Arthur Anderson, into Big 4. Let us now look into their individual history.

KPMG

KPMG was formed in 1987 with the merger of Peat Marwick International (PMI) and Klynveld Main Goerdeler (KMG) and their individual member firms. Spanning three centuries, the organization's history can be traced through the names of its principal founding members - whose initials form the name "KPMG."

K stands for Klynveld. Piet Klynveld founded the accounting firm Klynveld Kraayenhof & Co. in Amsterdam in 1917.

P is for Peat. William Barclay Peat founded the accounting firm William Barclay Peat & Co. in London in 1870.

M stands for Marwick. James Marwick founded the accounting firm Marwick, Mitchell & Co. with Roger Mitchell in New York City in 1897.

G is for Goerdeler. Dr. Reinhard Goerdeler was for many years chairman of Deutsche Treuhand-Gesellschaft and later chairman of KPMG. He is credited with laying much of the groundwork for the KMG merger.

In 1911, William Barclay Peat & Co. and Marwick Mitchell & Co. joined forces to form what would later be known as Peat Marwick International (PMI), a worldwide network of accounting and consulting firms.

In 1979, Klynveld joined forces with Deutsche Treuhand-Gesellschaft and the international professional services firm McLintock Main Lafrentz to form Klynveld Main Goerdeler (KMG).

In 1987, PMI and KMG and their member firms joined forces. Today, all member firms throughout the world carry the KPMG name exclusively or include it in their national firm names.

Presently KPMG is a Swiss Verein of which all KPMG firms are members. Each member firm is a separate and independent legal entity (None is a parent, subsidiary or affiliate of another) and

each describes itself as such (e.g. "KPMG LLP", a US limited liability partnership, is a member of KPMG International or "KPMG LLP, the US member firm KPMG International"). The global billing for the year 2001 was at USD 11.70 billion.

PRICEWATERHOUSECOOPERS

PriceWaterhouseCoopers has been created by the merger of two firms - Price Waterhouse and Coopers & Lybrand - each with historical roots going back some 150 years. Set out below are some key milestones in the history of both firms.

YEAR	EVENT
1854	William Cooper establishes his own practice in London, which seven years later becomes Cooper Brothers
1865	Price, Holyland and Waterhouse join forces in partnership 1874 Name changes to Price, Waterhouse & Co.
1898	Robert H. Montgomery, William M. Lybrand, Adam A. Ross Jr. and his brother T. Edward Ross form Lybrand, Ross Brothers and Montgomery
1957	Cooper Brothers & Co (UK), McDonald, Currie and Co (Canada) and Lybrand, Ross Bros & Montgomery (US) merge to form Coopers & Lybrand
1982	PriceWaterhouse World Firm formed
1990	Coopers & Lybrand merges with PriceWaterhouse in a number of countries around the world
1998	Worldwide merger of Price Waterhouse and Coopers & Lybrand to create PriceWaterhouseCoopers

Presently, PriceWaterhouseCoopers refers to the network of the member firms of PriceWaterhouseCoopers International Limited, each of which is a separate and independent legal entity. It has presence in 142 countries and territories and employs 124000 professionals. The firm's turnover is estimated to be around USD 15 billion.

ERNST & YOUNG

Young, born in Scotland in 1863 and a graduate of Glasgow University, was privileged and soft-spoken. His interest in investments and banking eventually led him to accounting. He migrated to the United States, settled in Chicago and, in 1906, founded Arthur Young & Co.

By contrast, the outgoing Ernst, born in 1881 in the United States, in Cleveland, was basically self-made. Following high school, he worked as a bookkeeper and, four years later in 1903, joined with his brother, Theodore, to start Ernst & Ernst.

Ernst pioneered the idea that accounting information could be used to make business decisions-the forerunner of management consulting. He also was the first to advertise professional services.

Young was profoundly interested in the development of young professionals. In the 1920s he originated a staff school; in the 1930s, his firm was the first to recruit from university campuses.

Both firms were quick to enter the global marketplace. As early as 1924, they allied with prominent British firms-Young with Broads Paterson & Co., and Ernst with Whinney Smith & Whinney. In 1979, Ernst's original agreement led to the formation of Ernst & Whinney.

In 1989, the firms combined to create Ernst & Young. The new firm quickly positioned itself on the leading edge of rapid globalization, new

business technologies, and continuous business change.

Presently, E & Y International, which has a presence in over 130 countries and employs, about 110,000 employees. The firm's turnover is estimated at over USD 10 billion. We are unable to get any reliable evidence about its headquarters.

DELOITTE TOUCHE TOHMATSU

DTT is a Swiss Verein, and each of its national practices is a separate and independent legal entity. With more than 100,000 people in over 140 countries, the member firms serve over one-half of the world's largest companies, as well as large national enterprises, public institutions, and successful, fast-growing global growth companies. As far as the history of the firm is concerned its website states 'Our international name-Deloitte Touche Tohmatsu-owes its existence to leaders in our profession who, from the beginning of their professional careers, recognized the importance of a worldwide practice'. It further states 'Contact us for more information about history'.

CHAPTER IV:

THE EVOLUTION AND STRUCTURE OF THE INDIAN CA PROFESSION, ITS REGULATORY MECHANISM AND CONTROL

It is necessary at this stage to capture and contrast the structure and ethical architecture of the Indian Accounting profession with the structure and ethical liberties of the MAFs to debate how level playing field has been denied to the Indian accounting profession. The Indian accounting profession was and continues to be a product of the mixed economy practised since Indian Independence under the socialist regime. The largely insulated nature of the Indian economy did not internalise high points of the finance, equity and derivative-led dimensions of the western economies. Therefore the Indian CAs who largely operated in India, or from India except for purposes of employment were largely unfamiliar with the financial institutions and financial products familiar to the free market, except perhaps at the theoretical level, till the liberalisation and globalisation process opened up in the early 1990s. Thus liberalisation and globalisation policies of the Government adopted since 1992 were the first opportunities to the Indian CAs to acquire the experience to handle these free finance-market dimensions, institutions and products of the western economy which were being brought into the Indian economy by the process of globalisation and liberalisation. Actually the manner in which the financial liberalisation was being calibrated, and is being calibrated, it would not have been difficult for the Indian CAs to upgrade their skills and competencies to internalise the global financial practices. In fact had the country not followed the socialist model and had from the beginning adopted the policy of calibrated opening of the economy in the early stages of our independence or even a little later and had the opening not been delayed to the extent it actually happened, the Indian CAs would have developed the requisite degree of confidence and competence to global ideas practices and institutions, given the fact that some of the best minds in the country entered the accounting profession during the 1970s and 1980s. This would have been made easy by the high levels of English education prevalent in India, an advantage no other country in the world could claim or have had. But even before the Indian CAs could understand and internalise the impact of the liberalisation and globalisation policies and adjust their skill and knowledge, the RBI permitted the MAFs to enter and grab the national professional space in the areas which normally would have been the domain of the Indian CA profession. Thus had the MAFs not entered India stealthily through the RBI route and grabbed the entire professional space which had emerged from the globalisation policies, the Indian CA profession would have been the total beneficiaries of the opportunities which liberalisation and globalisation had thrown up. This would have led to change in the psychology and strategy of professional practice by the Indian CAs. They would have consolidated and networked to match the scale of the MAFs. They would have leveraged on their historic and intimate familiarity with English, and like the software professionals, could even have made impact at the global level. But with the sudden induction of the MAFs in to India, these opportunities became lost opportunity to the Indian CAs. So the Indian CA profession was

totally unprepared for such eventuality of opening of the economy. Thus thanks to uneven level playing denying them the new and lucrative opportunities, the Indian CA profession continues to remain unconsolidated, un-networked and small in size as compared to the MAFs. They not only remain small size, they are without multi-disciplinary practice because they have no business necessity or compulsion to do so with the new opportunities being monopolised almost entirely by the MAFs because of their association with global finance which ensured their unimpeded entry into India and also granted to them extra professional advantage over the Indian CAs. Had the post liberalisation regime not permitted the easy and entry unreciprocated entry of MAFs, the Institute of Chartered Accountants of India too would have acted to put in place the requisite professional rules of change to suit the emerging situation. This would have happened only if the ready-made MAF presence was not available to grab the newly emerging space. Thus neither the Indian CA profession nor the CA regulatory was given the chance to prepare themselves to handle the new avenues opening up because of the liberalisation policies of the Government. In the process the Indian CA profession became sitting ducks for the MAFs.

Now having seen briefly how the post liberalisation regime denied the Indian CAs the benefit of the new avenues that emerged and how that acted as the professional disincentive for them to change, let us see the evolution, structure and anatomy of the Indian accounting profession, in comparison to that of the MAFs.

EVOLUTION

In India, prior to 1949 the profession of accountancy in India was controlled and regulated by the Government, which subsequently vested the regulatory power in the Institute of Chartered Accountants of India through an enactment in the parliament in the year 1949, (The Chartered Accountants Act 1949). It is an act for the regulation of the profession of Chartered Accountancy.

STRUCTURE OF INDIAN CA PROFESSION - a story of denied and missed opportunities

The Indian accountancy sector mainly comprises of small and medium sized firms, the number of firms with 5 or more partners being only about 375 as on 01.04.2001 out of 42,339 firms as on that day. The Indian CA firms are regulated very heavily. Some of the regulatory features are given below.

Size distribution of CA firms as at 01.04.2001

NO OF PARTNERS	NO OF FIRMS
2	7161
3	2104
4	796
5	375
6	305
7	206
8	101
9	61
10	34
>10	52

The number of sole proprietary firms as on that day was 31144.

The structure of the Indian economy which largely consisted of small and medium enterprises determined the size of the accounting firms in India. The structure of the Indian economy is dominated by small and medium enterprises. This is evident from the fact that the corporate sector, which largely consists of SMEs itself accounts for only 14% of the Indian GDP.

The Government sector which consists of large scale units accounts for 22% of GDP. The non-agricultural non-corporate sector accounts for 39% of the economy. This shows that the structure of the Indian accounting profession follows the structure of the Indian economy. Still the Indian accounting profession could service the demands of the Indian business consistent with the economic regime in operation. Even after the change of the economic regime with the era of liberalisation and globalisation opening up the Indian accounting profession would have serviced the Indian business but for the sudden and premature induction of the MAFs into the Indian economy. Therefore in the past the national economy being insulated from the global either way, that is, both the global being denied entry into India and local being discouraged to operate outside India because of the strict currency regime, the structure of the Indian CA firms was always dominated by small firms, with very small number being relatively large, that is large in the Indian context just as some corporates in India are relatively large in India but not large on global scale. But when the liberalisation and globalisation opened up new opportunities, the Indian accounting profession which stands next only to the English and the American in numbers, was not given the calibrated opportunity which the rest of the sectors of the Indian economy including the industry and other professions were given, to evolve in skills and confidence to continue to service the Indian business. Thus the Indian accounting profession did not have the opportunity to grow consistent with the Indian business in size and confidence. Had the Indian accounting profession been treated on part with, for instance, the Indian industry, [which had had the advantage of a reasonable degree of protection, not to speak of the legal profession which had total protection] the Indian accounting profession would have grown in size and confidence in the last decade and would have even challenged the MAFs in their own terrain, namely the West, just as the Indian doctors have done. But the inadequate and thoughtless response of the Indian establishment in which one cannot exonerate the ICAI, the Indian accounting profession not only lost the initial opportunity to upgrade its confidence and consolidate itself into larger one to take advantage of the space that the globalisation provided, it also lost where no one should lose namely at home. This is in fact a national loss and also a global one, as globalising Indian firms would have brought down the transaction cost to global business by their potentially higher levels of competence and their propensity to be reasonable in their charges. Thus it is a story of denied and missed opportunities for the Indian accounting profession in the first decade of liberalisation and globalisation.

Since the Indian accounting profession was not allowed to grow relative to the size of the Indian business and also the relative to the demand for services which the entry of the MAFs in India created and demanded, they did not have the need and the compulsion to consolidate and diversity into trans-disciplinary professional areas. Even in future, it may not be rational to presume that huge number of small and medium sized business enterprises in India will gradually coalesce within the foreseeable future, unless there is a clear professional need compelled by the opportunities provided by evolving a regime in which they will have level playing field matching the advantages which the MAFs in India enjoy Therefore, the large number of small and medium accounting firms will remain the same, as it exists today, unless the regime redesigns the structure of the profession and makes it turn in tune with the demands of the new economic regime.

REGULATORY MECHANISM

The Chartered Accountants Act 1949 established a regulatory body for the Indian accounting profession in the ICAI. The ICAI was essentially a mechanism to conduct examinations to generate accounting professionals and also to regulate their discipline. It was also responsible for developing professional standards. It was designed to operate more under controlled economy conditions, and not for facing the challenges of globalisation to the accounting profession. In fact the ICAI was independent body only in a theoretical sense of the term. It was in practice largely controlled by the Government. The council of the ICAI was also based on such broad-based electoral process and its decision making was so structured to make the 30 member elected council the supreme body that it is incapable of functioning except through the slow and painful process of consensual opinion making. Such a process, as explained elsewhere herein, is not adequate to handle the problem posed by the entry of the MAFs into India.

The Chartered Accountants Act provides for in built disciplinary mechanism against professional and other misconduct of the Chartered Accountants. Commissions or omissions which constitute professional misconduct are defined in two schedules to the Chartered Accountants Act, 1949. First schedule deals with the misconduct, which has the effect generally of compromising his position as an independent person. The second schedule deals with matters relating to failure to adhere to professional standards in discharging attest function.

But the ethical and regulatory regime operating on the Indian CA profession is not contained only in the Chartered Accountants Act and the regulations. It is also contained in the Companies Act which harmonises the regulatory and the ethical regime which is contained in the Chartered Accountant Act with the requirements of corporates under the Companies Act.

The ethical and regulatory prescriptions regarding the accounting profession in the Companies Act, 1956 and the Chartered Accountants Act, 1949, include, but are not limited to, the following:

- Section 11(2) Indian Companies Act, 1956 restricts the number of partners in a partnership firm to 20 partners. Further, the Chartered Accountants Act of India restricts a Chartered Accountant firm to be either a sole proprietary or a partnership firm. Under the conjoint reading of the Indian Partnership Act, the Indian Companies Act and the Chartered Accountants Act it is clear that there is a restriction on the type of entity and number of partners within such firms.
- Further there are restrictions under the Companies Act on the acceptance on the number of Audits that a Chartered Accountant may accept.
- There are disqualifications prescribed under the Companies Act on the indebtedness of the Auditor if it exceeds Rs. 1000.
- Further the Indian Auditor is disqualified under the Companies Act if he holds shares in that company. Under the Indian Companies Act, 1956 a firm cannot be a shareholder in a company and thereby cannot control a company. This restrains Indian Professional firms from floating and thereby controlling a company, incorporated for carrying out certain activities that are not legally or technically possible to be carried out by the parent Chartered Accountant firm. These dual restrictions, one by the Companies Act that prohibits Firms from being Shareholders of a company and two, the restriction of the types

of services that can be rendered only by a firm of Chartered Accountants by the ICAI are meant to regulate the profession of accountancy and audits within India. This in effect means that in India Chartered Accountants can carry out its activities only as a Partnership firm (or as a sole proprietor) and is incapable of being a shareholder in a company - thereby control the operation of the company and use that company to circumvent the restrictions placed on it by the ICAI on the nature of service to be carried out by it.

- The Indian company law insists that only the appointment of the statutory auditors can be in the name of the firm of accountants. But the audit report and the balance sheet will have to be signed by a partner of the firm in his own name and hand, not in the name of the firm. That is to say that the responsibility of the CA is personal, not collective, not that of the firm and it will follow the CA who signs the balance sheet wherever he goes. This is the best safeguard in terms of assumption of responsibility.

Thus the regulatory regime operating on the Indian CA is more shareholder-friendly and investor-friendly than the regulatory regime prevalent elsewhere.

ETHICAL ARCHITECTURE

The ethical architecture operating on the accounting profession in India may be summarized as under:

- Indian Chartered Accountants are subjected to certain Rules and Regulations made under the Chartered Accountants Act. One of the significant restraints that the ICAI places on its members is that the Indian Chartered Accountants cannot advertise, whether in India or abroad. They cannot canvass directly or indirectly for professional assignments. They cannot make presentations to prospective clients Even there are restrictions as to how a Chartered Accountant firm should design its web site. The code of ethics extant and the regulations laid out by the ICAI do clearly lay out the restrictions placed on its members on these issues. This laudable restriction draws the line between profession and business. Between ideas and products. Between professionals and traders. Between earning fee for personal value and charging on the basis of brand value.
- Indian CA firms cannot have non-CAs as partners. Nor can the Indian CAs or CA firms have any profit-sharing arrangement with non-CAs. Thus is it not possible for Indian CAs to structure multi disciplinary practice to offer a one stop professional facility to clients. The Chartered Accountants Act prohibits such multi disciplinary firms.
- One of the significant ethical requirements of the ICAI is that an Indian Chartered Accountant has to affix their individual signature while attesting. This singular requirement has ensured that the consequential liability arising from attestation are directly latched on the Chartered Accountant concerned and are not fixed to any firm or organization. This is accountability of the highest order.

The factual position of disciplinary mechanism and ethical practices standards as they are practiced in advanced countries is presented elsewhere.

A proper understanding of the ethical and regulatory regime operating on the Indian accounting profession is necessary to understand the relatively licentious and unsupervised liberties exercised by MAFs, which also add to the unevenness of the hostile playing field in which the Indian CAs are compelled to operate and compete with the MAFs under the present regime.

CHAPTER V

THE ENTRY OF MAFs IN INDIA AFTER THE ONSET OF LIBERALISATION AND GLOBALISATION, AND ITS CONSEQUENCES TO THE PROFESSION AND THE NATION

MAFs ENTRY INTO INDIA

It was when India faced severe foreign exchange crisis during early 90's and went to the IMF for a bailout package, the MAFs began to set foot as consultants in terms of the stipulations laid out by the IMF was to allow them to set up their own business in India. This was ostensibly to facilitate free flow of the foreign direct investments into India in the liberalized regime by the investing bankers, MNC's, and the multilateral investing agencies who would 'only be comfortable' with their own consultants as advisors to "help" them invest into India.

The colonial hangover which continues to mark the Indian psyche even more than half a century after Indian independence already gave and continues to give an unfair advantage to the western ideas, institutions and professionals over the local. The general tendency in India is to regard as superior to the local anything from the west has meant a non-tariff barrier for the locals in their competition with the foreign, particularly the western. So the non-tariff barrier works in India in reverse, that is, unlike in other countries where the non-tariff barrier works in favour of the locals against the foreigners, in India it works in favour of the foreigner, that is the westerner, as compared to the local. This peculiar psychology of Indians impedes the competitive ability of the Indian products and service providers.

But having entered India, the MAFs soon found India not only as a lucrative but also a gullible market. With the Indian system giving them red carpet welcome because of the colonial legacy and the Indian business associations and some of the well-connected bureaucrats welcoming them with reverence, the MAFs soon established themselves as the principal service providers of global quality. The MAFs soon began making rapid inroads in high end consultancy. With their impressive methods in presentations backed with intense lobbying, the MAFs started advising Government of India, on dos and dont's, as per the prescription of their bosses. The unsuspecting Indian establishment which had no idea that their designs will ultimately undermine our country's financial mosaic and that forever we will be in the clutches of the influence the global financial system, the Indian establishment, like the establishment in the west, fell to the designs of the MAFs. Thus, the MAFs soon became the torchbearers of reforms for the Government of India, found positions in all high-powered committee of the federal as well as state Governments. They have influenced, changed and dominated the Indian economic thinking for over a decade now. Their entry into India has completely changed the way the profession needs to operate in India. The following points illustrate the impact of the entry of these firms on the profession as well as on the nation.

MAFs: IMPACT ON THE PROFESSION

The lack of awareness in the Indian CA profession

The Indian accounting profession was almost totally unaware of even the fact of the entry of MAFs into India. They were not aware of even the mode of their entry. They were equally unaware of the purpose of their entry. The MAFs entered India through the floodgate of reform measures initiated by the Government in the name of liberalisation. There was no debate as to whether their entry was needed for Indian economy. There was no consultation process of any kind, with any stakeholder. The most relevant stakeholder, the Indian accountants were not in the picture at all. Those who knew the entry of the MAFs thought that their entry would enrich the Indian accounting profession and retrain and increase the skill levels of the Indian accountants. They thought that their entry would benefit the Indian accountants. But they never examined the terms of their entry into India. Nor did they stop for a moment to assess the import or consequences of their entry into India. Their entry became a fait accompli even before the Indian CAs could understand and react to their entry.

The entry was stealthy. Even ICAI was not consulted; Perhaps, it knew of the decision only in newspapers

In fact the entry by the MAFs into India was stealthy. Neither the accounting profession knew about it nor its regulatory body ICAI was consulted before this unilateral opening up of the profession. While it was true that the initial 'mistake' could probably be attributed to the RBI and the Government in as much as ICAI was not even 'consulted' before such opening up, the leadership of the profession has also failed in its part for its apparent apathy and indifference over the continued aberration, by not raising adequate objections.

No reciprocal right conceded to Indian CAs to practice their profession abroad: and this is deliberate; the entry is part of a wider agenda of the west to maintain its lead over the Rest

The most critical point about the entry of the MAFs is that they have entered India not only without any reciprocal right to the Indian accountant firms in western economies, but under a deliberate game plan of the west to deny such entry for their control of the financial world to maintain the lead of the west over the rest. This will require some explanation. The western economies, including the US economy, deliberately protect the accounting profession zealously for obvious reasons. The accounting profession is the backbone of the financial world which the west wants to dominate and through the financial world the west wants to dominate the rest. The most critical part of the financial world is the rules instruments and the institutions which conceive and enforce the discipline the global financial world requires for its functioning. This rule making mechanism is the most critical mechanism. These rules are not framed by global consensus, like for instance the environmental regulations. They are framed on the basis of the models and institutions born out of the experience of the west and universalised by the process of privatised dissemination of the official agenda of the west. The entire Washington consensus on the basis of which the idea of globalisation was centralised was a combined product of the US treasury, and the Breton woods institutions IMF and World Bank.

Till at least the collapse of the different economies starting with the East Asian economies and running through the Mexican and Argentine economies recently this was assiduously marketed as a total solution to the

world through agencies which are perceived as private, but are in-severably part of the official western and global institutions functioning on the agenda of the west. It was only recently the idea of total convertibility of national currencies given up as a solution as this turned out to be a problem rather a solution. But the other limbs of Washington consensus including privatisation and free trade, which means trade managed on western terms, are still very much part of the common agenda of the Breton woods institutions and Investment Bankers, Rating Agencies and MAFs functioning with a common agenda. The software to run these institutions is supplied largely by the accounting profession, and particularly by the large accounting firms.

These large firms become the informal but the effective instrument for driving the process of globalisation and the pathfinders for the globalisation process. They advise the corporates and Governments in the non-western countries. They are non-Governmental and therefore do not suffer political implications. They are part of the commercial world and so they carry the business tag. But they are part of the larger network the political and commercial institutions of the west. Their work is inextricably mixed with the world of private finance and rating as well as with the official policy making and strategies. Because of this the western countries are not too keen to open the accounting profession. In the EU half of the countries including Germany citizenship is the basic requirement for entering the accounting profession. In most other countries one must have a residential permit which is linked to emigration policies preventing movement of natural persons.

The US position in the WTO is that constitutional arrangement confers the right of regulation of corporates and the accounting bodies on the States and the Federal Government of US has no constitutional authority over the corporate or accounting regulation. Therefore the US had clearly maintained that it would only give the Best Endeavour Commitment, that is, they would try their best to open the accounting profession. Therefore it is obvious that the West is keen to maintain its lead over the rest in this crucial field. But one of the methods by which the west want to maintain the lead in the world of finance over the rest is not just by restricting the entry of the accounting professionals from the rest of the world into the west which is the nerve centre of global finance but also by entering the rest of the world armed with the rules, instruments and institutions theorised developed and put into practice in the west to capture the finance and accounting market.

That is why the one of the first areas which the western financial institutions wanted opened was the accounting sector which is part of the global financial mechanism whose trigger is held by the west. The entry of the MAFs was necessary from the point of the western system to guide the liberalisation and globalisation policies of the host economy along expedited lines to suit the interests of the west, rather than being calibrated to suit the interests of the host country. Thus the entry of MAFs is part of the larger agenda of the west-centric and west-directed process of globalisation.

The entry of MAFs is also ahead of the WTO negotiation schedule on the Services Sector; now a decade after the entry of MAFs the WTO members are exchanging wish lists from each other. The negotiation is likely to take years; thus the MAFs are at least two decades ahead of the possible, but uncertain availability of the right for Indian firms to enter the west.

Another critical aspect is that these firms have entered in to India far ahead of the WTO negotiations on the service sector. Even now, that is, even a decade after the MAFs have

entered India, the WTO negotiations are only at the stage of exchanging wish lists or 'request lists' from different member countries on different services. The unfair advantage, which the prior entry of MAFs into India into India has conferred on the MAFs much to the detriment of the Indian CA firms in their own land, can be judged from the fact that the Government of India in its proposals to the WTO has clearly refused to agree to the opening of the legal profession, but has agreed to the partial opening of the accounting profession. **The most probable reason why the Government has sought to make a distinction between the legal profession and the accounting profession is that in the case of the legal profession the organised strength of the profession prevented the entry of multinational law firms into India.** The organised legal profession agitated and obtained stay of the entry of the MNC firms, while the CAs did nothing to prevent the MAFs from entering India.. With the result as explained earlier the MAFs had entered India and their presence in India is the reason for the Government of India distinguishing between the MAFs and the MNC legal firms and proposing to open the partial accounting sector in the negotiations and not opening the legal sector to MNCs. Given the broad expectation that it may take another four or five years for the GATS to become effective, it means that the MAFs are having at least 15-20 year advantage over the Indian firms which will get the right of entry into the western market only when the GATS becomes effective.

The premium consultancy segment which opened on liberalisation of the economy in the 1990s monopolised by the MAFs

Having entered India and to the detriment of local firms these multinational firms were able to establish practice in the premium consultancy segment. Post liberalisation, this is an area which opened up for new opportunities for the Indian CA profession. But this area was totally monopolised by the MAFs. This was made possible because the MAFs managed to come to India stealthily by coining their connections in the international financial system and using the financial crisis which India faced. Thus the entire the financial and finance related consultancy work came to be monopolised by the MAFs. Had the MAFs not been allowed into India almost coinciding with the opening of the Indian economy, and had their entry been calibrated like in the case of other professions, and even as in the case of industry, the local firms would have had the opportunity to handle the new avenues and would have opened up their practice in these areas themselves or in association with the MAFs and other foreign firms, just as many audit firms in India had been the associates of foreign firms before liberalisation. This would have afforded adequate opportunity to the Indian CA profession to acquire the requisite experience, knowledge, competence and confidence to handle the evolving globalisation and liberalisation with India as its base. With the premature and stealthy entry of the MAFs the Indian CA profession lost its national base in the consultancy sector. Had their entry been calibrated, the ICAI and the Government could have had the time to formulate globally compatible regime for the Indian CA profession by allowing multidisciplinary firms and networking of CA profession and CA firms with non-CA professions like legal, management and technical consultants, like for instance networking of important CA firms with say a Tata Consultancy Services Ltd. This would have prepared the Indian CAs and also the country for an effective competition. Should any further

preparation be needed to handle the new situation, the networked large entities could have easily bought global level talent for India till the Indian situation evolved.

Surreptitious entry of MAFs into, and their illegitimate presence in, the traditional professional areas of Indian CAs through surrogate firms

These firms, having entered India by licence from the Reserve bank of India, as consulting firms, entered into an arrangement with a few local CA firms that turned them into surrogates. Each of the MAFs has more than one surrogate. Many of the surrogates are well-established Indian CA firms in traditional areas. With the entry of the MAFs and with their monopolising the high-end and high value consultancy areas and with their nexus with the global financial institutions, investment bankers and rating institutions, the balance of decision making power in the Indian corporate world and generally in the Indian financial system as well as in the India establishment, including the Government as a whole, shifted in favour of the MAFs in all areas including audit and attestation work where they were operating at the global level. With the decision making about the traditional areas of CAs also shifting in the Indian system because of the entry of FDI, Joint Ventures [JVs] with foreign companies, the entry of FIIs, and the foreign banks and other agencies, including the omnipresent World Bank and the IMF in favour of the MAFs, the traditional Indian firms which had large audit and other professional presence too felt insecure about their capacity to retain their position and therefore many of them began thinking in terms of becoming and being their affiliates or surrogates to retain the very work they were handling and to access new work through the MAFs. This was the trigger for the evolution of the surrogate professional circuit in Indian CA profession. The list of such surrogate CA firms for the MAFs is as under:

KPMG - BHARAT S RAUT & CO

ERNST & YOUNG - S R BATLIBOI & CO

DELOITTE TOUCHE AND TAHMATSU - S.B. BILLIMORIA & CO, DELLOITTE HASKINS & SELLS, CC CHOKSEY & CO AND FRASER & ROSS

PRICEWATERHOUSECOOPERS - PRICEWATERHOUSE & LOVELOCK & LEWES

The pernicious consequences of the surrogate arrangement may be summarised as under:

- Through these surrogates the MAFs have also begun to render attest and assurance services which only CAs and CA firms licensed by the ICAI could do.
- While acting and operating through the surrogates in traditional areas where the Indian CAs subject to the discipline of the ICAI were operating under great constrains like prohibition of canvassing, advertising their services, the MAFs began and continue to merrily advertise and brand-build their own names, and take advantage of their brand value built in defiance of the Indian CA regulations established by law, through their surrogates. This snide and devious exercise extends from holding cricket matches to high cost advertisement in the media to even higher cost events like instituting and giving Business Leadership and Entrepreneur Awards to squeeze themselves in to the high yielding corporate and financial market for professional work.
- Thus by establishing surrogates, these firms have ensured that the profession is carried on the lines of business and without any

regulatory mechanism. The ICAI which does not normally get into controversies and is in fact a mechanism to discipline the profession rather than a mechanism to fight for, defend and protect the profession in surprisingly bold initiative openly declared that the surrogate mechanism is an illegal and illegitimate device. In a report published in the 'Chartered Accountant', the official organ of the ICAI, the Institute had said:

"***The Government should review the alternative route of entry of accounting firms in India in the name of management consulting firm, and, circumvention of the law of the land taking place directly and indirectly by performing accounting services by them***"

Thus it is obvious that the surrogate practice is an unauthorised act, and yet goes on as the Government is mute and the ICAI is also not structured to fight the fight evil as it is a gentlemen's institution, not capable of fighting or used to fighting wars. It is a peace time institution, not capable of handling the unequal war forced on the profession by the entry of MAFs.

- These firms were able to coerce Indian corporates to replace their existing local firms with their own surrogate firms. There have been repeated instances of the MAFs forcing Indian corporates which have accepted FDI or privately placed FII investment or which have entered into JV agreements with foreign companies to change their statutory and internal auditors, even consultants and advisors in some cases, and appoint their surrogates. The Indian corporates have been forced by deliberately crafted terms of the agreements of investment or JV. This kind of pressure would be unacceptable under the ICAI regulations. Should an Indian firm enter into such dealings in the US, for instance, that will be deemed an offence under the provisions intended to curb lobbying for professional work should such provisions exist in that country. Because the MAFs are outside the scope of the discipline of the ICAI and for that matter any discipline, no such action is possible. Even there are instances of the surrogates tending to defy the ICAI when the regulator attempts to regulate them.

The Indian economy opened up after decades of controlled system, there was a general euphoria about foreign investment, foreign companies, foreign ideas, and foreign technology and foreign consultants, in fact things and thoughts foreign. While there is nothing wrong about induction of things and ideas foreign for developing the national economy, the manner in which the idea of globalisation and liberalisation was conceived and articulated in India eroded the confidence of Indians in India itself, and in Indian industry, Indian products, Indian technology, Indian professionals, and Indian institutions and laws. For almost the whole of the last decade the nation virtually became foreign-dependent in mindset, and almost became reconciled to the thought that India cannot be built by Indians and only foreign ideas, foreign capital, and foreign companies can build India.

Some sections of the Indian establishment including the Indian bureaucracy even began advising the Indian industry openly that they should leave manufacturing and get into trading as they cannot compete with the foreign companies. This eroded the confidence of the Indian industry so much that many industrial groups even postponed their investment programmes and virtually stopped thinking of establishing new businesses. In fact some of the Indian corporates were even advised to think whether they should be running the industries

they were be running. The most efficient steel maker in the private sector was forced by the prevailing atmosphere to engage a foreign consultancy company to advise whether it should be in steel business or not. The consultant promptly advised that they should get out of the steel business. Fortunately the steel maker did not accept that advice, but continued. Today it is recognised as the most cost efficient steel maker in the whole world. This instance is brought out only to demonstrate the extent of demoralisation that had been deliberately injected into the Indian system by the proponents of globalisation and liberalisation.

Thus the nation was rendered bereft of confidence, till the software boom began to place India on the global business map. This single factor in the late 1990s helped to rebuild the confidence of Indians in India and in them selves. The way the Indian economy showed its resilience when the Asian Tigers went for a six also reinforced the confidence of Indians in them selves. Added to that was the fact that politically, India had come to occupy a more powerful position having become a nuclear power. So in the latter part of the last decade and the early years of the current decade it is beginning to overcome the loss of self confidence which this nation suffered in the initial years of the liberalisation and globalisation era.

This confidence is today manifest in the enormous stability and reduction in poverty the Indian economy has achieved, including the strength it has acquired on the most critical external front the erosion in which landed India in a crisis in the year 1991. At the macro level it is also supplemented by the same degree of confidence at the micro level. The fear of being taken over and bought over by foreigners slowly reversed. Indian firms began to buy out their JV partners. Examples are the way the TVS group was able to buy out Suzuki and grow phenomenally in business and as was the case with Asian Paints. Thus the Indian economy is regaining the confidence which it had lost in the large part of the last decade of 1990s. The economy could do it because the state had in a way protected the economy during this period by adequate tariffs and investment restrictions like the ban on foreign JV partners from directly entering India through other routes including by establishing subsidiaries.

The story is a contrast in the CA profession. While the rest of the economy was given some kind of transition time by the state, the consultancy part of the CA profession was opened to MAFs and made defenceless. The MAFs entered the Indian economy and usurped the entire new opportunities and totally marginalised the Indian CAs. But the way it happened eroded the level of confidence of the Indian CAs in themselves and the confidence of the Indian system in the Indian CAs and in their capacity to render such services. Any new area of service particularly connected with the world of finance and particularly with world finance was presumed to be the preserve of the MAFs. With the result the Indian system including the Indian corporates, Indian Governments and even the state Governments in India began to engage increasingly and later exclusively the MAFs and other consultants for different assignments. Whether it was the planning commission or the divestment ministry, whether it was this bank or that, whether it was the financial institutions or the UTI or the LIC, they began engaging for all prestigious assignments only the MAFs.

This entire approach was fashioned by the foreign dependent mindset which drove the entire reform process. The other segments of the Indian economy had some kind of transitional

arrangement to manage such foreign dependent mindset provided by the state like the time provided to the industry to enable them to gather adequate strength to face up to foreign competition or by the organised strength of the concerned segment of the economy like the legal profession which fought to prevent the entry of multinational legal firms. The respite provided by the time given to different segments of the economy enabled them to tide over the foreign dependent mindset which the Indian economic thinkers and policy makers had created in the country and to regroup to gain confidence and strength as India as a whole gained strength in the last few years. That is why comparatively the different segments of the economy are showing confidence and growth. But in contrast the Indian CA profession has been rendered defenceless. The MAFs were allowed into India and their presence and the prominence have marginalised the Indian CA firms in high value and high end consultancy segments. With their name all over the media and in the relevant sections of corporate and Government decision makers, they had a larger than life impact.

They also reportedly followed other questionable methods to establish themselves. For example, a Government run development financing institution has been forcing many assisted corporates whose accounts were being monitored to get their quarterly income statements certified by MAFs only. This was part of the effort to undermine the confidence of the Indian industry in the Indian CAs. Some of these assignments carried remuneration as high as Rs 15 to 20 millions for four quarters. The helpless industry regards such assignments as nothing short of blackmail. But they can do nothing about it since they need the support of the finance institutions which had created two classes of CAs in India - the MAFs and their surrogates and affiliates on the one hand and the non MAFs associated Indian CAs on the other, the former being the preferred and respected and later being condemned to play a secondary role in their own country, occupying just about the same position which the Indians occupied during the British rule in India.

There are instances of official institutions, banks and even the officials of the Governments being actively or passively party to demeaning and eroding not just the confidence of the Indian CA firms, but also abridging their professional space. This is in addition to the enormous influence the MAFs exerted on the system because of their connection with the world of finance. Their capacity to lobby and connect with global financial forces, including the investment bankers and rating institutions, also enabled them to condition and even coerce the system to create professional opportunities to the MAFs. For instance, when the Oil Companies' divestment programme was postponed by the Government in the year 2002 for want of political consensus, the international rating institutions immediately brought down the rating of India when the Indian economy was actually booming on the external front and the exports were increasing at an unprecedented pace. This was because the professional opportunities of the MAFs were affected by the divestment programme. It has been well documented in other countries particularly in the UK that the MAFs deeply influence the decisions on disinvestment through their connection with private finance which means global finance.

With no one including the state to protect and defend them, the Indian CA profession is fast losing its primacy in India which is their spring board to emerge at the global level. Thus the potentiality of the Indian CAs emerging as a global power was effectively delayed if not scuttled by the MAFs being allowed to set up shops in India without affording the Indian CAs

the requisite time to reorient themselves and to the ICAI to reframe its regulations to suit the new situation emerging on the onset of liberalisation. Considering that Indian CAs constitute the third largest population of competent, skilled and English educated accountants in the world -the first being the US and the next UK-this constitutes potentially the most effective competitor to the western, and particularly, Anglo-Saxon nations, and therefore their global potential is immense. But despite being a profession which attracted the best talents in the country for three decades from around 1970 and despite being a potential global power, it was weakened in confidence at home and was deprived of a large space of consultancy work. In fact it is threatening to become a side show in its own territory in the consultancy field and is being further threatened even in the traditional areas of audit and taxation work. Thus CA profession did not merely lose the new opportunities which the liberalisation programme opened up it also lost substantially its confidence because of the prominence and pre-eminence given to the foreign consultancy firms, particularly the MAFs. Unlike the other segments of the Indian economy, the Indian CA firms could not recover from the loss of confidence as by the time the nation as a whole began recovering the MAFs have virtually usurped the entire consultancy space of the CA profession and also the prominent presence which marginalised the Indian CA firms. With the result the Indian CA firms have been not merely marginalised in India but they have also been in a sense demeaned and de-legitimised as the prime professional force in the country.

Different methods were followed to undermine the Indian economic players. An instance may help to understand. As part of the design to devalue and undermine the Indian CA profession, the MAFs came up with studies that exaggerated levels of NPA in our banking sector, which was significantly at variance with the levels mentioned in the audited balance sheets of Banks. This was calculated to undermine the audit process of Indian Banks by Indian CAs as an exercise in futility. These studies were a systematic and calculated assault on the professional dignity of the Indian Chartered Accountants and to harm the collective consciousness of the profession. In the end the NPA levels projected by the MAFs and their lobbies were not found to be correct and were only a transitional phenomenon. The Indian banking system which was compared to the Chinese and the South East Asian NPA levels had no such implications and had merely transited from the socialist methods to market driven methods and the NPA phenomenon in the Indian banking system was merely transitional. But the entire exercise was done by the MAFs and hyped to discredit the Indian CA profession as part of the effort to discredit the Indian financial system. Later substantively the criticism proved to be highly unwarranted. As compared to the hype the lobbyists had created about NPAs, there is no cry about NPA today.

All this has resulted in a paradigm shift in the thinking of the business, Government and community within India. These firms have consolidated their strong hold on Government and Industry through a process of crass commercialism, lobbying and aggressive marketing. These consultants have made everyone in Government, industry, banking and financial institutions believe that they had tailor-made solutions for all micro and macro economic ills. Further believe all operations - anything and anywhere - to be successful- had to be only based on the 'study' and 'reports' given by the "International Consultants". By such lobbying, huge consultancy assignments were generated liberally and fees paid in millions.

Even internal audit, a pure professional job, was labelled as 'corporate consultancy work'. Last but not the least, by making the best of Indian professionals as their subcontractors for their Indian operations, a subtle but powerful message is sought to be delivered - that one of the most intelligent professions of India are at best capable of being mere appendages of the global players and thereby prepare the national psyche for merely playing the second fiddle to any foreign player entering India.

The net result is that this has marginalized the Indian Chartered Accountants within India. The Indian Chartered Accountants were expected to dominate the world accounting sector as and when this sector was to be opened under the GATS as a service exporter. But by weakening them in India and that too ahead of the GATS regime the Government of India is impairing the confidence and competence of a potential national service provider, namely the CA profession in India, which could dominate the world. Indian CA firms are the biggest and the most potential danger to the Anglo Saxon world which is monopolising the rest of the world today. The MAFs targeted the Indian market even before the large army of Indian CAs even recognised the danger inherent in the aggressive and premature entry of the MAFs into India, so as to erode their confidence and space for practice in India. Thus the GATS negotiation on the accounting sector has been rendered at least partially meaningless exercise by the entry of the MAFs well ahead of the GATS schedule.

To summarise

First the Indian accounting profession did not know about the entry of the MAFs into India.

Second, the ICAI was not consulted about the entry. In fact the ICAI which is the main stakeholder in the decision of the RBI to allow the MAFs to operate in India came to know of the decision of the RBI only through newspapers.

Third, the Indian accounting profession could not judge the adverse impact the entry of MAFs will have on the national accounting profession and was taken in by the media and political hype that was created about the entire process of liberalisation and globalisation.

Fourth, by the time the Indian accounting profession came to know about the adverse consequences of the entry of the MAFs it was too late. The MAFs had entrenched themselves, and many Indian firms had even become their surrogates and subcontractors and therefore became their satellites with vested interest not only in their entry and continuation but also in their expansion. It is just like many Maharajas partnering the East India Company and the British when they entered India, and later losing their position and status and settled for pensions and salaries for surrendering their sovereignty and that of the nation to the British.

Fifth, the MAFs entered India without any right or licence for the Indian CA firms to enter the western market. This fact was not even known to the Indian CA profession. Thus it was a totally one sided story, and the Indian CAs were blatantly denied level playing field.

Sixth, the premium consultancy segment, which was opened up to the MAFs immediately after the liberalisation of the Indian economy started, was monopolised by the MAFs by making use of their connections with global finance and by pressuring the Indian system and by unprecedented public relations exercise and huge media campaigns and advertisements.

Seventh, the denial to the Indian CA profession of the legitimate transition period which the Government had given to the other segments of the Indian economy and the state preference to

the MAFs over the Indian CA firms and consequently the demeaning and de-legitimising effect it had had on the Indian CA firms finally undermined the confidence of the profession and of the confidence of the system in the Indian CA firms.

THE ENTRY OF THE MAFs AND ITS IMPACT ON NATIONAL INTEREST

De-legitimisation of the Indian CA profession in India

The entry of the MAFs and the consequent de-legitimisation of the role and relevance of the Indian CA firms has had adverse impact on larger national interest.. For instance the State Bank of Indian recently issued an advertisement inviting bids from accounting consultancy firms of Indian and abroad, but stipulated that the balance sheet size of the bidders should be Rs500 billions, that is Rs 50000 crores. The SBI knows too well that there is no Indian consultancy firm which is of that size. And even in the Indian industry only two groups have balance sheet size of Rs 50000 crores. Nothing can more effectively de-legitimise the Indian CA profession than this SBI advertisement humiliating the Indian CA profession.

Erosion of CA profession's confidence erodes national interests

If a critical profession like the CA profession's confidence is eroded it impacts adversely on national interests. In principle the interest of a national profession like the CA profession converges with national interest.

Role of national CA firms abridged and MAFs occupy the main space

If an important national profession like the CA profession's professional space within in the national territory gets abridged and foreign firms take their place it equally affects national interests. If particularly a national profession like the CA profession which some of the best minds in the country have taken to in the last three decades and more is losing out to foreign firms in its own territory it obviously impacts adversely on national interests.

Indian CA profession, a potential global power has been weakened at home

Again if a national profession like the CA profession which has the potential to emerge as a global power is weakened at home and because of that it loses its capacity to emerge at the global level, it is a great national loss and it adversely impacts on national interests.

The MAFs have entered India without any reciprocity to Indian CA firms to set up shops abroad: so MAFs entry not a mutually beneficial trade arrangement: it is like an invasion during the colonial days

But that is not all. The opening of the consultancy segment of the accounting profession without any reciprocity to Indian CAs to set up workstations in the countries from the MAFs come from is a clear bartering away of national economic interests for nothing in return. It is equivalent to India allowing market access to foreign goods in to India, even though similar goods are available in India, without seeking similar market access for its goods in countries from which goods are allowed access into India. The grant of market access to MAFs in India, that too to set up shops here by way commercial presence is more than allowing market access to them. In services sector market access is allowed by different methods. Two important methods are: one, cross border services, in which services are rendered by professionals from one country by temporarily visiting another country without setting up any establishment. And the other, commercial presence where the professional firms of one country are allowed to set up permanent establishments to render professional services in the other country. The first type of access, called Mode 4. is sufficient to protect the interests of the investors in India who came into India on the opening of the Indian economy.

This could have been sufficient as well as reasonable for the liberalisation programme undertaken by the Government of India. But what the Government, that is the Reserve Bank of India, did was to allow the MAFs to set up permanent establishment in India, which is called Mode 3 entry. Here the MAFs set up permanent establishment to access the Indian market without any right to the Indian CAs to set up shops in the countries from which the MAFs hail from. This is against all cannons of international trade norms and normative agreements. Only in countries where there is no local talent of competent and trained accountants that an extreme kind of non-reciprocal arrangement is sometimes resorted to as something inevitable because of acute local need for such services from outside. But in a country like India where we have global level competence available through Indian firms in India, importing MAFs for that purpose without any reciprocity amounts to totally mortgaging national interests. And this is precisely what the Reserve Bank of India has done. In fact the ICAI had been dealing with this issue of reciprocity with other accounting institutes in other countries.

The ICAI had appointed a committee to look into the issue of reciprocity. The committee had made surprising findings as to how the other countries, particularly the western countries protect their respective national interests. Many of the EU nations have prescribed citizenship as the qualification for practising as accountant and to carry on audit or consultancy work. In the US the regulation of the accounting profession is in the domain of the state Governments, not the Federal Government. The US does not recognise foreign accounting qualifications nor does it allow foreign accounting firms to practise in the US. With the result the Anglo Saxon nations whose market affords opportunity for the English educated CAs of India is virtually closed for India.

But India has without any reciprocal market access, and in the face of clear market access denial opened the Indian accounting sector to the MAFs. This has irreparably damaged the national interests and national economic and business interests of India. Recently the US regulations have been modified to stipulate that the companies listed in the US could only be audited by an audit firm registered in the US and in the country where the auditors practise. This regulation is intended to force countries like India which has not allowed foreign accounting firms to practice in India and therefore not registered the foreign accounting firms in India, to register the big four in India as otherwise the big four will not be able to certify the accounts of the companies listed in India and also the surrogates of the big four also will not be able to certify the accounts of such companies unless the surrogates are registered with the regulators in the US. It means that even the surrogates cannot do the audit of US-listed companies without being themselves registered with US regulators. And unless the big four or the surrogates certifying US listed companies are registered in the places where they practice they cannot certify the accounts. It means that in the case of India, either India grants registration to MAFs to practice in India or the US authorities grant registration to the Indian surrogates of MAFs to certify the accounts of US listed companies, in which case it is most likely there will be pressure on the Indian Government to allow the MAFs the right to practice in India. It is unlikely the Indian surrogates of MAFs will be allowed registration by the US regulatory. So the MAFs entry is not like a mutually beneficial trade arrangement, but more like an invasion, as in the colonial days.

The National accounting sector has been opened to MAFs a decade ahead of the start of the WTO negotiations on services sector. Consequence: Erosion of India's bargaining capacity for give and take at WTO

The issue goes farther. The services sector which is the largest segment of global economy and the national economies most of the developing nations and all developed nations is the biggest agenda of the WTO. The negotiations on trade in services which is covered under the General Agreements on Trade in Services [GATS] has not yet commenced in the WTO. Actually even as this White Paper is being written the member countries are merely exchanging their wish lists. It will take years for the multilateral GATS to emerge as it is inextricably mixed with the critical issue of mode 4 Entry, that is, immigration. While the multilateral negotiations on GATS has not yet started the Indian Government has already opened up unilaterally the accounting sector in so far as it relates to consultancy and the MAFs have entered illegally internal audit and attestation segments also by that route. With the result apart from the fact that India has allowed the Indian accounting profession to be weakened at home and thereby eroded its accounting profession's capacity to emerge as a global power, it has also eroded its negotiating power at the WTO. Had India not opened its accounting/consultancy sector it would have bargained better for opening it. But having opened it unilaterally it has largely lost its bargaining power at the WTO. Thus it is a loss to India both ways, namely, it has weakened the CA profession within India and thereby impaired the capacity of Indian CA firms to emerge as a global player and also impaired India's capacity for negotiation at the WTO.

Degeneration in professional standards and culture: trivialising a dignified profession and converting it into business, with lobbying and influence peddling as the escalators

The issue does not stop at that. The entry of MAFs is also impacting on the culture of the CA profession. The Indian CA profession had always maintained a high degree of professional dignity. Canvassing for work was not considered honourable. But with the entry of the MAFs marketing of services has become a commercial art. Nothing is a bar to marketing one's services. From media hype to advertising to giving leadership awards to holding cricket tournaments, every technique that is used to promote sale of toilet products are used by MAFs to market their services. Therefore, marketing ones professional skill which was not considered very respectable has become not only acceptable, even inevitable, why even respectable. This is a cultural degeneration forced by the entry of the MAFs. With the result lobbying and influence peddling have become the accepted forms of growth, the escalators.

Indian financial system under the spell of MAFs: Undue pressure on the corporate to deny space to Indian CAs and to enlarge the space for MAFs for considerations less than honourable

In fact the hyped marketing by MAFs has had such impact on the Indian corporate and financial system, the Indian financial system came under their spell due to different marketing methods including the pressure through the international financial institutions cleverly employed by the MAFs. Their influence became so pronounced and blatant that the Indian domestic financial institutions even issued circulars to all assisted units insisting that they should secure the services of MAFs for their company internal, management and other audits and consultancy services. The Financial Institution nominees on the boards of companies also began insisting on the assisted companies to appoint the MAFs as consultants and even as statutory auditors. Thus the Indian Government establishments themselves have turned promoters of the MAFs to the prejudice of the Indian Accountancy profession. There is a wide suspicion that like in the western countries the MAFs also indulge in unfair practices like financially benefiting influential persons.

CHAPTER VI

THE ISSUE OF LEVEL PLAYING FIELD FOR INDIAN CAs, IN THE CONTEXT OF THE STRUCTURE OF THE INDIAN CA FIRMS, THE BILATERAL RECIPROCITY AND FURTHER IN THE CONTEXT OF THE MULTILATERAL GATS

THE ISSUE OF LEVEL PLAYING FIELD

The idea of globalisation and institutions are fundamentally based on level playing field. The concepts of MFN, National Treatment, Tariff reduction, uniform trade regulations and quality norms and other aspects of the WTO are all rooted in the philosophy of globalisation to ensure level playing field. In fact the very purpose of the instruments of globalisation whether it is the WTO or any other international treaty, is to ensure level playing field which will contain the sovereign power of the member states of the WTO to offer better treatment to their own business and trade than what they give to the other states. It is not the purpose of the WTO or the object of globalisation to ensure better playing field to foreigners than for the nationals of a country. But what the Government of India, particularly the Governments which initiated the process of globalisation in the initial stages, has done is to place the MAFs at an advantageous position as compared to the national accounting firms. This is the issue in the main. But this issue has other dimensions also. It is necessary how instead of ensuring level playing field, the Indian Government has ensured a hostile playing field for the Indian CA firms.

This issue of lack of level playing field will have to be addressed from different angles.

One: the diversified and rainbow-like structure of the Indian accounting profession, large number of small and medium firms, which presents a contrast;

Two: the lack of bilateral reciprocity to the Indian CA firms to set up establishments in western countries;

Three: the erosion in the negotiating capacity at the WTO flowing from the prior entry of the MAFs;

Four: the national inertia which has allowed the MAFs to gobble up the professional space of the Indian CAs through surrogate Indian firms of MAFs;

Five: the harsh disciplinary regime operating on the Indian CAs restricting their capacity to compete with the discipline-free and regulation-less MAFs;

Six: the suddenness of the entry of MAFs without giving any opportunity to the local firms to to adjust and consolidate and network among themselves did not give the time needed for the Indian CA firms to prepare themselves for facing up the competition from MAFs.

Seven: the response of the Western countries to opening their respective national accounting profession to foreign CA firms including the firms from India.

The structure of Indian CA firms: small, numerous, and diversified; presents a contrast to the size of MAFs

The Indian accountancy sector mainly comprises of small and medium sized firms, the number of

firms with 5 or more partners being only about 375 as on 01.04.2001 out of 42,339 firms as on that day. The sizes of the Multinational firms are too huge, especially when they operate in over 130-150 counties with over 120,000 audit personnel. This distorts the level playing field especially when the Indian CA firms are regulated very heavily. In contrast the MAFs are globally organised, have thousands of partners and hundreds of thousands of CAs working under them. They are also multi-disciplinary firms acting as one stop shop. It is obvious from the structure of the Indian firms and of the MAFs that the competition between them is totally uneven.

Allowing the MAFs to enter without bilateral reciprocity, thereby demeaning the position of the Indian CAs

Reciprocity is the mutual recognition between two nations' accounting bodies whereby the members of one body are entitled to become members in another country's body and vice versa. An Indian CA is not permitted to enter into partnership with any one who is not a member of the ICAI. However partnerships between members of the ICAI and the members of the foreign accounting bodies were permitted provided members of such bodies are eligible to become member of ICAI under arrangements for reciprocity entered into between the ICAI and the foreign accounting bodies. But this was subject to the further condition that they share in the fees or profits of the partnership both within and without India.

However after the entry of the MAFs in India foreign accounting bodies withdrew the reciprocal arrangement and promptly ICAI also retaliated in Dec 97, with the result today no bilateral reciprocity arrangement is in effect. Based on the above developments, partnership between members of the institute and members of foreign professional bodies is not permitted since Dec 97. But the respected and valued principle of reciprocity has been rendered irrelevant and otiose by the entry and presence of the MAFs here who are present without the consent and approval of the ICAI and who have the grabbed the professional space of the CAs right under the nose of the ICAI. This has demeaned not merely the position of the Indian CAs but also the authority of the ICAI.

Erosion in the negotiating capacity of the India in WTO as a result of the presence of the MAFs far ahead of the GATS negotiations

Contrary to the common perception that the licenses given to these Multinational Consulting companies to operate in India are mandated by commitments given by India to the WTO, the fact, indeed is, that they are not. Rather they represent an autonomous liberalization programme pursued by the Central Government. These firms are in India far ahead of the GATS-WTO requirements. Emboldened by the complete lack of protest by the profession in India, these foreign consulting firms have subsequently entered into separate arrangements with Indian Chartered Accountant firms in providing licenses to certain Indian firms to act as their authorized representatives within India. This allows them to render both consulting as well as audit services within India. In effect a powerful group of consulting firms directly in competition with the profession has come into existence but remains unregulated on the lines of the professional firms. This aspect has been explained in detail earlier.

National inertia has allowed the invasion of the Indian CA firms' traditional professional space by MAFs through surrogate firms

That the MAFs through their consultancy wings have been allowed and have been allowed without any kind of regulatory discipline till date

and yet compete with the Indian CA firms implies the failure of the ICAI to protect the interests of the Indian CA profession. It must however be mentioned that the ICAI in its June 2002 Journal has admitted the existence of this problem and stated, "*The Government should review the alternative route of entry of accounting firms in India in the name of management consulting firm, and, circumvention of the law of the land taking place directly and indirectly by performing accounting services by them*". Nevertheless it means that the ICAI is just helpless about such "circumvention of the law of the land" by MAFs and in fact even the recognition of this serious public mischief itself took so long speaks volumes about the state of the Indian accounting professional leadership. It is obvious that what has allowed this kind invasion of the traditional space of the Indian accounting profession is the national inertia. This inertia had been fostered by the contrived atmosphere favourable to the idea of globalisation built by the MAFs, foreign investment banks and rating agencies with the active backing of the multinational trading and financing interests, both official and non official.

This inertia also prevented the Indian business and profession from evolving proper responses to the challenges posed by the suddenness of the arrival of the WTO on the national economy. It is a sad fact that in general, none of the industry representatives, the professional bodies, the intelligentsia or the academicians critically analysed the West-centric and West-driven Dunkel Draft, which was subsequently adopted as WTO Agreement at Marrakkesh. And the then Government in the absence of adequate inputs from industry and professionals seemed confused and could not evolve appropriate and nation-centric and nation-friendly responses. Even ICAI, the statutory body regulating the finance profession, did not prepare any worthwhile strategy to face the consequences of the GATS agreement on the profession. Even though over seven years have gone by since the date of signing the Marrakech Treaty, there is hardly integrated approach within the Indian CA profession to deal with this vexatious subject. Hence, it has become crucial to impress on the members of the profession to foresee the pitfalls arising on the issue of opening up of the profession under the GATS regime as well as to lay out the future negotiation positioning required keeping in mind on the presence of the Multinational audit firms already in India.

The harsh disciplinary regime operating on the Indian CAs restricting their capacity to compete with the discipline-free and regulation-less MAFs

The disciplinary regime operating on the Indian CA firms is a legacy of the controlled economy syndrome. In fact such disciplining was wrongly regarded as a sign of Government intervention. and as a sign of less developed economy. That was also regarded as part of the socialist or Government-led economy. Nevertheless the Indian CA profession and the Indian CA firms were always tightly regulated and continue to be. Let us see how this harsh disciplinary regime creates an uneven playing field between the MAFs and the Indian CA firms.

- While the MAFs can solicit and canvass for work, advertise their services, and even give leadership awards to businessmen who are their present or prospective clients and also hold cricket tournaments to build their brands, the Indian CA firms are bound by strict rules of discipline against any kind of soliciting or canvassing for work.

First the Indian CA firms are prohibited from canvassing and soliciting professional assignments. They are prohibited from advertising their firms or their names. In contrast

the MAFs regularly make presentations, and solicit work from all, including the Government of India which has made the regulations which prohibit the Indian CA firms. So the Government which has prohibited the Indian CA firms from canvassing and soliciting professional work, and the different agencies of the Government offer professional work to the MAFs based on their presentations and solicitation. That is what is forbidden in the case of the Indian CA firms is not only permitted in the case of the MAFs but also become legitimate and respectable. Not only that. The MAFs go farther. They not merely legitimately and respectfully canvass and solicit work at personal level, they also promote their brand through enormous advertisement, and by sponsoring events like corporate leadership awards, and even multinational cricket cup tournaments at enormous investment. By such methods they have converted this dignified profession into selling services like sale of cosmetics and soft drinks. If we have to compare the way the Indian CAs are being asked to compete with the MAFs, it is like asking the Indian cricket team to play foot ball with Brazil, a totally different game than that they are used, and on rules which do not apply to cricket at all.

In fact the Competition Commission headed by SVS Raghavan while dealing with the disadvantages encountered by the Indian CA firms in the matter of soliciting and canvassing and informing their prospective clientele, has suggested the following remedy.

"The accountancy sector is regulated in India through a combination of both law and professional self regulation. The Chartered Accountants Act, 1949 governs the profession of chartered accountancy in the country. The Chartered Accountants Act, 1949 and the regulations there under impose certain restrictions in forming partnership firms. There are restrictions on the trade name having a nexus with individual or group of individuals (abstract names are not allowed), on the number of partners (restricted to twenty) and the number of statutory audits of companies (not more than twenty per partner). For reasons of reciprocity the Institute of Chartered Accountants of India does not recognise any foreign qualification. This reciprocity factor is grounded on national honour, professional self-respect and the desire of the Institute to use it as a bargaining chip. While these considerations have some justification, they affect adversely the employment of Indian professionals abroad.

The regulations under the Chartered Accountants Act, 1949 prohibit an accountant from advertising, soliciting custom, paying commission, brokerage or share of profits to anybody other than accountant. An implication of these restrictions has been that there is in existence today of a rather fragmented market for professional services. Except a few (may be five or six) there are almost no all India firm of accountants. This structure handicaps the Indian accountant professionals from taking full advantage of the potential global market in accountancy services.

The restrictions on incorporation and size of partnerships tend to limit the size of growth of the profession and the professionals. Similarly, the restrictions on statutory audit bring about a limitation on the size of the clientele. These restrictions are hampering the growth of the profession and are also anti competitive in character as the consumers are prevented from selecting a professional firm with reasonable freedom of choice. While one would respect some degree of restraint in marketing professional services, the restriction on professional firms on informing potential users as to the range of their service, the restriction on professional firms on informing potential users as to the range of their services and potential is

a case in point, wherein competition is injured. For instance, a professional firm cannot brochures to inform consumers, it cannot even indicate the firm's name in articles contributed to journals nor can it hold seminars to promote and disseminate knowledge among potential clients. In other words the professional regulations are perhaps protecting the weak producers of professional services at the cost of information being made available to consumers. It is ironic that Indian firms are not permitted even to mention the existence of their collaboration agreements with foreign accounting firms.

The legislative restrictions in terms of law and self-regulation have the combined effect of denying opportunities and growth to professional firms, restricting their desire and ability to compete globally, preventing the country from obtaining the advantage of India's considerable human expertise and precluding consumers from the opportunity of free and informed choice."

While the Competition Commission is correct in acknowledging the serious disadvantage experienced by the Indian CA profession, it is a moot point whether the remedy suggested by it is appropriate. Because the remedy may be worse than the disease it seeks to address. The incorporation of the cultural dimensions of the MAFs will bring into the Indian accounting profession the same evils which the West is now finding it difficult to deal with in handling the MAFs.

- While the Indian CA firms are by law constrained to be small and medium ones, the very fact that they are small and medium ones and that the MAFs are large ones is cited as the reason for allowing the MAFs to enter and operate in India, on the ground only large accounting firms can only handle the new audit and consulting work.

Second, one of the reasons cited for the presence of the MAFs in India is their size. And their claim even to quality is based on their size. That is, only large sized firms can provide the kind of services which have emerged with the onset of globalisation and liberalisation; that there is need for large firms to undertake the new assignments; that small firms are incapable of serving the new demands for services. That the MAFs are large firms and the Indian firms are small and medium sized is the main reason for allowing the MAFs to operate in India. How is it that the Indian firms remain small and medium sized? That they are small and medium sized is essentially because of the structure of the Indian industry. The Indian economy essentially comprised small and medium scale units. The anti-monopoly laws effectively prevented the growth of large units. The large industry in India approximated to the medium industry in the west. So when the Indian business itself consisted of only small and medium units how could large accounting and audit firms develop. In addition for over three decades there had been a persistent attempt to ensure that CA firms did not grow into large firms. There were restrictions on the number of audits a firm could handle, limited to the prescribed number per partner. These restrictions continue even today, though these restrictions do not apply to MAFs operating in India. They could have any number of audits outside. Also the Indian law permits only a maximum of 20 partners for a firm. In contrast the MAFs have thousands of partners at the global and at the local level. Further under the partnership law of India the liability of the partners of the Indian CA firms are unlimited, while in contrast the MAFs and for that matter the CA firms in the western countries remain limited. Thus while on the one hand the Indian CA firms continue to be subject to regulations which restrict the growth and the size of CA

firms, on the other, the very situation created by this regulation, namely the existence of only small and medium sized firms, and the non-existence of large firms is cited as the reason for the entry and operation of the MAFs in India. The irony is that even after the entry of the MAFs, the Indian CA firms, which were not allowed to grow in size in the past, are not allowed to consolidate or network themselves into large firms. That is eternally by law the Indian firms are condemned to be small and medium in size, so that never will they emerge as a competitor to the MAFs in India.

- While one of the main reasons why the MAFs are preferred over the Indian CA firms is because the MAFs are a one stop shop where a client will get multi-disciplinary services, as they are allowed to partner with non-CAs also, the Indian CAs are not allowed to partner non-CAs with the result the Indian CA firms are not able to render multi-disciplinary services.

The MAFs are allowed to have as partners non-CAs, including lawyers, management consultants, cost accountants, valuers and other professionals and constitute not just a CA firm but a multi-disciplinary professional firm. With the result they are able to provide a one stop clearing house for all the requirements of a client. In fact this is one of the reasons why the MAFs claim to be preferred. In contrast even after the entry of MAFs and even after they have begun invading the traditional areas where the Indian CA firms have been operating, and even after the Indian CA firms have been asking for change of regulations to permit multi-disciplinary firms, the regime continues to be the same for them. With the result there are two kinds of accounting firms functioning in India, namely, the multi-disciplinary MAFs and the mono-disciplinary Indian CA firms. This has subjected the Indian CA firms to great disadvantage vis-à-vis the MAFs.

Thus the disciplinary regime operating on the Indian CAs with no such discipline operating on the MAFs itself impairs the competitiveness of the Indian CA firms and makes the playing field hostile to the Indian firms and favourable to the MAFs.

- The suddenness of the entry of MAFs did not give enough time to Indian CA firms any opportunity to adjust and to consolidate and network so as to prepare themselves for facing up the competition from MAFs.

This proved to be a fatal inhibition on the Indian accounting sector. As explained elsewhere in this White Paper, the suddenness and speed with which the MAFs were allowed to storm the Indian accounting and consulting market completely deprived the Indian accounting profession of all new opportunities which emerged on the dismantling of the socialist economy and with the on set of liberalisation and globalisation except as subcontractors or surrogates of the MAFs. The calibrated manner in which the Indian economy was opened in other segments including industry, and how the sister profession of law was treated and is continuing to be treated in the matter of opening the local economy to foreign legal firms, is a direct contrast. In every area of economic activity the policies of the Government were calculated to give to the Indian firms an opportunity to prepare for the high powered and hyped competition from MAFs. With the result it is not merely the new opportunities which the Indian CA firms lost out to the MAFs, even the existing opportunities which the Indian firms had had were invaded by the MAFs. Look at the enormity of the damage to the national interests and the Indian accounting profession's interest.

First, the Indian firms could were not allowed to become big because of the policy against allowing things to become big. This had

impaired the competitive ability of the Indian firms at the global level. So the Indian accounting sector needed time like all other sectors time to adjust their mind and the structure of their firms and their strategies to prepare for facing the entry and competition from MAFs.

Second, even after the onset of globalisation the Indian firms were not given sufficient time to come to terms psychologically and logistically with the idea of consolidation and networking to put up large firms or groups of firms. In fact the history of accounting profession in the west also shows that the evolution into large firms is by way of consolidation and merger of small firms or their networking in to big ones. This natural evolution could not take place in India because of the sudden invasion of the Indian market by the MAFs.

Third, they were not allowed to form cross disciplinary firms with other professionals so as to provide one stop service to their clients. This would have called for amendments of the rules and thus debate and discussion perhaps with other professions. This would mean time and a calibrated approach. Thus even the ICAI was not allowed the time to adjust its rules to suit the emerging situation. This deprived the young Indian accounting profession of all high-value and value added segments of practice.

The final picture that emerges is that the Indian firms appear to be losing their primacy in their own country as the adjustments needed to suit the needs of the times could not take place thanks to the sudden invasion by the MAFs.

These are, indeed, humiliating consequences to the nation which alone can challenge the Industrial nations in the field of consulting and audit. Most of these humiliating consequences are the product of the sudden, un-calibrated, and hostile regime which was forced on the nation.

- The situation which prevails in India is in total contrast to the response of the western nations toward opening the accounting profession -all western nations assiduously protect their accounting sector which is critical to the financial sector.

The situation which prevails in India is in total contrast to the situation in other countries, particularly the west. In USA, which is a federal Government, the profession of accountancy is a state subject and the US Government. When it had to give the commitment about opening the accounting sector in the WTO negotiations, simply shrugged off, and refused to give any firm commitment about opening the accounting sector. It gave only what is known as a "Best Endeavour Commitment" on behalf of its state Governments. It meant that the US Government would endeavour its best to persuade the state Governments to open up the accountancy profession.

In Germany, only a German citizen can practice the profession of accountancy and to become a German, at least one of the parents should be a German. Similar is the position in many of the European countries. In Japan and USA, one can practise the profession of accountancy only if he passes the examination conducted in those countries.

This national obsession in "protecting" the accounting profession from the onslaught of foreign players is a reflection of how various countries have viewed accounting as some kind of strategic issue being part of financial sector which is universally viewed as the strategic part of a nation's business. It is strange that India with a rich and healthy tradition of accounting profession and which has developed an army of modern accounting professionals, competent enough to take on the very best in the world should have viewed and continued to view the

issue of opening the accounting sector in a casual and non-serious manner. Worse still, by not recognising the innate strengths of this fraternity and exposing them to unhealthy competition, India is retarding the growth of a profession that has the potentiality to dominate at the global level.

It is evident from the facts and circumstances marshalled here that the Indian accounting profession suffers from uneven and hostile playing field and is greatly inhibited by from historic, structural, legal, procedural, regulatory and official attitudinal discrimination which gives to the MAFs an unprecedented advantage over the Indian CA firms. Thus Indian CA firms are kept out of the industrial countries and are virtually disowned at home. They are very much in the same situation in which the pre-independence Indians were at the mercy of the colonial masters. The only difference is that this is today happening not under an alien but under an indigenous regime. Unless these distortions are corrected and the Indian accounting sector is allowed to evolve on its own to realise its inherent potential and inner strength, an eminently capable profession which is a globally competent national asset will fail to deliver its true worth. It will not merely be a national loss. It will be a global one too.

CHAPTER VII

THE PHILOSOPHY, CHARACTER, WORLD-VIEW, GOALS OF MAFs: THEIR STRATEGIES AND METHODS; THE APPREHENSIONS ABOUT THEM; THEIR GENERAL IMAGE IN THE WEST

A curtain raiser on the MAFs, as perceived in the West and in India, in the context of this White Paper

Particularly after the Enron and Arthur Anderson fiasco, MAFs are subjects of cartoons in the West. But still they are objects of reverence in India. Even to the Indian accounting profession. This sums up the unimaginable gap between their image in India and the reality. Also sums up the enormity of the ignorance about them that informs India, the Indian system and the Indian corporate sector. There could not be a greater lie than their virtuous image in this country. One of the main objects of this exercise of a White Paper is to inform the Indian establishment, including the Indian media and the Indian state, the Indian corporate sector and even the Indian accounting profession about the true character of the MAFs and the true facts about them.

There have been critical reviews of their activities by corporate watch groups and public sentinels in the west; also by the media and by regulators. For example in UK Association for Accountancy and Business Affairs [AABA], a non-profit independent body critically scrutinises the audit firms, particularly the MAFs. Again, Unison, an organisation which represents over a million members in UK, acts as a watch dog on the MAFs. In the US, different initiatives including The Catbird Seat, a web site which carries on a powerful awareness campaign about the MAFs, and also an alert and critical media, analyses and informs the public about them and keeps the image of the MAFs close to reality.

In contrast, in India, there is not only no such effort, like many things foreign, whether it is the soap, or soap opera or toilet items or electronic gadgets, the MAFs are also treated as something superior. In fact the logic is that the Indian CA profession is no good. But this does not answer the question whether what is imported from the west, the MAFs, is good. The plain answer is 'NO'. But this is not the understanding about the MAFs in India. It is actually the other way round. Like the presumed superiority of many things from the west, the MAFs are also assumed to superior, not only superior to the local CA firms, but also superior to all other accounting talents in the world. While the West analyses the MAFs, India admires them; even as the West castigates them India compliments them. This is the contrast.

It is therefore necessary to inform and sensitise the Indian establishment, policy makers, corporate and financial decision makers and also the regulators and the media and the general public. What is the character of the MAFs? What is their philosophy? What is their world view? What are their goals, and the methods and the strategies to achieve them? These issues need to be addressed and answered for the benefit of the Indian business which adores them, the Indian Government which patronises them, the unsuspecting India media which reveres them like many things foreign, and the uninformed Indian nation which is totally unaware of the shenanigans and the maze of global finance of which the MAFs are a by-product. It is in the

interest of all of them that some one, in this case it happens to be the CAAC, to alert and sensitise all to the true facts about the MAFs in the larger interest all and more importantly the Indian nation.

If the study titled "DIRTY BUSINESS: THE UNCHEKED POWER OF MAJOR ACCOUNTANCY FIRMS" conducted by Austin Mitchell and Prem Sikka for the Association of Accountancy and Business Affairs [AABA] in UK is to be believed, the answer to these questions will be:

What defines their philosophy?	The answer is : Money.
What defines their character?	The answer is : Money.
What drives their world view?	The answer is : Money.
What are their goals?	The answer is : Money.

Their strategies and methods are driven by their character, philosophy, world view and goals, which is all money. That is, as Mitchell and Sikka say, it all 'MONEY, MONEY, AND MONEY' which drives the entire agenda of MAFs.

So it is no more a honourable and honest profession they are in. They are in business--as dirty a business as any dirty business person can be, but without the dirty image which a business person has to bear, and instead with the honour and the protection that goes with the image of being in a profession.

In addition they are an awesome power. They wield money power which is greater than the individual GDP of more than half of the nation-states in the world. The growth in their power synchronises with the rise of virtual money, the speculative money which began devastating the world from the time of the floating of the national currencies. A brief introduction to the awesome power of the MAFs and the methods and practices they adopt as part of their accepted professional conduct may be given from the Mitchell-Sikka Study:

In the pre-Enron world, five secretive firms dominated the global accountancy scene. Their income in greater than the Gross National Product (GNP) of many nation states.

FEE INCOME OF ACCOUNTANCY FIRMS

FIRM	UK INCOME £ millions	GLOBAL Income US$ billions
PricewaterhouseCoopers	2120	22.3
KPMG	1160	11.7
Deloitte & Touche	796	12.4
Ernst & Young	626	9.9
Arthur Andersen	619	9.3

Sources: Accountancy, July 2001, p. 16; February 2002, p. 13.

In pursuit of profits, major accountancy firms conduct "consultancy audits". They receive as much as 73% of their income from selling consultancy services to their audit clients (Accountancy, October 2001, p. 7). They hire company directors and management, create systems of internal control, director remuneration packages, transactions (e.g. tax figures), operate internal audits, form subsidiaries and design complex financial schemes, and then pretend to audit the same. In the name of efficiency, audit work is often falsified or not done at all (Willet and Page, 1996). Firms openly flout the rules on auditor independence (Securities Exchange Commission, 2000). The economic incentives for delivering good audits are weak. Unlike the producers of sweets and potato crisps, auditors do not owe a 'duty of care' to any individual stakeholder affected by their negligence.

So we are dealing with very different clones, different from what normal humans, societies, systems, and nations are familiar with. All MAFs share the same philosophy, character, world view, and goals. They share the same culture. Same personnel at times, as they merge and de-merge among themselves, take personnel from one another. Therefore their strategies and

methods are also identical. There is nothing to choose between them. Even though they compete against one another, none of them is an alternative to the other or others among them. They are mutual competitors, not mutual alternatives. Hence the need to alert, sensitise and warn the stakeholders in national and global economy and also the relevant players and the general public which is finally affected by the distorted philosophies, character, world view and goals of the MAFs and by their strategies, and methods.

The enormous public mischief and wrongdoings inherent in the very philosophy and structure of the MAFs: the different aspects of their wrong doing summarised

The best way of commencing a recital on the philosophy and character and the culture that the MAFs have come to internalise and promote is to reproduce the mock advertisement under the head 'Auditors Wanted' in the AABA study titled "DIRTY BUSINESS;THE UNCHEKED POWER OF MAJOR ACCOUNTANCY FIRMS": The mock ad reads [see box]

AUDITORS WANTED

Major British companies required technically qualified auditors. The work is unsuitable for those with a social conscience.

The job is extremely well paid and secure. The market for auditing is guaranteed by the state. You can audit the same company for years and there is no independent measure of your performance. The right candidate can earn bonuses and promotion by using audit as a market stall to sell other services. Specialists in tax avoidance/evasion are especially welcome. Training to launder money is available. Special bonuses for innovative ways of massaging company account, forming offshore companies, devising off-balance sheet financing schemes and lightening tax burdens for the rich.

Successful candidates should be ready to devise and use irregular practices and falsify audit work. The ability to shred key documents at short notice is an advantage. Our experience staff will provide expert training. You will not owe a 'duty of care' to any individual stakeholder. You will not be required to publish any information about your affairs. Your activities are lightly regulated by soft touch regulators who are sympathetic to auditors and their firms.

The standards of auditing are not demanding. Interest free loans, housing and favours from audit clients can be freely accepted. Fully bonded protection is available as our Institute is vastly experienced in whitewash and cover-up. You will learn how to individualise audit failures and blame everyone else for your shortcomings. No international regulator will gain access to your working papers. The Department of Trade and Industry will provide lucrative consultancy contracts but negligent audit firms will not be prosecuted. Political parties, politicians and ministers have been trained to understand your need.

Please do not apply if you have concerns about audit failures causing loss of pensions, jobs, investments, savings and taxes must not apply. Send your CV and a list of achievements to any major accountancy firm and the Institute of Chartered Accountants. Copies should also be sent to the Secretary of State for Trade and Industry, Department of Trade and Industry, 1 Victoria Street, London SW1H OET.

This mock ad speaks volumes about the philosophy, character, goals, strategies and methods of the MAFs.

The highly prejudicial records, performance and skills of MAFs and their global level malpractices and the concerns and consequences to the public at large summarised

Before going to the details of the contribution of individual MAF to the general kitty of the malpractices, and considering that they are all birds of the same feather, a helicopter view of their prejudicial record, performance and skill display and their global level malpractices and the concerns and consequences to the public at large should be summarised at the outset, even though it is difficult to choose where to begin first and how to order their wrong doings and to decide what to state first:

- **First, their ownership is secret; no one knows who their true owners are; their ultimate ownership is secreted away in tax havens; so they are global firms when they want to solicit business; but when the question of accountability arises, they claim to have no global character**

So, even as they claim to be global firms, they are actually global dodgers at law. That is contrary to the very purpose of their being - these firms which exist to ensure transparency in business accounts and finance are themselves secretive. They use this secrecy to claim to be global when it comes to seeking business opportunities, and disclaim to be global when it comes to answering global or local regulators, that is they dodge global and national regulators, exculpate themselves, and assist in illegal and even criminal activities.

- **Second, from around 1970's audit work has ceased to be their main income driver; now it is consultancy, which has become the other name for extra bonus to the MAFs to compromise on audit**

Today audit work is merely a marginal part of the multi-billion dollar income statements of the MAFs. Over 90% of their income in case of many critical clients cases, comes from consultancy services, which has become more or less the bribe that the clients pay to make them compromise with their independence in audit work. In fact some of them even accept audit for meagre fee, in return for lucrative consultancy assignments. The MAFs are more business corporates than professionals. All attempts of the regulatory authorities to de-link the audit and consultancy work have failed because of the unprecedented capacity of the MAFs to lobby out of all such attempts. Actually there are evidences to show that the MAFs merely use audit as a coercive mechanism to get consultancy.

- **Third, the MAFs have become skilled lobbyists and have become the tools in the hands of business to bribe the state and the regulators**

It is clear from the studies and reports which are now in the public domain, the MAFs spend millions of dollars for lobbying. In fact they accept lobbying assignments as part of their professional work. Many of them even make contributions to political parties. Thus they have become pincers for big business to deal with the state and the regulatory. They are no more professionals with independence.

- **Fourth, they have become experts in money laundering. They have become the wholesale dealers in off-shore companies which they sell off the shelf to the needy evaders of law**

A recent illustration of this dimension of the activities of the MAFs is KPMG which is perceived to be involved in laundering the corrupt and ill-gotten wealth of Ferdinand Marcos of Philippines to the tune of over $400

millions. It is now well known in business circles that the MAFs offer this services to their clients openly and not secretly or confidentially. They form off shore companies for their clients who evade taxes and launder money and they also manage it for them as part of their professional work.

- **Fifth, the MAFs have been repeatedly caught in frauds and malpractices which have forced them to seek compromises at billions of dollars of cost**

Each of the MAFs has been caught in different frauds in which they have either actively colluded with the offenders at law or they have been silent witnesses to the fraud with their silence having been purchased for tidy sums of consultancy fee and other means including off the record benefits to the partners and other officials of the MAFs. Theses settlements have resulted in pay outs for the MAFs in billions to those as reparations for the damage done to them by audits compromised by the MAFs. Ernst & Young which is the third largest of the four MAFs alone has paid over $.3.7 billions in different out of court settlements and fines.

- **Sixth, driven by their lust for money by any means MAFs are now turning into experts in shredding evidence and in suppressing facts and evidence, to escape the consequences of their fraudulent actions**

The famous Enron-Arthur Anderson episode has brought out another dimension of the MAFs. That is suppressing evidence if need be even by destroying them. This aspect which never got focussed when the BCCI fraud was being investigated in which PWC took a position that it could not make available to the US investigators the audit record of BCCI from London. The result of the position taken by PWC virtually derailed the investigation. This amounted to suppression of evidence. The same thing happened when Coopers and Lybrand which audited the Singapore branch of Barings Futures [Singapore] PTE limited, where the Barings fraud took place, clearly told the Bank of England that 'client confidentiality' prevented them from disclosing the audit papers of the Singapore branch. This too amounted to suppression of evidence. Now with the Enron fraud it has graduated to destroying evidence.

- **Seventh, the MAFs also are found to be manipulating privatisation policies of the Government and also gain by such manipulation and privatisation**

Unison which is a representative of over 1.2 million members drawn from different utilities has come out with a study demonstrably showing that the MAFs influence the privatisation policies of the Government and unethically and unprofessionally profit from them. They advise the Government on privatisation. They act as consultants for the privatising PSUs and at the same time act as statutory auditors of the contracting bidders. They are also mixed up with the officials and politicians who make the privatisation policies. Thus the MAFs are part of a huge manipulation mechanism in which they are the gainers. They also work with Governments in their countries to increase the export of privatisation expertise [in which the Governments in the West become part of the lobby] to developing countries like India to promote privatisation in those countries. That is they co-opt their own Governments for lobbying for privatisation in developing countries.

- **Eight, the MAFs are guilty of thousands of violations of audit independence and ethical requirements and are also guilty of acquiescing in fraud**

Though there are innumerable media reports on the violations of audit principles by auditors and of their acquiescing in frauds there is an official confirmation of this in the case of the largest of the MAFs. The Securities Exchange Commission of US reported that PWC alone is guilty of over 8000 violations of the basic rule of audit, that is the auditors should not hold investments in the companies which the audit. The Report estimated that 86% of the partners of PWC had at least one ethical violation. Repeatedly the MAFs have compounded by paying off actions against them for fraud.

- **Ninth, the MAFs are experts in advising tax-evasion and tax fraud to the clients on a global level causing losses to Governments of billions of dollars**

The study by AABA has shown that the MAFs specialise in consulting to avoid and evade taxes. They charge as much as $ 500 per hour for such consultancy. The estimated loss to the developing countries by such evasion is estimated at $ 50 billions and to the UK Government 85 billion Sterling.

Let us see in detail the wrong doings and malpractices of the MAFs summarised above.

The enormous public mischief and wrongdoings inherent in the very philosophy and structure of the MAFs: the different aspects of their wrong doing and malpractices explained in detail

The summarised version given earlier was considered necessary to demystify the mind of those in India who have reverential regard for the MAFs to prepare their minds for receiving the more detailed narration of the wrong doings. These narrations are from the work of media and from the study of the independent watch groups. Let us see in detail the wrongdoings and malpractices of the MAFs summarised earlier.

Global firms or Global dodgers? The issue of secret ownership of the MAFs and their accountability to national regulatory

How the ownership of the MAFs is kept buried in secrecy has been analysed by Mr Austin Mitchell, a Member of Parliament in UK and Mr Prem Sikka, Professor of Accounting in University of Essex, in a Study titled 'Dirty Business: The Unchecked Power Of Major Accountancy Firms' published by the AABA in the year 2002.

"The ownership structure of major accountancy firms is complex and secretive. Most seem to be ultimately owned by trusts registered in secretive offshore tax havens with no information sharing treaties with major nations. Such structures have been carefully developed to shield accountancy firms from public scrutiny and liability for their failures. The ultimate losers are the stakeholders affected by the failures of accountancy firms". [p 43]

Any one with basic familiarity with business knows that companies located in off shore tax havens prima facie desire that their ownership and even income structure should not be known. Can global accounting firms, which sit in judgement over the transparency of the client companies' transactions which they audit, themselves seek to hide themselves behind the secret maze of off shore tax havens. It is obvious. They have so much conceal about themselves. The very fact that these firms seek the protection of the secrecy laws of off shore tax havens should disqualify them from appointment as auditors to certify the accounts of corporations which are trusted by the shareholders and the general public on the strength of the certificate issued by these off shore global firm controlled national firms.

Why do the MAFs seek the protection of off shore tax havens to conceal their ownership? The

answer lies in the very study of Mitchell and Sikka mentioned above.

Mitchell and Sikka then trace how the MAFs which claim to be global firms for purposes of soliciting business for their different national member firms, turn the other way round and claim that they are not global the moment they are called upon to answer any regulatory for any wrong doing. Mitchell and Sikka have traced the conduct of MAFs in four cases. This is what they say:

THE GLOBAL UNACCOUNTABILITY

Increasingly, accountancy firms secure audits of major corporations by claiming that they are 'global' organisations (US Senate Committee on Foreign Relations, 1992). With the aid of private sector organisations, such as the International Accounting Standards Board (IASB) and the International Auditing Practices Committee (IAPC), the firms have sought to develop standards and pronouncements that reduce their training costs, dilute liabilities and hence increase profits. The same vigour is missing in developing organizational structures that would enhance accountability or require accountancy firms to cooperate with local/global regulators. Four examples illustrate the arguments. These relate to real/alleged audit failures at Bank of Credit and Commerce International (BCCI), Enron, Barings and International Signal and Control Group.

In July 1991, amidst allegations of fraud, the Bank of England closed down the Bank of Credit & Commerce International (BCCI), considered to be the "world's biggest fraud" (Killick, 1998, p. 151). At the time of its closure, BCCI operated from 73 countries and had some 1.4 million depositors. Whilst there has been no independent investigation of the real/alleged audit failures in the UK, an inquiry by the US Senate concluded that "Regardless of the BCCI's attempts to hide its frauds from its outside auditors, there were numerous warning bells visible to the auditors from the early years of the bank's activities, and BCCI's auditors could have and should have done more to respond to them. The certification by BCCI's auditors that its picture of BCCI's books were "true and fair" from December 31,1987 forward, had the consequence of assisting BCCI in misleading depositors, regulators, investigators, and other financial institutions as to BCCI's true financial position"6 (US Senate Committee on Foreign Relations, 1992, p. 4).

An examination of the working papers and files of the BCCI's auditors, Price Waterhouse (PW), had a considerable potential to provide public information about the organisational practices of auditing firms. It could also have provided some pointers for possible reforms. The US Senate sought access to auditor files. Despite claiming to be a 'global firm' Price Waterhouse remained reluctant to cooperate with international regulators. An investigation of BCCI by New York state banking authorities was also frustrated by the auditors' lack of co-operation. The New York District Attorney told the Congress that 6 It may be argued that auditors did not wish to qualify the accounts of a bank, for fear of causing a run. However, in 1999, PricewaterhouseCoopers issued a qualified report on the 1997-98 accounts of the Meghraj Bank, a major Asian bank with branches in the UK (Financial Times, 19 May 1999, p. 23)

"The main audit of BCCI was done by Price Waterhouse UK. They are not permitted, under English law, to disclose, at least they say that, to disclose the results of that audit, without authorization from the Bank of England. The Bank of England, so far -- and we've met with them here and over there -- have not given that permission. The audit of BCCI, financial statement, profit and loss balance sheet that was

filed in the State of New York was certified by Price Waterhouse Luxembourg. When we asked Price Waterhouse US for the records to support that, they said, oh, we don't have those, that's Price Waterhouse UK. We said, can you get them for us? They said, oh, no that's a separate entity owned by Price Waterhouse Worldwide, based in Bermuda".
Source: United States Senate Committee on Foreign Relations, 1992b, p. 245.

BCCI's auditors also refused to co-operate with the US Senate Subcommittee'sinvestigation7 of the bank (US Senate Committee on Foreign Relations, 1992, p. 256). Although the BCCI audit was secured by arguing that Price Waterhouse was a globally integrated firm (p. 258), in the face of a critical inquiry, the claims of global integration dissolved. Price Waterhouse (US) denied any knowledge of, or responsibility, for the BCCI audit which it claimed was the responsibility of Price Waterhouse (UK). Price Waterhouse (UK) refused to comply with US Senate subpoenas for sight of its working papers and declined to testify before the Senate Subcommittee on the grounds that the audit records were protected by British banking laws, and that "the British partnership of Price Waterhouse did not do business in the United States and could not be reached by subpoena" (p.256).

PwC website refers to the firm as a "global practice", but in a letter dated 17 October, Price Waterhouse (US) explained that the firm's international practice rested upon loose agreements among separate and autonomous firms subject only to the local laws:7 Price Waterhouse (UK) partners did agree to be interviewed by Subcommittee staff in PW's London office. The offer was declined due to concerns that the interviews would be of little use in the absence of subpoenaed documents (US Senate, 1992, p. 258).

"The 26 Price Waterhouse firms practice, directly or through affiliated Price Waterhouse firms, in more than 90 countries throughout the world. Price Waterhouse firms are separate and independent legal entities whose activities are subject to the laws and professional obligations of the country in which they practice... No partner of PW-US is a partner of the Price Waterhouse firm in the United Kingdom; each firm elects its own senior partners; neither firm controls the other; each firm separately determines to hire and terminate its own professional and administrative staff.... each firm has its own clients; the firms do not share in each other's revenues or assets; and each separately maintains possession, custody and control over its own books and records, including work papers. The same independent and autonomous relationship exists between PW-US and the Price Waterhouse firms with practices in Luxembourg and Grand Cayman".
Source: United States Senate Committee on Foreign Relations, 1992b, p. 257.

In December 2001, Enron, an energy conglomerate, became the world's biggest bankruptcy. Arthur Andersen, a worldwide accountancy firm, not only audited Enron's global business, but also provided numerous consultancy services, including internal auditing, tax and devising financial schemes. Andersen-Brazil rendered services for the Cuiaba, Brazil Power Plant. Andersen-India provided services related to the power plant in Dabhol. Andersen-UK provided services relating to commodities trading and the Wessex Water Company. Andersen cemented its close links with Enron by portraying itself as a global firm. As the events leading to Enron's bankruptcy unfolded Andersen allegedly engaged in a worldwide campaign to destroy any documents that could implicate it in the Enron frauds. In March 2002, a federal grand jury indicted Andersen on

charges that Andersen knowingly persuaded employees in Houston, Chicago, Portland and London to withhold records from regulatory and criminal proceedings and alter, destroy and shred tons of documents with the intent to impede an investigation. A federal jury convicted Andersen on 15th June 2002. The 'global' credentials of accountancy firms once again came under scrutiny. Andersen website claims that the firms trading as Andersen trade under a "common brand, philosophy, technologies and practice methods [and have a worldwide] Board of Partners", but n response to lawsuits and requests for documents, the firm claims that Arthur Andersen is not global. An official statement said that "Arthur Andersen LLP [the US firm], an autonomous member firm of the Andersen Worldwide SC organisation, contracted with, performed the audits of, and signed the audit opinions on Enron's financial statements. Accordingly, Arthur Andersen LLP is the only proper defendant in claims relating to that audit opinion". John Ormerod, managing partner of Andersen in the UK, said:

"Naming our firm as a defendant has no legal basis. While we have sympathy for those affected by Enron's failure, Andersen in the UK has no obligation to satisfy the legal liabilities of other member firms."

Source: http://www.accountingweb.co.uk; 9 April 2002.

The third example is Barings. On 26th February 1995, amidst revelations of £827 million fraud, Barings Plc collapsed (Bank of England, 1995). For many years prior to the collapse, Barings had been audited by Coopers & Lybrand (C&L). The Singapore office of C&L was appointed to audit the affairs of Baring Futures (Singapore) Pte Limited (BFS) for the year to 31st December 1994. The 1992 and 1993 accounts of BFS were audited by the Singapore office of Deloitte & Touche (D&T) who reported to C&L London for the purposes of its audit of the consolidated financial statements of Barings plc. C&L audited all other subsidiaries of Barings in 1992, 1993 and 1994 either through its London office or other offices spread around the world. As part of its inquiry, the Bank of England (BoE) sought access to the auditor files but the audit firms did not cooperate. The BoE noted, "We have not been permitted access to C&L Singapore's work papers relating to the 1994 audit of BFS [Baring Futures (Singapore) Pte Limited] or had the opportunity to interview their personnel. C&L Singapore has declined our request for access, stating that its obligation to respect its client confidentiality prevents it assisting us". "We have not been permitted either access to the working papers of D&T or the opportunity to interview any of their personnel who performed the audit. We do not know what records and explanations were provided by BFS personnel to them".

Sources: Bank of England, 1995, pp. 15 and 153.

The organisational structures and practices of accountancy firms also came under scrutiny in the aftermath of the financial problems at Ferranti, caused by the US$1 billion fraud at one of its subsidiaries, International Signal and Control Group Plc (ISC). The company was primarily engaged in the design and manufacture of military equipment. In 1987, the ISC and its subsidiaries, including a company called Technologies, were acquired by Ferranti. Technologies had factories and head office in the US and was audited by Peat Marwick Mitchell (PMM), subsequently part of KPMG. Over a period of time, $1 billion worth of fraudulent contracts had been placed on ISC's balance sheet. Some directors of ISC had been engaged in a massive fraud and money

laundering operation through shell companies in Panama, Switzerland and the US. The company's directors allegedly laundered $700 million through the network of Swiss and US bank accounts. Fictitious contracts and transactions were created through offshore companies to boost profits. Following an investigation in 1988, ISC's founder and director pleaded guilty and was given a prison sentence. Ferranti bought the company without any knowledge of the frauds and sued auditors for negligence. An out of court settlement of £40 million was reached.

In response to complaints, the Joint Disciplinary Scheme (JDS), an organization operating on behalf of the UK accountancy trade associations, was asked to investigate the matter. It sought sight of the audit working papers for the period 1986 to 1989. Its report noted that

"It quickly became clear that a substantial part of the audit work for Technologies had been undertaken on behalf of PMM in London by the American firm of the same name. .... considerable difficulties were experienced in gaining such access. ... I was informed that it was not that firms' policy to make papers available in situations of this kind. .... Copies of the American firm's working papers were eventually made available, "exceptionally and in order to assist the investigation", at the offices of a law firm in New York. ..... The copy files produced in New York were inadequate for the purposes of the investigation and it was necessary to arrange access to be gained to the original files. I was told that these were in the possession of the US Attorney in Philadelphia. My investigating accountants went there to examine them. They discovered that many of the files relevant for my purpose had remained in the possession of PMM. The firm had considerable difficulty in locating these files. Once they had been found a third visit to America was arranged. My investigating accountants were not permitted to photocopy relevant material of an [sic] any of American firm's files, rendering extensive note-taking necessary."

Source: Joint Disciplinary Scheme, 1996, p. 7.

The structure of major accountancy firms has been carefully organised to maximise their profits and minimise accountability. Major accountancy firms use the same name, logo and stationery and advertise themselves as 'global' organisations. They claim to have the 'global' structures and organisation to audit businesses and sell integrated consultancy services. The firms secure business by parading their 'global' credentials. Their partners share revenues generated by global clients.

Episodes such as Enron, BCCI, Barings and other episodes show that when the firms are called to account, their charade of being 'global' dissolves away. At critical times, major firms claim that they are no more than a disparate collection of 'national' firms or franchised businesses. As the Manhattan district Attorney put it, "Even McDonald's has more control over its franchises" (New York Daily News, 10 January, 1999).

It is evident from the study of Mitchell and Sikka that the MAFs have a design in locating their ultimate control in off shore tax havens. The intent is to avoid and evade law regulatory from linking national firms to the controlling firm. So the MAF are not global firms. They are global dodgers at law.

How consultancy, not audit fee drives the top line and bottom like of the MAFs and how consultancy fee has become a tool to bribe and compromise the MAFs

In recent times, particularly in the context of the exposure of the Enron fraud, no issue has received such wide attention as the disproportionate consultancy fee arising out of

the consultancy assignments handled by the MAFs as statutory auditors from their clients. The enormity of this issue was always in the radar of the regulatory in the USA but owing to the power of the MAFs to lobby their way through, the regulatory repeatedly failed in its effort to discipline the MAFs.

In their study [Dirty Business] Mitchell and Sikka bring out the enormity of the problem [see box]

MONEY, MONEY, MONEY

Paralleling a fateful remark of General Ratner's to the effect that his shops sell 'crap', the chairman of Coopers and Lybrand (now part of PricewaterhouseCoopers) stated that "there is an industry developing, and we are a part of it, in [accounting] standards avoidance" (Accountancy Age, 19 July 1990, p. 1). In this environment, firms will do almost anything to make a fast buck.

Double Digit Growth

An analysis of the fees paid by the FTSE 350 companies shows that only 27% of the fees paid to auditing firms are for the audits (Accountancy, October 2001, p. 7). The consultancy income from some clients companies dwarfs the audit fees.

SOME EXAMPLES OF FEES PAID TO MAJOR AUDIT FIRMS

Company	Audit Firm	Audit Fee £m	Non-audit Fee £m
AstraZeneca	KPMG	2.14	9.31
BAE Systems	KPMG	3.03	16.21
BP Amoco	E&Y	18.70	34.20
British Airways	E&Y	1.25	4.07
CGNU	PwC/E&Y	6.70	43.00
Cable & Wireless	KPMG	2.70	17.00
Kingfisher	PwC	1.60	8.30
Lloyds TSB	PwC	4.00	32.00
Prudential	KPMG	1.90	18.80
J. Sainsbury	PwC	0.70	12.90
Scottish Power	PwC	1.50	11.40
Shell T&T	PwC/KPMG	11.40	31.50
Unilever	PwC	8.17	39.00
United Business	PwC	0.60	13.30
Vodafone	D&T	3.00	22.00
WPP	AA	3.70	6.40

Source: Accountancy, October 2001, pp. 72-73.

Audit gives accountancy firms easy access to company directors and a competitive 'inside' advantage over their consultancy rivals. They use audits as a stall to sell executive recruitment, internal auditing, financial engineering, advice on mergers, downsizing, information technology, trade union busting and tax avoidance. For a fee, some firms will front shell companies, act as company directors, post boxes, print T-shirts and badges and lay golf courses. In pursuit of money they have become part of client companies and an extension of their finance and personnel departments. Instead of conducting 'independent audits', major firms offer 'consultancy audits' where the aim is to maximize the opportunities to sell consultancy services. All this has enabled them to achieve double-digit growth in profits and fees.

The Enron scandal has shown that major accountancy firms exert pressures on partners and senior staff to increase revenues and profits. Those doing that are rewarded with status, bonuses and salary increments. Some firms intimidate audit clients in an effort to sell consultancy work. Angered by a client who used the services of an independent consultancy company to value its brands for accounting purposes, the audit firm threatened the client suggesting that audit costs and 'problems' would rise if the independent

consultancy company was used in preference to the firm's consultancy division (Accountancy Age, 14 February 1991, p. 1 and 17; Accountancy, March 1991, p. 11). The consultancy company complained to the ICAEW by arguing that "We find attempts to cajole clients into using consultancy services by threat of "problems" exceptionally seedy and unpleasant" (Accountancy Age, 14th February 1991, p. 17). The ICAEW did its usual whitewash.

A myth promoted by the accountancy industry is that the purchase of auditing and non-auditing services from the same firm somehow results in lower costs. Such myths are not supported by research (Simunic, 1980, 1984). This shows that when management invite competitive tenders, shop around and purchase auditing and non-auditing services from two separate firms, they get a lower price. As Simunic (1984) concludes, "audit fees for clients who purchased MAS [Management Advisory Services] from their auditors are higher than those of clients who did not do so" (p. 699).

Thus it is not just that the MAFs get consultancy arrangements for their undisputed competence. They solicit them. Even coerce the clients on pain of adverse audit remarks to give consultancy assignments to them. They charge predatory audit prices to get consultancy work; the proportion of the audit fee has rendered audit work irrelevant except as a tool or a mechanism to get consultancy assignments.

In an article titled 'How Independent are those book checkers' published in US News and World Report, Marianne Lavelle says that only 27% of the fee paid to the auditors by companies was for audit work. The balance fee 'went for services that the so called Big Five accounting firms have branched into, from information technology to management consulting'. The author says that 'An SEC analysis of 563 proxy statements filed by big companies shows Big Five firms made $ 5.8 millions in non audit fees from the average client, while pulling of only $ 2.2 million for audit work.

An illustrative sample of the relative fee for audit and non-audit [consultancy work] paid by some of the leading corporates is revealing:

Marriot Ltd paid to Arthur Anderson a total fee of $. 33,331, 300, out of which the non audit fee amounted to 96.65%

Sprint paid a total fee of $ 66,300,000 to Ernst & Young, out of which the non-audit fee amounted to 96.23%

Raytheon paid a total fee of $ 51,000,000 to Pricewaterhouse Coopers, out of which the non-audit fee was 94.2%

Motorola paid a total fee of $ 66,200,000 to KPMG out of which the non-audit fee amounted to 94.11%

Gap paid a total fee of $ 8,245,000 to Deloitte and Touche out of which the non audit component was 93.10%

How and when did this change take place? In an article by Daniel L Berger and Blair Nicholas carried in the web site 'The Cat bird Seat' the authors say under the subtitle to the article ' the metamorphosis of the auditing profession: the watchdogs become the puppies of the management':

The Metamorphous [sic] of The Auditing Profession: The Watchdogs Become the Puppies of Management

In the 1970s, accounting firms like **Ernst & Young** and **PWC** functioned largely as independent auditors. Business consulting was merely an offshoot of traditional accounting and auditing - a way to derive more income from the

same base of clients. But the consulting business took off beginning in the mid-1980s, when consultants from large auditing firms won over the trust of corporate chief financial officers and landed huge technology consulting projects.

Today, corporate accounting firms view auditing as a low-profit, low-growth service of diminishing importance, and have instead focused their resources on the more profitable and faster growing non-audit services, including business consulting, tax consulting, human resources consulting, and corporate finance consulting. As a result, non-audit consulting fees have increased as a percentage of the largest accounting firms' revenues from 15% in 1978 to 24% in 1990 and to 38% in 1996.

This explosion in growth and demand for non-audit services has resulted in auditing firms "lowballing" their quoted auditing fee (whereby firms offer big reductions in their audit fees), in order to more easily leverage themselves into the companies to cross-sell the firm's more profitable non-auditing services, usually on a no-bid basis. For example, in 1991, **PWC** won a contract to audit **Prudential** after offering a discount of almost 40% off its original quote.

By the time **Prudential dropped PWC** as its auditor last year, PWC's annual consulting fee was more than 300% greater than PWC's annual audit fee. What is the reasonable investor to think when an auditing firm certifies a company's financial statements as complete and accurate, yet the auditing firm is generating three times its auditing fee from providing business consulting to the same company?

Clearly, the independence of the auditor is contaminated, the auditor is more reticent than ever to disagree with corporate management on financial reporting issues, and the credibility of an industry which is suppose to be free of potential or actual **conflicts of interest** is diminished. **Auditing the Auditors**

As business consulting services continue to grow at a rapid clip in this Internet age and auditing firms continue to direct more of its resources toward providing non-audit services to its clients, the issue of auditor independence will only intensify. In fact, Lynn Turner, chief accountant for the SEC, recently advocated that public companies should disclose all business links with outside auditors so shareholders can better evaluate possible **conflicts of interest.**

Ms. Turner stated that "given the explosion of these [non-audit] services, it's time for the public to know" and urged that mandatory disclosure of possible **conflicts of interest** should be required by the Independence Standards Board, a self-regulatory organization, or a new SEC rule. Clearly, someone needs to watch the watchdog.

The SEC's willingness to raise tough questions about **conflicts of interest** has been rewarded by the recent separation of auditors' consulting arms. **PWC** recently announced that it will split its business into two parts, with separate management teams and boards, one to run the audit business, the other to run the consulting business. Similarly, following the SEC's report exposing PWC's ethical violations, Ernst & Young sold its consulting arm to Cap Gemini, a French computer-services company.

The SEC should keep the heat on auditing firms to divest or at the very least, come up with some reorganization scheme that protects shareholders from actual or potential **conflicts of interest.**

Independence and integrity have always been the bedrock of the accounting profession and, in order to inspire investor confidence in the integrity of the American financial market, the auditor must remain independent.

As the writers say, in 1970s the MAFs functioned largely as independent auditors. It

was only in mid-1980s the consulting business took off. This also coincided with the arrival of the derivative trading and other financial instruments in the international finance market. The scope of the accounting-consulting profession expanded dramatically since then.

MAFs as skilled lobbyists and as tools in the hands of business to bribe the state and the regulators

From being merely specialists in audit services, the MAFs turned into consultants with a catch all and hold all consultancy packages, and finally they have turned into lobbyists and pincers for their clients with the Governments, regulators, and even politicians and political parties. This is undoubtedly a dangerous development for a profession which owes a duty to care to the investors who rely on their certificates and risk their money. The facts marshalled in the website The Catbird Seat are amazing and should be extensively communicated to create awareness in the system and also among the public.

In an article written by John Dunbar and Natheniel Heller in 'The Public I' and carried in The Catbird Seat website, the authors say:

"Arthur Andersen LLP, the accounting firm that has been implicated in the collapse of **Enron Corp.,** was a top contributor to **President George W. Bush's** political campaigns. (See the tables below)

Since 1998, Andersen and its employees have contributed $212,825 to Bush, including $25,000 in donations to Bush's inaugural celebration when he was governor of the state of Texas. The total makes Andersen one of Bush's biggest financial backers.

Overall, since 1998, Andersen has spent $8.1 million to influence the federal Government, including $6 million on lobbying expenditures. Like its client Enron, Andersen had strong ties to the Bush campaign and administration. Two former lobbyists for the firm now occupy high-level positions in the administration.

Stephen Goddard Jr., a managing partner in charge of Andersen's Houston office who was relieved of management responsibilities on January 15, 2001, was a Bush "pioneer," meaning he raised at least $100,000 for Bush's presidential campaign.

Andersen's political action committees also gave generously to members of Congress. They contributed $27,000 to **Rep. Billy Tauzin** (R-La.) over the last three years. Tauzin, the chairman of the **House Energy and Commerce Committee,** is currently leading one of the congressional investigations of Enron and Andersen. Over the last three years, he's been the top congressional recipient of Andersen political action committee contributions, according to the Center for Responsive Politics.

In researching "The Buying of the President 2000," the Center determined Andersen was **Bush's 13th largest career patron** through June 30, 1999. By comparison, former **Vice President Al Gore** received $8,200 from Andersen employees when he ran for president, according to documents from the Federal Election Commission.

Capitol Hill connections

The company's political action committee has spent **$1.3 million** on House and Senate members since 1998, with Democrats receiving slightly less than half as much as Republicans. Among the recipients was current **Attorney General John Ashcroft,** who accepted $10,000 for his unsuccessful Senate reelection campaign, according to CRP.

Ashcroft recused himself from the criminal investigation of Enron after the Center reported

one of his campaign committees received a $25,000 contribution from the company.

Andersen also spent a little over $500,000 in unregulated, soft money contributions to political parties, the vast majority going to the GOP.

Outstripping those numbers by far, however, is the amount Andersen spends on **lobbying.** Since 1998, the company has spent **$6 million** in-house on lobbying Congress, according to lobby disclosure records. They also retained outside firms to lobby for them.

Among the issues the company pushed was legislation to consider the retail **deregulation** of the electric utility industry, a key issue for Enron and its chairman, **Kenneth Lay.**

Andersen's stable of lobbyists includes names from Washington's power elite.

Former Andersen lobbyists Nicholas Calio and Kirsten Ardleigh Chadwick, who worked for the firm O'Brien Calio, now head up President Bush's legislative affairs office at the White House.

The two are the White House's top lobbyists to Congress and are charged with pushing the administration's legislative agenda on Capitol Hill.

According to federal lobbying records, Andersen paid O'Brien Calio $60,000 to lobby on **Internal Revenue Service** reform legislation in the first half of 1998. Calio and Arleigh Chadwick worked on that effort, according to the lobbying disclosure form. They moved to the White House shortly after President Bush's inauguration.

Interests beyond accounting

Andersen began **lobbying** on the issue of **electricity deregulation** as early as 1996, and continued into 1998. Enron had been trying to get Congress to create a wholly competitive environment in the electric utility industry for years. One state that deregulated, California, still has utilities that owe millions of dollars to Enron. Similar efforts to pass legislation to deregulate electric utilities at the federal level have failed.

Andersen has also spent large amounts of money to influence the **Securities and Exchange Commission** to allow large accounting and consulting firms to perform both services for their corporate clients."

Another source mentioned in the same website gives the break up of PwC's lobbying expenses and revenue earned through lobbying, which is interesting as well as instructive:

From *opensecrets.org*
1998 Profile: PricewaterhouseCoopers
Total Lobbying Expenditures: $960,000.
Total Lobbyng Income: $6,500,000.
~ ~ ~
Some of PricewaterCoopers' Lobbying Clients
El Paso Energy
Electronic Commerce Tax Study Group
Enron Corp
Entertainment & Media Cybertax Study Group
Equitable Companies
Fremont Group Inc
General Electric
Goldman, Sachs & Co
IBM Corp
Kamehameha Schools/Bishop Estate
Morgan Stanley Dean Witter & Co
Multinational Tax Coalition
Section 41 Coalition
Securities Industry Assn
Shell Oil
Starwood Capital Group
Walt Disney Co.
* * *

So a good margin of over 85% in the lobbying business, the lobbying revenue is $6.5million

and the expenditure is a bare $960,000. So lobbying is not a side show. It has become a focus area for MAFs. The following extracts from the report of an SEC official dated 26 January 2000, reproduced in The Catbird Seat website, is also revealing:

"During my seven and a half years in Washington, I was constantly amazed by what I saw. And nothing astonished me more than witnessing the powerful special interest groups in full swing when they thought a proposed rule or a piece of legislation might hurt them, giving nary a thought to how the proposal might help the investing public. With laser like precision, groups representing Wall Street firms, mutual fund companies, **accounting firms,** or corporate managers would quickly set about to defeat even minor threats.

Individual investors, with no organized lobby or trade association to represent their views in Washington, never knew what hit them....

The American Institute of Certified Public Accountants is another major player on investment issues. It represents 330,000 individual CPAs but is dominated by **PricewaterhouseCoopers, KPMG, Deloitte & Touche, Ernst & Young, and what's left of Arthur Andersen.** It has a **$140,000,000 budget** and employs fourteen lobbyists, three of whom lobby full-time, but the real source of its clout is a widely dispersed membership. Every Congressional district is home to hundreds of CPAs who are often prominent members of the community. They frequent the local golf course, are active in local business clubs, and contribute to local politicians.

I saw the AICPA unleash this grass-roots force when the SEC was pursuing stiffer auditor independence rules. The SEC and Congress within weeks heard from thousands of accountants. Many of their written comments were suspiciously alike; the AICPA had mass-mailed sample letters, and members dutifully copied them and sent them under their own names. The same goes for the letters the SEC received from Capitol Hill. Lawmakers put their own signatures on letters that were word-for-word the same, written by accounting lobbyists"

Some of the MAFs, particularly PwC, seem to have connections with the controversial US espionage agency, the CIA [Central Intelligence Agency]. Look at the following source listed in The Catbird Seat website:

CIA "Fronts"
From: HarrySweeney<Sweenfam@teleport.com>
Newsgroups: alt.politics.org.cia
Subject: Re: Known CIA fronts (200+ listed here)

Date: 20 Sep 1996

Organization: Teleport - Portland's Public Access (503) 220-1016

The following several hundred firms and persons represent "suspected" or reported fronts as found in various published resources or based on my personal beliefs arrived at through personal experience and research.

Most of these are out of date, out of business (disbanded or evolved to some new operation), but the list serves as example of the marvellous diversity and clever (or not so clever) naming conventions applied. . . .

Keep in mind that there ARE NO FRONTS. CIA was ordered by Congress to divest, and they have. The CIA obeys Congress and the law... by "selling" the fronts to "retired" CIA.

Of course, if they should still do favours for CIA, that would be OK. If CIA gives them business, that would be OK. So it is business as usual, with LESS oversight by Congress, thanks to their "crack down" on errant CIA activities. . . .

Here are just a few familiar names from Harry Sweeney's list:

.....

.....

.....

Pricewaterhouse (not a true front, but, certified obviously fraudulent books for CIA fronts) : Johathan Kwitny, *The Crimes Of Patriots*

.....

Even in its association with the CIA the MAF appeared to have only used its specialised knowledge in the area of its expertise, to fudge the CIA accounts. It is evident from its link with the CIA, particularly that the CIA had chosen the MAF for a highly confidential assignment of certifying fudged accounts of the espionage organisation, that the powerful spy agency must be obliged to the MAF. This shows the extent of their penetration into the highest and the most sensitive echelons of power. There can be no greater evidence of their lobbying power than such critical piece of information as this. Also this kind of information is not easily available in the public domain. Such leaks are, and can only be, just tips of the iceberg.

The lobbying power of the MAFs is not limited to the lobbying fee received by them and their lobbying budget. It includes more sophisticated methods, like secondment of MAF officials to the state to influence policies, manipulations of policies through different methods which will be explained at another place.

The expertise of MAFs in money laundering and their skill in forming and managing off-shore companies for the benefit of the needy evaders of law. In the end not just professionals for fraudsters, but their accomplices and co-sharers

In their study 'Dirty Business' Mitchell and Sikka extensively deal with the issue of money laundering by MAFs and their skill in promoting and helping tax evasion and avoidance. The facts brought out by them are amazing and need to be set out in detail.

All over the world, ordinary people bear a higher share of tax to finance essential social infrastructure. This burden is increasing because a rich elite and many major corporations are avoiding taxes through novel avoidance schemes. Major accountancy firms charge around £500 per hour to devise elaborate schemes for tax avoidance. Accountancy firms such as Arthur Andersen, KPMG, Deloitte & Touche, Price water houseCoopers (PwC) and Grant Thornton have become multinational enterprises by advising companies on strategies for avoiding taxes (New York Times, 16 April 2002). A favourite tactic is to advise major corporations and the rich to escape to secretive offshore tax havens. Developing countries are losing some US$50 billion due to tax avoidance. The UK taxpayer is estimated to be losing some £85 billion of tax revenues (Mitchell et al., 2002). Inevitably, ordinary people bear the cost of this by paying a higher proportion of their income in taxes and receiving worse public services.

With the rise of information technologies, deregulation, globalization and easy transfer of money, accountancy firms have added money laundering to their list of profitable services. More than US$1.6 trillion (roughly equivalent to the gross national product of France) is estimated to be laundered each year. Most of the money comes from tax evasion, illicit trading, narcotics, bribery, smuggling, murder, slavery, pornography, robberies and prostitution. The illicit cash is turned into cybercash and transactions through shell companies and bank accounts. Accountants and lawyers, whose main concern is to secure private fees, front many of these. Their reward is around 20% of the money

laundered. No one can launder large amounts of monies without the direct or indirect involvement of accountants. Accountants report less than 1% of the suspicious transactions reported to the National Criminal Intelligence Service (NCIS).

TOTAL NUMBER OF DISCLOSURES MADE TO NATIONAL CRIMINAL INTELLIGENCE SERVICE

YEAR	TOTAL DISCLOSURES	DISCLOSURES BY ACCOUNTANTS	DISCLOSURES BY SOLICITORS
1992	11289	1	4
1993	12750	2	4
1994	15007	6	86
1995	13710	38	190
1996	16125	75	300
1997	14148	44	236
1998	14129	98	269
1999	14500	84	291
2000	18408	77	249

Source: Annual Reports of the National Criminal Intelligence Service.

Each year the NCIS complains that accountants do not report money laundering and suspicious transactions to it. In response, the DTI Ministers wring their hands and the accountancy trade associations make pious statements. The 'Proceeds of Crime Bill' proposes to make it a criminal offence for accountants not to report any suspicions or dubious transactions to the National Criminal Intelligence Service (NCIS), as well as the Inland Revenue. In response, the ICAEW claims that the "government plans to crack down on money laundering could be very damaging economically and pose a serious threat to the role of the accountant" (http://www.accountingweb.co.uk, 6 June 2001).

Evidence relating to the involvement of accountancy firms in money laundering is not hard to find. In a High Court case, Lord Justice Millett pointed the finger at accountants and accountancy firms and said that

"Mr. Jackson and Mr. Griffin knew .... Of no connection or dealings between the Plaintiffs and Kinz or of any commercial reason for the Plaintiffs to make substantial payments to Kinz. They must have realized that the only function which the payee companies or Euro-Arabian performed was to act as "cut-outs" in order to conceal the true destination of the money from the Plaintiffs .... to make it impossible for investigators to make any connection between the Plaintiffs and Kinz without having recourse to Lloyds Bank's records; and their object in frequently replacing the payee company by another must have been to reduce the risk of discovery by the Plaintiffs".

"Mr. Jackson and Mr. Griffin are professional men. They obviously knew they were laundering money. .... It must have been obvious to them that their clients could not afford their activities to see the light of the day. Secrecy is the badge of fraud. They must have realized at least that their clients might be involved in a fraud on the plaintiffs".

‘‘Jackson & Co. were introduced to the High Holborn branch of Lloyds Bank Plc. in March 1983 by a Mr. Humphrey, a partner in the well known firm of Thornton Baker [now part of Grant Thornton]. They probably took over an established arrangement. Thenceforth they provided the payee companies... In each case Mr. Jackson and Mr. Griffin were the directors and the authorised signatories on the company's account at Lloyds Bank. In the case of the first few companies Mr. Humphrey was also a director and authorized signatory".

Source: High Court judgement in AGIP (Africa) Limited v Jackson & Others (1990) I Ch. 265 and 275; also see Mitchell et al., 1998.

In the above case, 27 separate companies were used to launder money, making it difficult to trace the source and destination of the proceeds. The paper trail went from Tunisia, London, the Isle of Man and Jersey to France and beyond. Most of the companies never traded but millions passed through their bank accounts. Accountancy firms collected fees for forming, operating and liquidating the shell companies. Despite the very clear and strong court judgement, there was no independent investigation or inquiry. The ICAEW and the UK government did the usual whitewash. Their main priority, as always, was to shield accountancy firms and their partners (Mitchell et al., 1998). Not surprisingly, money laundering is on the increase and accountancy firms don't bother to report suspicious transactions to the authorities.

To maintain their growth in profits, accountancy firms constantly need to find new ways of making money. Anything and everything is commodified to make money. Some firms have little hesitation in bribing officials to ensure that their 'private' interests triumph over the wider social interests.

"In 1996, the US regulators concluded a case involving the bribery of bank officers in U.S. and foreign banks in connection with sales of emerging markets debt, transactions that earned millions for the corrupt bankers and their co-conspirators. In this case, a private debt trader in Westchester County, New York, formerly a Vice President of a major U.S. bank, set up shell companies in Antigua with the help of one of the **"big-five" accounting firms.** Employees of the accounting firm served as nominee managers and directors. The payments arranged by the accounting firm on behalf of the crooked debt trader included bribes paid to a New York banker in the name of a British Virgin Islands company, into a Swiss bank account; bribes to two bankers in Florida in the name of another British Virgin Islands corporation and bribes to a banker in Amsterdam into a numbered Swiss account" [emphasis added].Source: Evidence by Robert Morgenthau, New York District Attorney, to the Permanent Subcommittee on investigations on 18 July 2001 (http://www.senate.gov/~gov_affairs/071801_psimorgenthau.htm)

The shell company in the above case went under the name of Merlin Overseas Limited. There was no actual physical business in Antigua, named Merlin. It consisted of little more than a fax machine in a Caribbean office of Pricewaterhouse (New York Daily News, 10 January 1999). "This accounting company was complicit", said Robert Morgenthau, the Manhattan district attorney. "They facilitated hiding of bribes that were paid to bank officers and they provided the officers and directors for those phoney companies". Morgenthau prosecuted the rogue at the centre of the scheme but could not put his hands on Pricewaterhouse. The district attorney's office asked Pricewaterhouse in Manhattan for help in reaching the people behind Merlin, but the help was not forthcoming. They were told that the Pricewaterhouse in Antigua is not the same legal creature as the one in New York.

All over the world major accountancy firms are facilitating anti-social activities. They obstruct inquiries into frauds and fiddles and shield money launderers and fraudsters.

"In 1996, the U.S. Department of Justice came into possession of a tape containing computerized records of a defunct Caymans bank, Guardian Bank and Trust Company. The bank was started by John Mathewson, a businessman from Illinois. Years after opening a numbered Swiss bank account whilst

vacationing in the Caymans, he was persuaded by a Caymans banker to start his own bank. According to Mathewson, his application for a bank license asked for little more than his name, address and previous bank history. The bank was set up and used to launder money for its depositors, 95% of whom were U.S. residents. Fake invoices to enable U.S. citizens and corporations to disguise deposits were used. The government of Cayman sought to block the release of banking information and refused to help the FBI to decode computer records. The official Cayman liquidators of the bank **(two partners in another major world-wide accounting firm)** brought a suit in the U.S. District Court in New Jersey seeking the return of the computer tape to the Caymans. In their brief, the liquidators argued that disclosure of the contents of the records to, among others, the U.S. Internal Revenue Service would "Have a significant negative impact on the integrity, confidentiality, and stability of the financial services industry of the Cayman Islands. .... The confidence of the offshore financial community in the privacy afforded to legitimate account holders of Cayman Islands offshore banks is at the heart of the Territory's financial services industry and economy, as a whole.....

Thus, not only would the Bank be irreparably injured by the government's retention of the Tape, but the international bank and Eurocurrency industries of the Cayman Islands (and, indeed, the economy of the Territory), could suffer irreparable injury as well". After decoding the tape without the help of the Caymans government, the US authorities discovered that the Guardian Bank's U.S. depositors has $300 million offshore, hidden from tax authorities, litigants and creditors. In view of his help to the US authorities, Mathewson was given a five year suspended prison sentence and said, "I have no excuse for what I did in aiding US citizens to evade taxes, and the fact that every other bank in the Caymans was doing it is no excuse".Source: Evidence by Robert Morgenthau, New York District Attorney, to the Permanent Subcommittee on investigations on 18 July 2001 (http://www.senate.gov/~gov_affairs/071801_psimorgenthau.htm); also see The Times, 4 August 1999, p. 16; Mitchell et al., 2002.

The Mitchell-Sikka study is a shocking revelation of the extent to which the MAFs have degenerated in their pursuit of money. But despite all this they have been able to maintain a thick veneer of professionalism through their powerful brand building methods. Particularly in India they have invaded the Indian consulting market with such brand effect and good will which is the very reverse of their real character. While the Indian CAs had been vilified as promoters of tax evasion, the MAs who have global tax evasion and money laundering a business, and yet they are respected and revered in India.

But the story of money laundering by MAFs will be incomplete without reference to the apprehended role of KPMG in the laundering of the corrupt and ill-gotten wealth of Ferdinand Marcos, the deposed dictator of Philippines. This fraud has been brilliantly exposed by Lucy Komisar, in an article under the title 'Marcos' missing millions' This article dated August 2, 2002, has been carried in the website The Catbird Seat. The entire article is reproduced below for a full understanding of the culture and drive of the MAFs, and particularly KPMG which is believed to be involved in this fraud.

Corporate corruption scandals roil the United States, dragging down with them the reputations of the major accounting firms that signed off on--or even designed--fraudulent financial practices. These global auditors were supposed to keep corporations honest. But a closer look at Switzerland, the birthplace of financial legerdemain, shows that accounting deceit is nothing new. Western financial managers cut their teeth designing systems for Third World dictators to loot their countries.

Perhaps the most notorious example is **Ferdinand Marcos,** who is suspected of stealing at least **$10 billion** from the Philippines before being overthrown in February 1986. The Philippine Government has spent more than 15 years trying to track and recover the money, some of which was secreted away by Swiss bankers and stashed in offshore havens.

Now, a former attorney with accounting firm **KPMG** in Zurich has come forward claiming she has evidence that on March 23, 1986----just a day before a freeze would be placed on Marcos' accounts -- **KPMG** secretly transferred **$400 million** from **Credit Suisse Zurich** to a Liechtenstein trust on the ex-dictator's behalf.

The attorney, **Marie-Gabrielle Koller** -- named in this article for the first time -- first testified about the events behind closed doors before a French parliamentary commission in May 2000. Its report referred to her only as "**Madame Z.**" Last year, the Quebec native sent her information to U.S. authorities, but elicited no interest from Washington. Now Koller, 46, has privately offered to provide evidence to the Philippine government in exchange for a cut of the amount recovered. With interest, the hidden **$400 million** would be worth twice as much today.

Koller didn't join **KPMG** until 1996, when she was assigned to the **Credit Suisse** account -- a decade after the Marcos government fell. She learned of the midnight Marcos money-laundering operation from a colleague that year, after a Zurich court ordered the transfer to the Philippines of another account -- originally worth $356 million -- frozen in Switzerland since 1986.

That money had been held on the basis of documents found in the Presidential Palace days after Marcos fled to **Honolulu** in February 1986. But there were no documents about the **$400 million.** Bank officials had been warned that the Swiss Banking Commission, bowing to international pressure, was about to freeze all suspected Marcos accounts.

So, in the dead of night on March 23, 1986, lawyers for **KPMG** (then known as Fides, a subsidiary of Credit Suisse) moved the **$400 million in Marcos funds** to a Liechtenstein trust, **Limag Management und Verwaltungs AG** -- which dispersed the money via new secret "foundations" (in German, anstalts). **Limag AG** was headed by **Peter Sprenger,** also the director of **Liechtenstein's Credit Suisse Trust AG** and parliamentary leader of the **Vaterlandische (Fatherland) Union,** one of Liechtenstein's conservative main parties.

Europeans joke that **Liechtenstein** is where Swiss bankers go to hide their money. The tiny country, just 72 miles east of **Zurich,** is the place where the Swiss send their dirtiest customers. **Liechtenstein** has gotten rich **by laundering the money of drug traffickers, Mafiosi, tax cheats and other criminals.**

A 1999 report from the German secret service described Liechtenstein as a criminal state in the middle of Europe. The German finance minister denounced the country as "a worm in the European fruit."

Indeed, when clients wanted to transact "**sensitive**" business, **KPMG** referred them to

associates in Liechtenstein -- with the assurance of added secrecy and protection from foreign law enforcement inquiries. Koller says even Liechtenstein was initially "unhappy" with Marcos' money being transferred there, but Limag resolved the problems by giving a well-paid board chairmanship to **Prince Constantin,** the elderly uncle of constitutional monarch **Prince Hans-Adam II.**

"**The bank bought the Prince's uncle,**" Koller explained to the French parliamentary commission that was investigating money-laundering in Switzerland. "**Everybody is bought in Liechtenstein.**"

In 1997, Koller was fired by the manager of **KPMG Zurich** (which had been made independent of Credit Suisse -- at least officially -- so that it could continue as its auditor under new accounting regulations). She was sacked after testifying against a **Credit Suisse Trust AG** client who was involved in a conspiracy to sell tainted blood forcibly taken from prisoners by the **Stasi,** the East German secret police.

In addition, Koller believes she was fired because **Credit Suisse** realized that she -- like other **KPMG** and bank employees -- knew what happened to the Marcos money. She told the French inquiry: "My superior told me ... that I would never work again as a lawyer and that my career was finished in Switzerland and in Liechtenstein because I had spoken to the authorities. "

Last year Koller approached the Justice Department via Virginia lawyer **David Smith,** a former associate director of the Asset Forfeiture Office. There was no response from the Justice Department's anti-money laundering division or from the FBI. Both offices declined to comment for this story.

So in February, Koller anonymously approached the Philippine government through her attorney, **Ian M. Comisky** of high-powered Philadelphia law firm **Blank, Rome, Comisky & McCauley,** which has close ties to the Bush administration.

In his letter, Comisky wrote, "**KPMG-Fides** and **Limag AG** employees made admissions regarding the transfer of the Marcos monies to Liechtenstein, and our client has contemporaneous memoranda prepared at the time of the admissions." . . .

Lucy Komisar, *a New York journalist, is writing a book about how bank and corporate secrecy support international crime and corruption. She reported from the Philippines at the time of the Marcos overthrow.*

This astonishing revelation came not by an investigation or finding by any investigatory or regulatory body. It came as the result of the guilty conscience of an attorney of KPMG. This reveals an activity which could not have been just one error or the initiative of one erring element or a 'bad apple' in KPMG or in the MAFs. Such a deep criminal complicity, as it seems on the face of it, would have been impossible unless it was a pattern; unless it was part of the accepted but acknowledged culture of the profession at the level of the MAFs. As Mitchell-Sikka study says "The auditing industry's standard response to such failures is to blame some one else, claim that the failures are the work of some 'bad apples', tweak accounting standards, code of ethics, regulation and make calls for better training of accountants". "These tactics", say Mitchell and Sikka, "are designed to deflect the attention away from the culture and values of the accountancy firms. Failures are not the result of 'bad apples'; the bad apples are the product of rotten orchards, and the trees need a good shake. Accountancy firms are engaged in "dirty business' and their power is unchecked because they colonised and captured the regulatory and

political scene to protect their economic interests". The conclusion is obvious that the MAFs are collaborators of deeper offenders in global finance and it cannot be a exception, but a regular and accepted practice. This kind of taste, involvement and practice is unavoidable when the MAFs seek the same secrecy around them as Ferdinand Marcos did with his ill-gotten money. This makes the MAFs not professionals for fraudulent elements, but their accomplices and co-sharers.

Paying billions of dollars as fines, reparations and compensations for wrong doings and frauds in they have been found to be accomplices to buy certificates of good conduct by reparatory payments

Most players in world business do not know that the MAFs are repeatedly caught in frauds and wrongdoings in their professional conduct, particularly as auditors. In India it is certainly not known to any. Whenever the White Paper editors have had interactions in Indian businessmen or professionals, they found that they have never heard that the MAFs are capable of any thing wrong. Their misdeeds and misconduct are totally unknown in India to the stake holders who engage them at phenomenal fee simply because they have come from the West, even though their work here is done by the low cost Indian partners and audit managers only. While this ignorance is true of all aspects of their misdeeds, this is particularly true of the fact that the Indian businessmen and the Indian policy makers, and unfortunately even the Indian media, do not know that they have paid billions of dollars to escape civil and criminal action and also additional payments to secure good conduct certificates from the affected parties. This aspect needs to be highlighted. An illustrative catalogue extracts from the website contents relating to the settlements effected by the MAFs, particulars of which are given in the website of The Catbird Seat, are revealing:

"Judge Friendly of the Second Circuit in ***United States v. Benjamin,*** noted three decades ago: "In our complex society the accountant's certificate . . . can be instruments for inflicting pecuniary loss more potent than the chisel of the crowbar."

Judge Friendly's words have been borne out, as independent auditors have been held responsible for the outright manipulation and inflation of public companies' earnings to boost stock prices, despite the auditing firms' claims that they departed too early, arrived too late, or for some other reasons were not knowledgeable about the huge financial frauds that have recently rocked our nation's securities market.

For example, ***In re Waste Management Securities Litigation*****, Arthur Anderson** paid **$70 million;** in **Cendant , Ernst & Young** paid **$355 million;** and in ***Informix*** **Ernst & Young** paid **$32 million -** all to resolve securities fraud actions where there were egregious irregularities with the financial statements of these publicly traded companies and the auditors were at the epicenter of the financial fraud."

"PricewaterhouseCoopers (PwC), itself the target of three ongoing SEC investigations, agreed in May to pay **$55 million** to settle a class-action lawsuit by shareholders of **MicroStrategy Inc.**

The software maker was forced last year to admit it had been losing millions while telling investors it was profitable. PwC profited from consulting for MicroStrategy and also acted as reseller for some of its software. Like Andersen, PwC denies that its independence has been impaired, but this will not be the firm's last such legal tussle.

A pending lawsuit by **Raytheon Co.** shareholders, who lost millions when the defence contractor restated its earnings, may also raise the conflict issue. Nearly 95 percent of the $51 million Raytheon paid PwC last year was for nonaudit services, though Raytheon says much of that was for work it considered audit-related, like tax services".

"SEC Wants Suspension for Ernst & Young"

WASHINGTON (AP) -- In a rare move, federal regulators are seeking to have Ernst & Young suspended from accepting new corporate clients for six months because of the big accounting firm's alleged failure to remain completely independent from companies whose books it audits.

The Securities and Exchange Commission contends in a legal proceeding that Ernst & Young's internal controls are inadequate to prevent its auditors from becoming too cosy with client companies.

In a case before an administrative law judge that began last year, the SEC alleges that Ernst & Young, the nation's third-largest accounting firm, violated rules designed to keep accountants independent from the companies they audit when it engaged in business with a software company client.

The SEC filed a brief in the case a week ago that criticized the firm's internal controls and asked that it be suspended for six months from new business from any publicly traded companies. The agency has not sought a suspension of a major accounting firm since 1975".

"It seems likely that (Ernst & Young) will continue to commit independence violations in the future," the SEC said in its brief.

New York-based Ernst & Young issued a statement late Friday calling the SEC's request "irresponsible" and saying that regulators had no reason to seek sanctions against the firm".

"In the administrative proceeding, the SEC said that **Ernst & Young** was auditing the books of business software maker **PeopleSoft Inc.** at the same time it was developing and marketing a software product in tandem with the company. Ernst & Young engaged in the dual activities from 1993 through 2000, according to the SEC.

The firm has said that its conduct was appropriate and conformed with accounting profession rules.

It was the second time the SEC had brought an auditor independence action against Ernst & Young, which settled a 1995 action by agreeing to comply with independence guidelines.

The firm recently has come under fresh scrutiny over its role as long time auditor for **HealthSouth,** the rehabilitation services company embroiled in a **$2.5 billion accounting scandal.**

Ernst & Young has been sued by shareholders seeking billions of dollars in damages in connection with its audits of HealthSouth and other big companies with accounting troubles, **including AOL Time Warner and Cendant.**

- Securities and Exchange Commission: http://www.sec.gov"

"FIRMS SETTLE IN FRAUD CASE

USA Today

Accounting firm **Ernst & Young** and law firm **Jones, Day, Reavis & Pogue** agreed Monday to pay **$63 million** and **$24 million** respectively to settle charges in a $1.2 billion civil fraud suit involving **Charles Keating.**

The firms were accused of helping deceive federal regulators about the health of Keating's **American Continental** while the firm was allegedly **defrauding investors** who bought ACC bonds".

"Daniel Wise, New York Law Journal

Record-breaking awards in the Cendant securities fraud case were approved by a federal judge yesterday in New Jersey: a **$3.1 billion** settlement amount and **$262 million** in fees to attorneys for the plaintiffs' class.

Cendant, a conglomerate that includes Avis car rental agencies and Ramada Inn Hotels, had agreed to pay $2.8 billion in December to settle security fraud charges stemming from the collapse of its stock price after accounting irregularities were disclosed in April 1998.

Ernst & Young, the accounting firm that had certified Cendant's financial statement, also agreed to contribute **$335 million** toward the settlement. . . ."

"**KPMG LLP -** Uh-oh! . . .

KPMG is **HUD's** auditor.....and was their auditor when the **$59 billion** went missing and audited financials were simply not produced.....apparently, they have decades of experience of helping government money go missing.....

http://www.inthesetimes.com/issue/26/20/feature3.shtml"

"If accounting firms are the financial police for insurance companies, who will police the police? State departments of insurance, that's who.

Two major accounting firms are taking heat from the New York and Ohio insurance departments for recent insurance company failures. The New York superintendent of insurance, Neil Levin, has filed a lawsuit against **PricewaterhouseCoopers LLP,** alleging the firm was negligent in its audit of three failed insurance companies that allegedly cost New York residents $100 million.

The Ohio Department of Insurance (DOI) settled a lawsuit for $9.99 million with accounting firm **KPMG Peat Marwick** for its involvement in the **PIE Mutual Insurance Co.** insolvency.

The Ohio DOI had alleged that KPMG Peat Marwick "failed to detect that PIE had fraudulently recorded a $58 million asset on its financial statements" in 1996. As part of the settlement, KPMG Peat Marwick admits no wrongdoing".

For the moment, however, the SEC is active on the issue. Last month, it levied the largest penalty ever against a Big Five firm.

Arthur Anderson LLP agreed to pay **$7 million** to settle charges relating to its mid-1990s work for **Waste Management, Inc.** The SEC said Andersen helped the huge trash hauler overstate income by more than **$1 billion.** Noting the **$11.8 million** in nonaudit fees Andersen got from WMI, Unger calls the case the "smoking gun" proving consulting gigs can compromise independence.

The Ohio suit

PIE Mutual was Ohio's largest medical malpractice insurer until 1998, when the DOI seized control of the company because its liabilities exceeded its assets by $275 million. The DOI is currently liquidating PIE Mutual, attempting to pay off the estimated $600 million to $800 million in outstanding claims. The Ohio DOI has recouped approximately $240 million from the sale of PIE Mutual's assets and the settlement with KPMG.

Andersen's audits have been questioned before. The firm was the accountant for **Sunbeam,** which grossly overstated its profits, and Andersen agreed to pay **$110 million** to settle shareholder suits without admitting or denying blame.

Waste Management, another client of Andersen, **overstated income by $1 billion.** Andersen agreed to pay part of a **$220 million** class-action settlement and a **$7 million** civil penalty, without admitting liability, according to a New York Times story.

SEC seen settling with PwC

Reuters

NEW YORK - The U.S. markets' top regulator is expected to close its probe of the audit of once high-flying software maker **MicroStrategy Inc.** (MSTRD.O) by settling with the **PricewaterhouseCoopers** partner who led the account, a source familiar with the situation said on Friday.

A final settlement, which has not yet been inked, would close the chapter on a prominent accounting irregularity case that has hung over the world's largest accounting firm for more than two years.

Under the terms of the deal, the **Securities and Exchange Commission has decided not to bring an enforcement action against the accounting firm,** the source said. But the partner at PricewaterhouseCoopers, **Warren Martin,** who led the **MicroStrategy** account for the accounting firm, **will be suspended from practicing as an auditor for two years,** the source said.

McLean, Virginia-based **MicroStrategy Inc.** has struggled since ***its shares plunged 62 percent in one day*** from a high of $333 in March 2000 after it was forced to restate three years of profits as losses. . . .

The technology firm, including its top executives, settled with the SEC over the issue and paid out ***$10 million in stock*** to shareholders as part of a lawsuit settlement.

PricewaterhouseCoopers has already forked out **$55 million** to settle a shareholder lawsuit stemming from the case but admitted no wrongdoing.

PricewaterhouseCoopers in July agreed to pay **$5 million** to settle charges brought by the SEC that its auditors approved improper accounting and that it violated independence standards for several clients in the past. It was the second-largest payment ever by an accounting firm to the market's top regulator.

PricewaterhouseCoopers in June also agreed to make a payment to settle with the **Internal Revenue Service** over advice on tax shelters it provided clients. . . .

Together with Tax **Magician Mark McConaghy** of **PricewaterhouseCoopers** they "negotiate" with the IRS to make over $650 million of taxes **"disappear".**

(The secret behind this trick, if you watch closely, is to quietly slip the tax burden over to the millions of US ordinary citizens while we're distracted by an attractive, young magician's assistant named Monica showing hand-tricks to another master magician named Slick Willy.)

MAXWELL AUDITORS AND SELF-REGULATION: THE VERDICT

By Prem Sikka, Professor of Accounting, University of Essex

What do **Edencorp, International Signal Corporation, London and Capital, London**

and Counties, London United Investments, Ramor Investments, Sound Diffusion, Lloyd''s of London, Johnson Matthey and **Atlantic Computers** have in common?

They are examples of audit failures.

Each involved a major accountancy firm that ticked and blocked, collected its fees, issued worthless audit reports and trusted people's inability to call auditors to account.

Coopers & Lybrand became auditors of most of the Maxwell controlled companies and their pensions funds. Then in 1990, an investigative journalist (Daily Mail, 24 October 1990) began to investigate unusual movements in the monies of the pension schemes run by Maxwell's businesses. A large amount of Mirror Group pension fund money was being invested in companies in which Maxwell had an interest.

In a very elaborate regulatory maze, such tasks are delegated to the Joint Disciplinary Scheme (JDS); an organisation originally created in 1979 in response to the previous audit failures. **The JDS is financed by the accountancy profession which also decides the cases which are referred to it.**

The Institute of Chartered Accountants in England & Wales (ICAEW) asked the JDS to investigate **35 complaints** against **Coopers & Lybrand** and 24 complaints against four individual partners, in relation to Mirror Group of Newspapers and other Maxwell companies for the period 1988 to 1991.

The verdict on Maxwell auditors, **Coopers & Lybrand** (now part of **PriceWaterhouseCoopers**) was delivered in February 1999, some seven years after Maxwell's suicide.

A three man panel found that a lack of objectivity in dealing with Mr. Maxwell and his companies lay at the heart of many of the 35 complaints laid against the firm and four of its partners.

The JDS concluded that "The complaints reveal shortcomings in both vigilance and diligence and a failure to achieve an appropriate degree of objectivity and scepticism, which might have led to an earlier recognition and exposure of the reality of what was occurring". The report concludes that the "firm lost the plot" and "got too close to see what was going on". The firm admitted 59 errors of judgement.

Most of the blame is allocated to the main audit partner Peter Walsh, who died in 1996. According to the JDS report, four Coopers & Lybrand partners failed to meet the required professional standards in auditing various parts of the Maxwell empire. The next senior partner John Cowling, against whom twenty complaints were listed, is censured and ordered to pay costs of **£75,000** and fined a total of **£35,000.**

The report says that Cowling had never encountered fraud before and criticised him for too easily accepting management explanations. He failed to qualify the accounts of **London & Bishopsgate Investment;** a business controlled by Maxwell, even though it had failed to maintain proper records or adequate control systems and did not reconcile clients'' money. Of the other three partners involved, two paid costs of **£10,000** each and were admonished. Another partner paid costs of **£5,000.**

What would happen to a doctor/surgeon who admits to 59 errors of judgement and generally ''losing the plot''? That surgery is likely to be closed down. The licences of the doctors concerned would be withdrawn and their standards of work would probably be subject to an independent investigation.

But auditing is a law unto itself. The four audit partners concerned are still employed by the firm and earn six-figure salaries. None of the partners

have been disqualified from public practice. No one has investigated the overall standards of the firm, or its successor firm.

Coopers & Lybrand have been fined **£1.2 million** which works out at £2,000 per partner (Coopers had 600 partners). The firm has also been asked to pay **£2.1 million** in costs. Taken together this amounts to £6,000 per partner, all probably **tax deductible.**

To put this in context, it should be noted that for the period under investigation, Coopers received £25 million in fees from Maxwell. The UK fee income of **PriceWaterhouseCoopers** is estimated to be around **£1.8 billion** and the firm's world-wide income is around **£10 billion.** The major firm barons would, no doubt, be quaking in their boots, all the way to the bank.

The accountancy establishment's public "spin" is that the JDS is a tribunal and a quasi-court. But the JDS processes are remarkably different. It does not owe a "duty of care" to anyone and the public is not admitted to any of its proceedings. The JDS report does not list the evidence examined, the questions asked and the replies received. It does not indicate how the JDS came to filter and weigh various pieces of evidence or why it decided to neglect or downgrade some categories of evidence. The transcripts of the JDS proceedings are not publicly available.

Under its rules, Coopers can appeal against its findings, but the investors and pension scheme members affected by the audit failures cannot. It is inconceivable that any judge or jury can find a firm guilty and then proceed to pocket the fines. Yet this is exactly what has happened for the Maxwell audits.

The fines and costs will go to the JDS instead to being used to compensate the victims of audit failures.

This in turn reduces the financial contributions that the accountancy profession is obliged to make towards the running of the self-regulatory structures.

The JDS report is a major disappointment for a number of additional reasons as well.

In addition to acting as auditors, Coopers & Lybrand sold a variety of non-auditing services to the Maxwell empire. This increased the firm's income dependency on Maxwell and must have, at least in the eyes of the outside world, compromised auditor independence. Yet the JDS report makes no effort to investigate the ''independence'' aspects.

Will the paltry fine and the adverse publicity do anything to curb audit failures? The answer has to be no. No doubt, the auditing industry would argue that complex frauds are difficult to unravel, and that no one can stop a determined fraudster. Such comments are designed to disarm critics, journalists, politicians and academics alike. They deflect attention away from the economic and cultural context of auditing.

The truth is that audit failures are not brought to public attention through any vigilance by audit firms, professional bodies or the regulators. They came to light because the stench of scandal became too strong. One can only wonder how many others are waiting to be discovered. If by hook or by crook a business survives, audit failures remain concealed....

Overall, the verdict on the Maxwell auditors amounts to the usual feather-duster approach to auditor regulation. The punishment will not curb audit failures. The JDS has squandered another opportunity to examine the institutionalisation of audit failures. . . .

***

COOPERS FACES RECORD FINE FOR MAXWELL AUDIT FAILURES

COOPERS & LYBRAND, long-time adviser to **Robert Maxwell,** is to pay a punitive **£3.5 million** in fines and costs over failings in its audit work on the late publisher's business empire.

The fine against Coopers, which has since merged to become **PricewaterhouseCoopers (PwC),** is the largest ever levied by the accountancy profession's regulators.

The profession's Joint Disciplinary Scheme (JDS) is expected to hand down the fine today after the firm, it is understood, admitted all 35 charges levelled by the tribunal. The report by the disciplinary tribunal, headed by Roger Henderson, QC, and Ian McNeil, former president of the Institute of Chartered Accountants in England and Wales, will say that in its opinion, **"Coopers & Lybrand lost the plot".**

Coopers is expected to be castigated in the report for a lack of planning and vigilance in its work.

The report cites two instances where Coopers has admitted that it should have "whistle-blown" to the authorities and another instance in which the firm admits that it should have qualified the accounts of an investment trust that had no books or records detailing assets lent to Robert Maxwell.

The report is also expected to show that work on the Maxwell account was conducted by inexperienced staff. One of the partners had only been a partner for two weeks before taking on the job. The manager on the job had just qualified as an accountant and the rest of the staff were trainees.

The JDS action comes as a serious reputational blow to Coopers, which has long been criticised over the "cosiness" of its relationship with Maxwell. Neil Taberner, the senior audit partner, worked closely with Robert Maxwell for nearly 15 years, in what became one of Coopers's longest client relationships. The firm was paid about ££4 million for its audit work in 1991 alone. **Mr Taberner remains a PwC partner.**

Peter Walsh, another senior partner, now dead, appeared as a witness in the Maxwell fraud trial. Mr Walsh denied that the firm's standards had been allowed to slip because of Maxwell's domineering personality. A colleague, Stephen Wootten, also giving evidence, denied turning a blind eye to cash movements between Maxwell companies.

Coopers argued that Maxwell's raids on the pension funds occurred after March 1991, when it signed off the books. Maxwell died in November 1991.

Brandon Gough, then senior partner of the firm, said Coopers had never contemplated dropping Maxwell as a client. He said: "You can take it for granted there were some fairly intensive discussions about accounting methods. But if we had any major differences, we would have qualified the audit."

Coopers was appointed auditor to the Maxwell group of companies in 1971, shortly after a report by Board of Trade inspectors into Pergamon Press said Robert Maxwell "could not be relied upon to exercise proper stewardship of a publicly quoted company".

Coopers tried to have the JDS investigation postponed, arguing that it would "impose intolerable strains on the few individuals within Coopers actively involved in the relevant audits". The High Court ruled in December 1994 that the investigation should proceed.

The previous highest penalty levied by the JDS was for £600,000 in costs plus £150,000 in fines against BDO Stoy Hayward over its auditing of

Astra. Recoveries are used to bolster the JDS "war chest" to investigate alleged miscreants in the profession.

The JDS is separately investigating complaints against two Coopers partners who led the audit team working on **Barings** at the time it was laid low by the **Nick Leeson** "rogue trader" scandal.

Coopers is also being investigated over its role as auditor to Resort Hotels, the collapsed hotels group.

Coopers was previously being sued over its auditing by **Price Waterhouse** as administrators of **Maxwell Communication Corporation** but that role was transferred to the accountant Grant Thornton because of the two firms' merger. . .

Source: The Times February 2, 1999

Contributed by Andrew Priest, Edith Cowan University

From MediaGuardian.co.uk by Jill Treanor and Charlotte Denny,

Monday February 12, 2001:

MAXWELL SCANDAL REIGNITES

DTI report into former MGN owner will unsettle top City and political figures The Department of Trade and Industry's potentially explosive report into the collapse of **Robert Maxwell's** business empire will be published by the end of next month, reopening the controversy sparked by the sudden death of the former owner of the Mirror newspaper.

Almost a decade after Mr Maxwell disappeared off his yacht, the inspectors recruited by the DTI to examine his complicated web of companies are finalising their detailed inquiry, which many figures in the City and in politics would probably prefer to keep away from the printing presses.

The inspectors, according to a report this weekend, highlight the iron fist with which Robert Maxwell controlled his business empire, looting money from the **Mirror Group Newspaper's** pension fund soon after taking over the paper in 1984. It outlines the role played by the then investment bank **Samuel Montagu,** which floated MGN on the stock market in 1991, and **Coopers & Lybrand,** which acted as accountants to the Maxwell empire.

While the inspectors conclude that some of the firms involved could have blown the whistle on Maxwell, they also argue that he was often the only person who really knew what was going on inside his sprawling business empire. The report is said to give details of money channelled from MGN and private Maxwell companies. It is also said to show deals **Robert Maxwell** conducted by using the assets of the Mirror's pension funds to trade in shares and channel the profits into his own company. . . .

The investigators are reported to have concluded that companies and executives dealing with Robert Maxwell, who was also investigated by the DTI 30 years ago, should have treated him with caution. He is also said to have courted politicians in a bid to boost his credibility.

Leading investment bank **Goldman Sachs** is said by the report to have played a crucial part in ensuring that the flotation of one of Maxwell's other companies was a success. **Coopers & Lybrand,** now part of **PricewaterhouseCoopers,** has already been fined by the accountancy profession's policing body for its role in the **Maxwell affair.**

Goldman Sachs was unavailable for comment while **HSBC,** now owner of the former **Samuel Montagu,** was unable to comment.

PricewaterhouseCoopers also declined to say anything.

This catalogue of the different audit failures to audit frauds of the MAFs is not exhaustive. An exhaustive list with details of the offences in which each individual MAF is involved is given in another chapter. It is evident from the details given above that the MAFs are not independent auditors as they were once considered to be. In the light of the other influences including the disproportionate non-audit work and the questionable and unethical activities, from which they seem to be making most of their revenue, it is obvious that the audits done by them lack credibility. And the different cases illustratively mentioned here and in detail later merely bare testimony to that lack of credibility. And this lack of credibility is proven by the billions of dollars of fines and compensation which they have had to cough out in the class and regulatory actions against them.

Driven by their lust for money by any means, some of the MAFs have become experts in shredding evidence and in suppressing facts and evidence, to escape the consequences of their fraudulent actions in pursuit of money

While the Enron case is the most infamous instance of an MAF adopting methods which normal White collar criminals will do to escape the long arm of law, it is by no means a solitary instance of suppression of evidence, nevertheless it is a crude method of suppression of evidence as a result of which it got highlighted. But the MAFs have been regularly suppressing evidence of their wrong doing. It is only in rare cases that the MAFs are questioned, only where there has been a business collapse-be it Enron, or Maxwell or Barings or BCCI. But in each of these cases the MAFs have successfully suppressed the vital papers and evidence from the regulatory. Let us examine the cases in which the MAFs have suppressed evidence available with them to the regulatory of one country or the other.

FIRST, THE BCCI CASE

The US Senate investigated into the BCCI fraud. The details of how the auditors of BCCI, the PwC, refused to co-operate with the US investigation is given before while dealing with the issue whether the MAFs are global firms or global dodgers. The summary of the facts are given here for proper appreciation of another dimension of the culture and character of the MAFs, namely suppression of evidence. The US Senate committee sought the files of PwC for its investigation. PwC was reluctant. When the New York state banking authorities sought to investigate the case and for which they sought the assistance of the local PwC. This was the end result:

The New York state attorney told the Congress

"The main audit of BCCI was done by Price Waterhouse UK. They are not permitted, under English law, to disclose, at least they say that, to disclose the results of that audit, without authorization from the Bank of England. The Bank of England, so far -- and we've met with them here and over there -- have not given that permission. The audit of BCCI, financial statement, profit and loss balance sheet that was filed in the State of New York was certified by Price Waterhouse Luxembourg. When we asked Price Waterhouse US for the records to support that, they said, oh, we don't have those, that's Price Waterhouse UK. We said, can you get them for us? They said, oh, no that's a separate entity owned by Price Waterhouse Worldwide, based in Bermuda".

Source: United States Senate Committee on Foreign Relations, 1992b, p. 245.

Commenting on the BCCI case Mitchell and Sikka observed

BCCI's auditors also refused to co-operate with the US Senate Subcommittee'sinvestigation7 of

the bank (US Senate Committee on Foreign Relations, 1992, p. 256). Although the BCCI audit was secured by arguing that Price Waterhouse was a globally integrated firm (p. 258), in the face of a critical inquiry, the claims of global integration dissolved. Price Waterhouse (US) denied any knowledge of, or responsibility, for the BCCI audit which it claimed was the responsibility of Price Waterhouse (UK). Price Waterhouse (UK) refused to comply with US Senate subpoenas for sight of its working papers and declined to testify before the Senate Subcommittee on the grounds that the audit records were protected by British banking laws, and that "the British partnership of Price Waterhouse did not do business in the United States and could not be reached by subpoena" (p.256).

PwC website refers to the firm as a "global practice", but in a letter dated 17 October, Price Waterhouse (US) explained that the firm's international practice rested upon loose agreements among separate and autonomous firms subject only to the local laws:7 Price Waterhouse (UK) partners did agree to be interviewed by Subcommittee staff in PW's London office. The offer was declined due to concerns that the interviews would be of little use in the absence of subpoenaed documents (US Senate, 1992, p. 258).

This is a successful suppression of evidence by the MAF, namely PwC.

SECOND, THE BARINGS CASE

In Barings case the Singapore office of Coopers and Lybrand [then C&L and now part of PwC] had audited the accounts of Barings Futures [Singapore] PTE Limited, which was the epicentre of the fraud. For two years Deloitte and Touche [DT] had done the audit of the Singapore companay. When the fraud was investigated by Bank of England, the PwC and DT claimed immunity from having to produce the files on grounds of client confidentiality. This is what the Bank of England noted:

"We have not been permitted access to C&L Singapore's work papers relating to the 1994 audit of BFS [Baring Futures (Singapore) Pte Limited] or had the opportunity to interview their personnel. C&L Singapore has declined our request for access, stating that its obligation to respect its client confidentiality prevents it assisting us". "We have not been permitted either access to the working papers of D&T or the opportunity to interview any of their personnel who performed the audit. We do not know what records and explanations were provided by BFS personnel to them".

Here too the MAF has clearly and unequivocally refused to part with evidence, that is is it has successfully suppressed the evidence which the Bank of England considered necessary from the Bank of England.

THIRD, THE INTERNATIONAL SIGNAL AND CONTROL CASE

In this case a billion dollar fraud in International Signal and Control Plc [ISC], one of the subsidiaries of Ferranti, was the subject matter of investigation. The ISC was audited by Peat Marwick Mitchell [PMM] later part of KPMG, Some of the directors of ISC were involved in fudging accounts and laundering $700 millions through secret banks accounts in Swiss and in the US. Ferranti had bought ISC without the knowledge of the fraud and filed a case against the auditors for negligence. It was satisfied with an out of court settlement. But in UK the matter was investigated in response to complaints. The investigating authority sought the working papers of KPMG. In its report the authority said:

"It quickly became clear that a substantial part of the audit work for Technologies had been undertaken on behalf of PMM in London by the

American firm of the same name. .... considerable difficulties were experienced in gaining such access. ... I was informed that it was not that firms' policy to make papers available in situations of this kind. .... Copies of the American firm's working papers were eventually made available, "exceptionally and in order to assist the investigation", at the offices of a law firm in New York. ..... The copy files produced in New York were inadequate for the purposes of the investigation and it was necessary to arrange access to be gained to the original files. I was told that these were in the possession of the US Attorney in Philadelphia. My investigating accountants went there to examine them. They discovered that many of the files relevant for my purpose had remained in the possession of PMM. The firm had considerable difficulty in locating these files. Once they had been found a third visit to America was arranged. My investigating accountants were not permitted to photocopy relevant material of an [sic] any of American firm's files, rendering extensive note-taking necessary."

Source: Joint Disciplinary Scheme, 1996, p. 7.

This is the third case involving suppression of evidence by a MAF, in this case it happens to be KPMG.

FOURTH THE ENRON CASE

And finally, the most infamous Enron case. It is the latest and the crudest form of suppression and destruction of evidence. The MAF involved in this case was Arthur Anderson. The Enron Corporation and AA shared virtually an incestuous association. AA provided both audit and consultancy services to Enron. It received $ 27 millions for consultancy work and $25 millions for audit work. AA worked for Enron everywhere in the world from Cuiaba in Brazil to Dabhol in India, through its national franchisees or network. But when the Enron bankrupted, AA engaged in a world wide effort to suppress and destroy evidence by shredding the files and papers, to avoid being implicated in the Enron fraud. "In March 2002 a federal grand jury indicted Anderson on charges that Anderson knowingly persuaded employees in Houston, Chicago, Portland and London to withhold records from regulatory and criminal proceedings, and alter, destroy, and shred tons of documents with the intent to impede the investigation. A federal jury convicted Anderson on 15th June 2002.

It is therefore obvious that the MAFs are part of the questionable activities of the unlawful corporates and their managements and that is why they are willing to go as far as to suppress and destroy evidence. If they have been driven to this kind of desperation it is because the only philosophy by which they operate is the philosophy of money, money and money and nothing else.

Manipulation of the privatisation of policies of the government and gaining by privatisation-incentives by foreign Governments to MAFs to export privatisation expertise to countries like India

When in October 2002 the Government of India announced the deferment of the privatisation of the oil companies HPCL and BPCL, the international rating agencies immediately downgraded the outlook for the country's economy. This was followed by extensive media campaign, edits and special articles critical of the Government. The Government of India became defensive and apologetic about its decision. Any one who differed from privatisation was castigated. How was it that the Indian economy which was undoubtedly strong on the external front, and was getting stronger every day, with annual average inflation at less than 4%, and with FDI into the economy looking

up, not down, could be rated unfavourably? The answer is simple. There is complete, but un-spelt, co-ordination between the rating agencies, investment bankers and the MAFs as all of them, and definitely the latter two, are gainers if privatisation goes through. The downgrading of the outlook for India because of the deferment of the decision on the privatisation of the oil companies was a design to warn and coerce the government to go ahead and not to defer the process.

The idea of privatisation is part of the agenda of Washington consensus which had evolved since around the late1970s and had become the mantra of the US treasury and Wall Street, the IMF and the World Bank. Thus it had become the prescription of the West for the rest of the world. In the rest of the world it is the state which has the potential to stand up to the competitive strength of the trans-national corporations. In fact the empirical study of Francis Fukuyama in his famous book 'Trust' brought out the fact that in nations and societies which function on the basis of individualism, market forces build global level corporations.

But in nations and societies where family and community system is a dominant factor, the private sector will have to partner the state to promote global level corporations. In his study Fukuyama even includes countries like Italy and France in the West and countries like Japan, Korea and Taiwan as family based societies and rationalises the private sector-state co-operation in building up trans-national size corporations. But the Washington consensus and the promoters of Washington consensus make no such distinction and tend to follow the US experience and to force the rest of the world to experiment the experience of the US and particularly the west, on the rest.

So the entire global financial interests and institutions led by the IMF and World Bank and also private financial institutions, banks, investment banks and all those dependent on them for business, including the rating agencies and MAFs, are part of this incredibly powerful global lobby to promote privatisation. The states in the west also give aid and other encouragement to the developing countries to promote privatisation. Thus privatisation is an area where the MAFs have a collusive interest with other financial and finance market related institutions of the world and this has the approval and encouragement of the IMF and the World Bank.

A study by Unison, a trade union representing 1.3 millions members from a large range of service sectors, titled "How the Big Five accountancy firms influence and profit from privatisation policy" is extremely important. This research for this study was conducted by the Health Policy and Health Services Research at University College London. The facts brought out in this study would demonstrate beyond all doubt the devious role of the MAFs in promoting privatisation not so much from the point of view of common interest, but for their own personal, pecuniary gain. The British governments had initiated Private Finance Initiative [PFI] and Private Public Partnerships [PPPs] to promote, accelerate and finance privatisation. The Unison study exposes how the MAFs have developed a profit industry around the PFI and PPPs. The summary of the Unison study is very instructive and has been quoted in chapter of this White Paper.

The study introduces the subject of how the big five profit from privatisation policies saying that "Companies profiting from privatisation are also running privatisation policies" It continues, "The UK government relies on the reputation and expertise of the Big Five accounting firms to develop, promote, and implement Public Private

Partnerships and Private Finance Initiative whilst the management consultancy arms of the Big Five profit hugely from the government's flagship policy". The study points out, "The management consultancy arms of the Big Five are both clients and client advocates in the privatisation industry. As fee earners they benefit from the policy, and as auditors and consultants to the public utility companies and private consortia buying into privatised sectors they benefit from their clients increased profitability".

The study demonstrates the extent of dominance of the MAFs in the privatisation work.

In the UK the Big Five also act as financial advisers on the many PFI and PPP projects. Table 2 lists the numbers of projects that each of the Big Five are advisers to and their capital value.

Table 2: The Big Five as Financial Advisers on PFI Projects

No.	Name	Number of PFI/PPP contracts			Project Capital Value
		In Progress	Signed	Total	(£m)
1	PricewaterhouseCoopers	36	106	142	15,498.34
2	KPMG PPP Advisory Services	36	78	114	22,143.24
3	Deloitte & Touche Ltd.	21	45	66	4,385.69
4	Ernst & Young	9	31	40	1,953.32
5	Andersen	6	26	32	10,294.99
	Total	108	286	394	54,275.58

Source: PublicPrivateFinance and OGC Database, May 2002

The size of the privatisation business

Privatisation became a major earner for UK accountancy firms when Mrs Thatcher came to power in 1979. By 1985, Price Waterhouse as it then was had set up a new section to deal with the burgeoning programme of privatisation. By the end of 1999 PwC had been responsible for world-wide for privatisation deals worth about £ 22 billion, and in 2000 it led the table of PFI signings having advised on 90 UK PFIs worth £ 8.3 billion, nearly 40% of total signings by the big five in the UK. Only Arthur Andersen, with a quarter of PwC signings, achieved a higher value in that year (£ 9 billion).

In 2000 PwC handled 222 privatisation deals for international clients valued at $5.1 billion and described itself as "the market leader in project finance and privatisations". PwC now boasts that it has "acted on more privatisation than any other financial advisor, from steel and heavy manufacturing to utilities, public transport, health and education services."

The fees associated with this type of work come from business case preparation, arranging finance and advising public bodies and governments. More recently fees have been earned from refinancing existing PFI deals. Refinancing produces extra profits when loans are re-negotiated at lower rates of interest after completion of the construction period when risks have been reduced. For example, last year PwC was appointed to lead the deal that could land Carillion, United Medical Enterprises, and the venture capitalist Innisfree around £20 million extra profit from refinancing the Dartford and Gravesham Hospital.

These gains are at the expense of the public sector. The National Audit Office calculated that when refinancing of the Fazakerley PFI prison contract increased shareholder's rate of profit from 16% to 39% it left the prison service with increased liabilities of up to £47 million.

As we shall see, the same accountancy firms that extract windfall profits for their private sector clients also devised the system for the public sector that permits the gains.

Since there is a multi-point profit making possibilities in privatisation programmes all over the world, the MAFs have turned global lobbyists for privatisation. This is what the Unison study finds:

The Big Five as international lobbyists for privatisation

With so much potential fee income riding on privatisation, it is hardly surprising that the Big Five should take an entrepreneurial interest in the policy.

Accountancy firms work with government to increase the export of privatisation expertise. Top firms KPMG and PwC have just launched a joint document with the Partnerships UK (PUK, a private sector agency in partnership with the government) and International Financial Services London (IFSL) to boost the export of management consultancy. Published in late 2001, *Public Private Partnerships, UK expertise for international markets aims* "to develop commercial opportunities" internationally in public services including health, education, transport, prisons and defence.

IFSL, formerly British Invisibles, is a private sector lobby group promoting UK-based financial service industry. It works closely with the UK government and EC through the Liberalisation of Trade in Services (LOTIS) committee. It markets the "expertise of UK firms" which it says is "crucial to the budding international market for public private partnerships." The expertise "has been built on 400 PFI contracts worth over £ 17 billion signed in the UK up to the end of 2000". IFSL is banking on further £20 billion by the end of 2002 "of which a half may be attributed to the London Underground and the National Air Traffic Services." It says it is currently active in promoting PPPs in Mexico, Spain, Germany, Denmark, Poland, Canada, Czech Republic and Egypt. The IFSL has a PPP working group chaired by Tim Stone of KPMG that runs training sessions for foreign governments. Stone is also the MoD's advisor on the largest PFI deal to date, the 'Future Strategic Tanker Aircraft'.

Accountancy firms also lobby governments to liberalise and privatise through the World Trade Organisation. Arthur Andersen has lobbied the US International Trade Commission and the new US chair of the Transatlantic Business Dialogue (TABD), a private lobby created to influence US and EC trade negotiators, is James Schiro of PwC.

The accountancy firms have privileged access to the corridors of power. When representatives of the powerful public-private industry group, LOTIS, gave evidence to the House of Lords, it had to explain why alone among EC citizens it had direct access to the European Commission rather than access through its national government (House of Lords, Select Committee on European Communities. Tenth report session 1999-2000. The World Trade Organisation: the EU mandate after Seattle, HL 76, 22 June 2000).

The important point to note is that not only the MAFs are global lobbyists for privatisation they also "work with government", [that is the UK government] "to increase the export of privatisation expertise". The study also explains the strategies which the MAFs adopt in to which they also co-opt the government, to lobby for privatisation in other countries. Now one can understand why the rating of India was downgraded after the postponement of the decision on privatisation of the oil companies.

The study also explains how the MAFs influence the policy development and implementation. The study identifies three distinct components of the influence. First the MAFs second their officials, of course for a fee, to the government departments that devise, negotiate, and drive

privatisation policy. [This is how the MAFs become advisers to the Divestment Ministry in India]. Second, they commercially appraise the public sector by evaluation and methodology based on value for money [VFM]. Third, they carry on relentless propaganda. The extracts from the study is enlightening.

How do the Big Five influence policy development and implementation?

(a) Secondment

The accountancy firms have not simply sat back and profited from government policies. They have been at the heart of policy development. From this too they have earned fees. Their secondees work in government departments that devise, negotiate and drive privatisation policy.

When in 1997 the Treasury created a Taskforce to encourage PFI, a merchant banker was appointed to lead it supported by a small team of experts from the private sector. Among these experts were personnel from the Big Five. The secondees laid on briefings for the civil servants and "in-depth training in Private Finance Initiative (PFI) project management, project finance and negotiating skills."

(c) Propaganda

Andersen report

In 2000, with PFI's financial soundness still being questioned, Arthur Andersen, of Enron fame came to the government's rescue with a report claiming that a study of 29 schemes showed PFI had saved 17% on the conventionally procured projects and that most of the savings (60%) was due to the private sector assuming risks formerly borne by the public sector. (Value for Money Drivers in the Private Finance Initiative, Arthur Andersen and Enterprise LSE, January 2000)

But the study could not substantiate its central claim that PFI was 17% "cheaper" sine most of the savings occurred in just three schemes. Nor could it show that the savings were mostly due to risk transfer. In fact, the source of the most of the cost savings could not be identified at all.

In reality, the Andersen data simply recycled the rosy value for money claims made for government approval purposes before implementation. Ironically, it was an Andersen project that would show how unreliable such claims were. The Andersen Consulting PFI project known as National Insurance Recording Scheme 2 (NIRS2) predicted economics so large that 80% of all savings ascribed to PFI risk transfer occurred in this one scheme. But the projected savings did not materialize. The project is currently running three years late, and the extra cost to the taxpayer has been put at £53 million, according to the National Audit Office.

PricewaterhouseCoopers Report

PwC has now stepped in with what it calls new "hard evidence". PwC, which describes itself as No.1 in the privatization league table, has stepped up its promotion of PFI with a report that claims to have evidence that "PPPs work" (Public private Partnerships: A Clearer View, October 2001). This will be balm to the ears of a government that says what works is all that matters.

However, PwC's evidence turns out to consist of 90 anecdotes about the benefits of PFI from senior managers directly responsible for introducing it. There is no financial or service data despite major criticisms that PFI increases costs and reduces staffing, service volume and terms and conditions of employment. Asking those with the job of introducing PFI to their services whether the policy is good or bad is by any standards a pretty lame research method. But after 9 years of PFI the government is still relying on evidence of this sort from one of the policy's main financial beneficiaries.

Obviously the role of the MAFs introduces conflict of interest. The study demonstrably brings out this conflict. Says the study on conflict of interest:

Conflict of Interest

As advisors to government the Big Five devise, audit and evaluate the policy from which they are profiting. Public alarm is growing. The Greater London Authority is contemplating legal action against the London Underground PPP because PwC, which evaluated the deal, and Ernst & Young, who did the VFM calculations, are auditors to five of the eight private bidders set to profit from the contract. The European Union, if not the UK government, has rules forbidding potentially corrupting arrangements of this type.

Such conflicts are the rule not the exception. When UNISON examined PFI schemes where the Big Five acted as financial advisers to the public sector, we found 35 cases where the advisor to the public sector was also the auditor to at least one of the consortium members. (See table 4)

Tables given in the study also bring out the blatant conflict of interest in the involvement of the MAFs in the privatisation agenda of the government.

Table 4: PFI/PPP Projects where the Big Five act as financial advisers and as auditors

Project	Financial Adviser to public sector	Project stage	Contractor	Status on project	Auditor
Sheffield City Council - Schools	Deloitte & Touche	Signed	Interserve plc	Contractor	Deloitte & Touche
Inland revenue/HM customs and Excise serviced Accommo-dation (STEPS)	Deloitte & Touche	Signed	ISS UK Ltd	Shortlisted bidder	Deloitte & Touche
LB of Richmond Upon Thames - Schools Project	Ernst & Young	Preferred Partner	Jarvis plc	Contractor	Ernst & Young
University College London - Cruciform	Ernst & Young	Signed	Jarvis plc	Consortium member	Ernst & Young
Defence Housing Executive - Serviced families Accommodation	KPMG PPP Advisory Services	Signed	John Mowlem	Bidder	KPMG
A92 Dundee - Arboarth	KPMG PPP Advisory Services	Shortlist	John Mowlem	Shortlisted bidder	KPMG

Cerdigion CC - Penweddig School	KPMG PPP Advisory Services	Signed	John Mowlem	Consortium member	KPMG
Oxford Radcliffe Hospitals NHS Trust - Radcliffe Infirmary	KPMG PPP Advisory Services	Shortlist	John Mowlem	Shortlisted bidder	KPMG
A13 Thames Gateway	KPMG PPP Advisory Services	Signed	John Laing	Shortlisted Bidder	KPMG
A13 Thames Gateway	KPMG PPP Advisory Services	Signed	Amec	Consortium member	KPMG
Newport CBC - Southern Distributor Road (SDR)	KPMG PPP Advisory Services	Signed	John Laing	Shortlisted Bidder	KPMG
Newport CBC - Southern Distributor Road (SDR)	KPMG PPP Advisory Services	Signed	Amec	Shortlisted Bidder	KPMG
Newport CBC - Southern Distributor Road (SDR)	KPMG PPP Advisory Services	Signed	Carrillion	Shortlisted Bidder	KPMG
University Hospitals Coventry and Warwickshire NHS trust - New Hospital	KPMG PPP Advisory Services	Preferred Partner	John Laing	Shortlisted Bidder	KPMG
West Middlesex University Hospital NHS Trust	KPMG PPP Advisory Services	Signed	John Laing	Shortlisted Bidder	KPMG
West Middlesex University Hospital NHS Trust	KPMG PPP Advisory Services	Signed	Amec	Pre qualified Bidder	KPMG
North Staffordshire Combined Healthcare NHS trust -Reprovision of Mental Health Facilities	KPMG PPP Advisory Services	Signed	Carrillion	Consortium Member	KPMG

Secure Training Centre - Cookham Wood/Medway	KPMG PPP Advisory Services	Signed	Carrillion	Consortium Member	KPMG
South West London Community NHS Trust - Queen Mary's Hospital	KPMG PPP Advisory Services	On Hold	Carrillion	Shortlisted Bidder	KPMG
University Hospitals Coventry and Warwicshire NHS Trust - New Hospital	KPMG PPP Advisory Services	Preferred Partner	Carrillion	Shortlisted Bidder	KPMG
University of Hertfordshire - Accommodation and Sports Facilities	KPMG PPP Advisory Services	Signed	Carrillion	Consortium Member	KPMG
Calderdale & Huddersfield Healthcare NHS Trust - Halifax General Hospital	PwC	Signed	Sodexho Holdings	Consortium Member	PwC
Central Manchester & Manchester Children's University Hospitals NHS Trust	PwC	Preq-Qualification/ Bidder Stage	Sodexho Holdings	Shortlisted Bidder	PwC
Fazakerley Prison/ HMP Altcourse	PwC	Signed	Sodexho Holdings	Shortlisted Bidder	PwC
The Royal Logistics Corps	PwC	Shortlist	Sodexho Holdings	Shortlisted Bidder	PwC
Wirral Metropolitan Borough council - schools	PwC	Signed	Sodexho Holdings	Consortium Bidder	PwC
A92 Dundee - Arboarth	PwC	Shortlist	WS Atkins	Shortlisted Bidder	PwC
Ayshire & Arran Community Health Trust - Cumnock Community Hospital	PwC	Signed	WS Atkins	Consortium Member	PwC

Bridgend Prison	PwC	Signed	WS Atkins	Consortium member	PwC
Cornwall County Council - Schools	PwC	Signed	WS Atkins	Consortium member	PwC
Dept of education (NI) - Belfast Institute of Further & Higher Education	PwC	Signed	WS Atkins	Consortium member	PwC
Dept of Education (NI)-Northwest Institute of Further and Higher Education	PwC	Signed	WS Atkins	Consortium member	PwC
Doncaster & South Humber Healthcare NHS Trust - Mental Health Facilities	PwC	Signed	WS Atkins	Shortlisted bidder	PwC
East Renfrewshire Council - M77/ Glasgow South Orbital Road	PwC	Shortlist	WS Atkins	Shortlisted bidder	PwC
East Riding of Yokshire Council - East Riding Grouped Schools	PwC	Signed	WS Atkins	Shortlisted bidder	PwC

It is therefore explicit that the role of the MAFs is not limited to professionally handling the privatisation decisions of the government. It extends to lobbying for formulation of the policies for privatisation. It also includes manipulating the very process of privatisation. It is a maze. From the above discussions one can understand how and why the MAFs are in India. The policy of privatisation is a golden goose. Their own governments incentivise them to lobby and promote privatisation in countries like not so much for the benefit of India as for the promotion of export of privatisation expertise of the MAFs.

Thousands of violations of audit independence requirements and ethical standards and acquiescing in fraud

There is a myth in India that the MAFs, which keep giving certificates of good and bad character to the players in Indian economy, are superior in standards of audit and in ethical considerations. The first consequence of the assumption that they are a superior breed is on

the Indian CAs. Their very presence has devalued the Indian CA profession, except the Indian CAs employed by them or affiliated to them. They did not only devalue the Indian CA profession. They also evaluate and give certificates for different segments of the Indian economy. For instance sometime ago KPMG gave a report, titled annual fraud survey virtually stating that the youthful executives in corporate India are fraudulent. These certificates are taken as Gospel in India. That is the effect of the aura attached to the MAFs in India. They make presentations and suggestions to the authorities. The authorities also receive their advice and recommendations with reverence. This is because of the brand effect, not because of their verified worth. It is therefore necessary to bring on record their true performance as accountants.

They have violated such simple rule as that which prohibits the auditors from having pecuniary stake in the client whose accounts the auditors certify. This violation has no taken place once, but thousands of times, in the case of one MAF, that is PwC alone. This is what the Mitchell-Sikka study says about this basic rule violation by the MAFs. These are mere illustrative, not exhaustive of their violations.

In the case of PwC

In January 1999, the US regulator, the SEC, censured PricewaterhouseCoppers (PwC) for "violating auditor independence rules and improper professional conduct" (SEC press release, 6 January 2000) and ordered an internal review of PwC's compliance with the rules of auditor independence. As part of review, PwC staff and partners were asked to self-report independence violations, and the independent reviewers were asked to randomly test a sample of the responses for completeness and accuracy. The review revealed more than 8,000 violations, including those from partners responsible for overseeing and preventing violations. The report concluded that there was "widespread Independence non-compliance at PwC... despite clear warnings that SEC was overseeing... 77.5% of partners and 8.5% non-partners selected for audit in Random Sample Study failed to report at least one violation. ... Many of the partners had substantial number of previously unreported violations. A total of approximately 86.5% of partners and 10.5% of non-partners in the Random Sample Study had at least one reported or unreported Independence Violation. These results suggest that a far greater percentage of individuals in PwC's firmwide population had Independence violations than was revealed by the self-reporting process .... The number of violations .... reflect ***serious structural and cultural problems*** [emphasis added] that were rooted in both its legacy firms [Price Waterhouse and Coppers & Lybrand merged to form PwC]."

Source: Securities and Exchange Commission, 2000, pp. 122-123.

In the case of Ernst & Young

In May 2002, the SEC accused Ernst & Young of violating the ethics rules by having a seven-year business relationship with a client, PeopleSoft (The New York Times, 21 May 2002). The SEC alleges that whilst Ernst & Young was auditing the company, its tax department and PeopleSoft jointly developed and marketed computer program to help clients manage payroll and tax withholding for overseas employees. As part of the joint venture, Ernst & Young agreed to pay PeopleSoft royalties of 15% to 30% for each sale of the program.

In the case of KPMG

In pursuit of profits, accountancy firms continue to have deep organizational and cultural problems in complying with the rules. Further

support for this view is provided by an investigation by the Securities and Exchange Commission (SEC). In June 2000, the SEC started "look back" program and required major accounting firms to review their independence procedure and violations (SEC press release, 7 June 2000). As part of this, KPMG was admonished (SEC press release, 14 January 2002). The findings showed that contrary to the 'independence' rules, KPMG had a substantial investment in Short-Term Investment Trust (STIT), part of the AIM Funds, a collection of mutual funds audited by the firm. After the initial investment of $25 million, KPMG made 11 additional investments and by September 2000, its investment constituted some 15% of the STIT's net assets. The audit firm issued reports stating that it was "not aware of any relationship between [KPMG] and [AIM] Funds that, in our professional judgment, may reasonably be thought to bear on our independence".

The violation of auditor independence rules was highlighted by third parties, as KPMG did not have the necessary organisational procedures. As the SEC put it,

> "KPMG lacked adequate policies and procedures designed to prevent and detect independence problems caused by investment of the firm's surplus cash. The failure constituted an extreme departure from the standards of ordinary care, and resulted in violations of the auditor independence requirements imposed by the Commission's rules..."
>
> **Source:** SEC press release, 14 January 2002, p.6).

Thus the record of the MAFs compares poorly with the record of the Indian CA firms. Yet the public image is the other way round. It is necessary that the Indian accounting profession endeavours to clear this impression. This is in the larger interest of Indian corporate sector, of the accounting profession and also in the larger national interest.

Expertise in advising and executing tax-evasion and tax fraud to clients causing losses to governments of billions of dollars

The MAFs are skilled in advising and executing global level and trans-country tax evasion and promote tax frauds. They do so openly. This is what the Mitchell-Sikka study has to say about this dimension of the work of MAFs:

All over the world, ordinary people bear a higher share of tax to finance essential social infrastructure. This burden is increasing because a rich elite and many major corporations are avoiding taxes through novel avoidance schemes. Major accountancy firms charge around £500 per hour to devise elaborate schemes for tax avoidance. Accountancy firms, such as Arthur Andersen, KPMG, Deloitte & Touche, PricewaterhouseCoopers (PwC) and Grant Thornton have become multinational enterprises by advising companies on strategies for avoiding taxes (New York Times, 16 April 2002). A favourite tactic is to advise major corporations and the rich to escape to secretive offshore tax heavens. Developing countries are losing some US$50 billion due to tax avoidance. The UK tax payer is estimated to be losing some £85 billion of tax revenues (Mitchell et al., 2002). Inevitably, ordinary people bear the cost of this by paying a higher proportion of their income in taxes and receiving worse public services.

One of the MAFs went to the extent of devising a secret scheme for tax evasion. This has been explained in the website The Catsbird Seat, in a write up by Charles Lewis and Bill Allison titled "The Cheating of America". It reads:

On May 4, 1999, **PricewaterhouseCoopers L.L.P.** sent out a confidential letter, some 22,000

words in length, to invite corporations to take part in its **Bond and Options Sales Strategy,** or **BOSS shelter,** which, like the shelter Merrill Lynch sold, **involved investment vehicles with foreign partners created solely to provide a paper tax loss....**

On Dec 9, 1999, the Treasury Dept issued notice 99-59, warning companies that if they made use of BOSS, the IRS would challenge any losses they claimed.

Representative Lloyd Doggett (D) of Texas and a member of the House Ways and Means Committee ... issued a statement welcoming the notice. "While encouraged that Treasury has quickly shut down an obviously abusive tax shelter," he said, "I am reminded that one Big Five accounting firm requires staff to cook up a new shelter every week."

This skill does not include the more skilled game of money laundering in which the MAFs seem to have greater expertise.

Thus by any yardstick the MAFs are emerging as a great public risk and even greater public mischief, unless the national regulators wake up and act fast. The Mitchell-Sikka study concludes the chapter on 'Money, Money, Money as under which is very apt to be quoted here:

'Accountancy business is big business. Concerns about efficiency, accountability, stewardship and primacy of private property rights encourage social investment in surveillance systems, such as accounting and auditing. Capitalist enterprises legitimize their operations by audits and people are encouraged to believe that the published information is somehow reasonable and fair. Auditors are often portrayed as watchdogs. Such images have enabled accountancy firms to secure state guaranteed monopolies of auditing and insolvency industries, but without a 'duty of care' to stake holders affected by their actions. These monopolies are regulated by accountancy trade associations rather than by an independent regulator. In such an environment, accountancy firms make profits by heaping misery on others. To make profits, accountancy firms have been placing thriving businesses into receiverships and liquidation (Cousins et al., 2000). Ordinary people have lost their homes, jobs, businesses and savings whilst firms collect fees for many years.

The world of insolvency and auditing are dominated by handful of secretive firms who publish little meaningful information about their affairs. They operate cartels, all with a view to making private gains and disadvantaging the wider public. They have added money laundering, bribery and obstruction of legitimate inquiries to their trade. Upon discovery of audit failures and abuses of insolvency services, some may expect one major firm to give evidence on the incompetence of another. But the pursuit of profits has created new brotherhoods of deceit and silence. In November 1998, the *New Zealand case of Wilson Neil Vs Deloitte - High Court, Auckland, CP 585/97, 13 November 1998* revealed that "The major accounting firms have in place a protocol agreement promising none will give evidence criticising the professional competence of other Chartered Accountants" (reported in the (New Zealand) Chartered Accountants' Journal, April 1999, p.70). In an ideal world, the regulators would step in and tackle the institutionalised corruption of accountancy industry. But accountancy firms live in a world regulated by accountancy trade associations. As our investigation of accountancy firm involvement in money laundering showed (Mitchell et al., 1998) accountancy regulators are primarily concerned with shielding accountancy firms rather than tackling the abuses.'

This sums up the world of MAFs, their operation and activities, their culture and ethics and their philosophy and models.

THE WESTERN GOVERNMENTS' GROWING CONCERN AT MAFs

The litany of scandals that were exposed in an incredible pace has shattered the credibility of these MAFs completely and has destroyed the confidence of public in the west in them, who are rightly perceived as the prime abettors of these acts. The urgent need to rein these firms has been felt by countries like UK, which is contemplating several steps towards this direction.

U.K. GOVERNMENT'S INITIATIVE

The Office of Fair Trading examined the case for a competition inquiry into the big four accounting firms - PWC, Ernst & Young; KPMG; and Deloitte & Touché - after MPs urged the government to break their dominance. Patricia Hewitt, the trade and industry secretary published a report setting out a series of possible reforms to restore confidence in audited accounts. The Commons Treasury select committee called for the Competition Commission to hold an inquiry into the dominance of the big four accounting firms. "It is not clear to us that the market is truly competitive," it said. To help reduce the degree of concentration in the accounting industry, the committee asked the government to place more work with other firms.

The UK government has asked the OFT to examine the case for a competition inquiry, though it would be difficult for an inquiry to recommend the break-up of one of the firms because they were global businesses:

MPs in UK expressed support for the mandatory rotation of audit firms every five years, and called for restrictions on non-audit services offered by accountants to audit clients. The big four firms are opposed to audit firm rotation and restrictions on non-audit work.

The Treasury select committee said it would be "dangerously complacent" to assume that the risk of an Enron-style corporate failure in the UK was lower than in the US.

(SOURCE: ANDREW PARKER: FINANCIAL CORRESPONDENT, FT.com-24.07.02 and a complete text of the same is given in ANNEX 2 to this document. Further we have placed in ANNEX 4 and ANNEX 5 certain relevant reports of the UK government).

ITALIAN GOVERNMENT'S ACTION

The Mitchell-Sikka study notes the action taken by the Italian government to prevent the MAFs from cartelising the market. The study says:

The carefully constructed veneer of professionalism conceals anti-social practices. They operate cartels of carve-up and control markets. Italy's competition authority has fined five leading accountancy firms £1.4 millions for anti-competitive practices between 1991 and 1998. The competition authority said it was fining Ernst & Young, PricewaterhouseCoopers (PwC was formed by the merger of Price Water House and Coppers & Lybrand in 1998), Deloitte Touche Tomatsu, KPMG and Arthur Andersen for "consistently distorting market competition in Italian accountancy services", in particular by standardising prices co-ordinated to win clients. The firms admitted the charges and provided information which helped the Italian competition watchdog in its inquiry. The antitrust body said that it had taken this into account when imposing the fines (Financial Times, 22 Feb 2000, p.8).

Thus national regulators have begun taking action against the malpractices of the MAFs. After the Enron fraud came out the US Securities Exchange Commission has begun taking a tough line against the MAFs. This is evident from the unprecedented step taken by SEC to issue show cause notice to E&Y to stop accepting new audit work of listed companies. The US government has also legislated to curb malpractices, through the Sarbanes law.

CHAPTER VIII:

THE TRACK RECORD OF INDIVIDUAL MAFs - A CONTINUING STORY OF COMPLICITY IN CORPORATE WRONGS TO ASSISTING AND PLANNING WRONGS:

It is necessary at this stage to set out the individual record of the different MAFs so as to enable the different stake holders in the Indian economy -- the government, the public sector undertakings, the corporates, the regulators, the Indian accounting profession and the media and the general public --- to know about their true image and worth.

CASES INVOLVING PRICEWATERHOUSE COOPERS

The following cases demonstrate the failure of PWC, in some cases wilful failure, to discover blatant accounting frauds and the failure to maintain one of the cardinal principles of auditing-INDEPENDENCE.

In the first case, the SEC is seeking to sanction Coopers & Lybrand (later merged with Price Waterhouse to become PriceWaterhouse Coopers in July 1998) because of their failure to discover that their client, Advanced Micro Devices, had falsified over one third of its 1994 revenues by booking non-existent sales to bogus companies. The Coopers gave Advanced Micro Devices a clean bill of health less than one month after the company wrote off half of its receivables because of supposed "returns."

According to the SEC, Coopers & Lybrand ignored some pretty prominent red flags. The SEC is troubled by the failure of the Coopers audit team to discover a series of blatant accounting frauds by Advanced Micro Devices that should not have, according to the Commission, so easily escaped detection. The SEC cited, as examples, the fact that the Company booked revenues from sales before products were even shipped, recorded bogus shipments, booked sales before customers wanted them, failed to reverse sales when customers returned goods, and paid distributors to accept products that had unlimited rights of return.

In the second case the SEC made public, the report of an independent consultant who reviewed possible independence rule violations by accountants at PriceWaterhouse Coopers (PWC). The consultant's review disclosed that PWC has failed to maintain its independence from corporate clients. Outside auditors are required to remain "independent" from their corporate clients so that they can fairly and objectively assess a company's financial condition. This means, among other things, that auditors may not own shares of their clients. According to the Report, PWC violated this standard at an alarming rate. The independent consultant discovered that almost half of the PWC partners reported at least one independence violation - 1301 of the firm's 2698 partners held shares in one or more of PWC's clients. Worse yet, the PWC partners reported an average of five violations per person, with 153 of the partners reporting ten or more violations. Over 2500 violations involved holding a client's stock or options. The report had mentioned 'Investors want to know whether they can rely upon the integrity of financial statements. The SEC

appears to share that concern. Will it lead to further SEC action, and will auditors now rededicate themselves to maintaining independence?'

Source: www.stockpatrol.com

AUDITOR'S INDEPENDENCE AND CONFLICT OF INTEREST CASE

Name of the Firm	PriceWaterhouseCoopers LLP
Nature of Allegation	Conflict of interest with Audit Clients
Investigator	SEC
Amount of penalty or compensation paid	$ 2.5 million
Source	WSJ-15.01.99-Michael Schroeder and Elizabeth Macdonald

Facts: The SEC has accused that PWC LLP and some of its partners and managers have violated the concept of auditor's independence by investing in 70 companies in which they were the auditors. This is the largest case involving conflict of interest handled by the SEC so far. PWC neither denied nor accepted the allegation but allowed it to be censured and agreed to establish a $ 2.5 million education fund for accountants, to improve its internal procedure and to conduct an internal investigation supervised by an outsider named by SEC.PWC was formed in July 1998 by merger of Coopers and Lybrand & Price Waterhouse LLP. According to SEC, between 1996 & 1998, C & L's compliance procedure failed to detect 35 instances in which 11 professional employers primarily in the firm's Tampa, Florida's office, bought stock in companies for which the firm provided audit and other services. SEC further alleged that C&L's company wide retirement plan owned stock in 45 public held audit clients. Some of those violations involved merged entity. The firm admitted the violation and accepted responsibility for those incidents and agreed to the terms of the settlement. This action of the SEC is one of a growing number of actions involving big five accounting firms and public companies as part of a campaign against accounting fraud. Incidentally, PWC's top executive James Schiro, is on the board of independence Standards Boards, which primarily overseas the auditor's independence. SEC has termed the magnitude of the violation makes this an unusual case.

MICRO STRATEGY & RAYTHEON CO

Name of the firm	PriceWaterhouseCoopers LLP
Nature of Allegation	Conflict of interest with Audit Clients
Investigator	SEC
Amount of penalty or compensation paid	$ 55 million in Micro Strategy Inc
Source	US News and World Report, 23.07.2001-Marianne Lavelle & Business Line 16.05.2001

Facts: PWC agreed to pay $ 55 million to settle a class-action lawsuit by Shareholders of Micro Strategy Inc. It got embroiled in a class action court case in which shareholders of the company accused the audit agency of misleading them by certifying profit figures for 1999. The audited financial statement showed earnings of $12.6 million on a revenue of $205 million in 1999, whereas the true position was that Micro Strategy had incurred a net loss of $33.7 million on an earning of $151 million! The same company under the mentoring of the same audit firm had shown profits in 1997 and 1998 also which subsequently turned out to be losses.

The direct consequence of all this fiddling was to catapult the share price of the company to $333 in March 2000 from a 1998 initial offering

price of a mere $6 per share. It sank to $1.75 in April, and recovered slightly and stood at $4.95 on May 9. The utter devastation caused by the stocks collapse was one of the factors that forced the audit firm to settle without further ado, although it claims that it soon corrected its earlier certificate of profit to reflect the real state of affairs. It has offered no explanation why it gave a false certificate in the first place.

The travails of PriceWaterhouse Coopers is not expected to end with the payment of the hefty penalty. The US Securities and Exchange Commission sources revealed that it had taken up the possible wrongdoing inherent in the practices adopted by the auditors for investigation. ``The latest development in the sordid series of happenings is the resignation of Mr James J .Schiro, the Chief Executive Officer of the audit company. No reason was cited, but the New York Times in its report of May 12, mentions the Micro Strategy imbroglio as also the humiliation suffered by the firm when the SEC issued a report in January 2000 that Pricewaterhouse Coopers gravely compromised its independence by allowing its partners to hold investments in companies of which it was also the auditor and by undertaking non-audit (consultancy) services for them.''

PWC profited from consulting for Micro Strategy and also acted as reseller for some of its software. PWC denied its independence has been impaired, but this will not be firm's last such legal tussle.

A pending lawsuit by Raytheon Co's shareholders, who lost millions when the defence contractor restated its earnings, may also raise the conflict issue. Nearly 95% of the $ 51 million Raytheon paid PWC last year was for non audit services though Raytheon says much of that was for work it considered audit related like tax services. Investors allege that if an accounting firm was making money from its audit client through non-audit services, "it shows motive".

HOME STATE HOLDING INC CASE

Name of the firm	**PriceWaterhouseCoopers LLP**
Nature of Allegation	Failure to detect financial stability
Sued by	Superintendent of Insurance, New York
Amount of penalty or compensation paid/ demanded	$ 100 million
Source	www.insure.com Joe Frey- website last updated on 03.11.00

Facts: The New York superintendent of insurance, Neil Levin, has filed a lawsuit against PWC LLP alleging the firm was negligent in its audit of three failed insurance companies that cost New York residents $100 million. Coopers and Lybrand, which merged with PWC in 1998, served as financial auditor for Home State Holdings Inc and two of its subsidiaries, Home Mutual Insurance Co and New York merchant Bakers Insurance Co., from 1989 to 1997. The lawsuit alleges that PWC failed to catch "numerous red flags" about the insurer's financial stability that could have prevented insolvency. They filed for bankruptcy in 1998. The lawsuit alleges the failure of the PWC to notify the insurance department that Home State failed to maintain enough cash reserves to pay claims. Mr. Levin, is seeking $ 100 million in punitive damages from PWC to offset the estimated price tag that New York state insurance guarantee funds-which are financed by all policyholders in the state through insurance premiums- had to pay to rescue Home State's insolvent subsidiaries. PWC maintained that the lawsuit is totally without merit and his company plans to vigorously fight it.

TYCO INTERNATIONAL CASE

Name of the Firm	PriceWaterhouseCoopers LLP
Nature of Allegation	Failure to disclosure bonus payments to CEO of Tyco International
Sued by	New York State
Amount of penalty or compensation paid	
Source	New York Times-09.10.02 & Bloomberg News

Facts: Manhattan district attorney is examining whether PWC auditors based New York and Boston broke the law when they failed to disclose that a proxy statement did not include $ 33 million bonus paid to then CEO Dennis Kozlowski of Tyco International. Mr. Kozlowski was indicted in Sept 02 for looting Tyco International. In this connection, New York State Prosecutors are considering criminal charges against PWC, who reviewed the compensation paid to the former CEO of Tyco International.

CORPORATE COMMUNICATION CASE

Name of the Firm	PriceWaterhouse Coopers LLP
Nature of Allegation	PWC's patent disregard for the ethical standards of ICAEW in undertaking the receivership of a company with which it had a material professional relationship. More shockingly, the first piece reveals the clandestine understanding that PWC as a receiver had with directors of the company, to sell the assets of the company to the very directors at less than half its acknowledged realisable value, and in the process deprive the unsecured creditors of the company of their legitimate dues.
Source	Extracted from Insolvency, Market Professionalism and the Commodification of Professional Expertise by:Patricia Arnold, University of Wisconsin-Milwaukee ;Christine Cooper, University of Strathclyde and Prem Sikka, University of Essex

Facts: Corporate Communications was the darling of the 1980's, was audited by Price Waterhouse (now part of PriceWaterhouseCoopers) who also acted as advisers. An unqualified audit opinion was given on the 1990 accounts, but it was subsequently learnt that the affairs of a subsidiary had been omitted from the accounts altogether. Before the 1991 accounts could be finalized, it appeared that the company would break its financial covenants to the bank. Price Waterhouse was asked to prepare a restructuring package. For this the firm's fees came to more than a million pounds. The company was told that its restructuring proposals were not acceptable and was placed into receivership as its bankers, the Royal Bank of Scotland, were unwilling to restructure its finances. Coopers & Lybrand (subsequently part of PriceWaterhouse Coopers) were appointed as receivers and the main part of the business was sold back to the directors at half the price of its value at £11 million (including debts of £32 million). Corporate Communications' bankers had got their money back, but the main casualties were the unsecured creditors, estimated to be losing some £16 million. The receivers explained that the assets had been sold off and that no money was available for unsecured creditors.

Some leaked documents (secured by the BBC Radio for its File on Four programs broadcast on

21 June and 25 June 1994) showed that, at least a month before the receivers were called in, the group's management and bankers were considering a plan to transfer all the group's assets to brand new companies, leaving the main creditor, its landlord, high and dry. Another document showed that just three days (i.e. 27 July 1992) before the date they were appointed, the receivers took part in discussions about how to sell the main assets back to the management. A letter from the company's US based lawyers stated that "The proposed receivership for Corporate Communications plc, the senior management, and the Bank of Scotland, are discussing the following transaction to be offered after the receivership of Corporate Communications". The letter then went on to detail a complex mechanism for buying the company in a way that "accommodates all of our respective concerns". The concerns of the people who would lose their money were not mentioned. No one other than the directors was given enough time to bid for the company's assets. No creditor was told of the prior connection between the receivers and the company management.

The ethical guidelines issued by the ICAEW stated, "where there has been a material professional relationship with a company, no principal or employees of the practice should hold appointment as a receiver in relation to that company" (ICAEW, 1979). In this case, Coopers had been doing work for the company and its management before their appointment as receivers. This is a classic case conflict of interests and breach of ethical guidelines.

THE ROBERT MAXWELL'S CASE

Name of the Firm	PriceWaterhouseCoopers LLP
Nature of Allegation	The firm was heavily censured for its 'Incompetence', 'Lack of independent judgment' and 'Lack of robust implementation' of audit procedures
Fined by	Tribunal of the accountancy profession's Joint Disciplinary Scheme (JDS)
Amount of penalty or compensation paid	£1.2m plus £2.1m costs
Source	The Associated News Papers Ltd

Facts: Robert Maxwell's publishing and newspaper, empire spectacularly collapsed shortly after his death at 68 in November 1991. It emerged he had stolen more than £400m from pension funds in a desperate bid to keep his debt-laden companies afloat.

Eight years later, a tribunal of the accountancy profession's joint disciplinary scheme (JDS) fined Coopers & Lybrand, auditor of several Maxwell companies, £1.2m plus £2.1m costs. The firm was also heavily censured for its 'incompetence', 'lack of independent judgment' and 'a lack of robust implementation' of audit procedures.

Coopers accountants John Cowling, Stephen Wootten, Ian Steere and Nicholas Parker were also admonished, fined or ordered to pay costs. Michael Stoney, the former deputy-managing director (finance) of MGN, was heavily censured and excluded from membership of the profession.

THE BCCI CASE

Name of the Firm	PriceWaterhouseCoopers LLP
Nature of Allegation	Investigation by JDS into alleged failure of the firm in the audit of BCCI
Fined by	Tribunal of the accountancy profession's Joint Disciplinary Scheme (JDS)
Amount of penalty or compensation paid/claimed	$ 3.5 billion
Source	The Associated News Papers Ltd & Accounting, dishonour and a dash of bad manners-Robert A Spira & Shirley Goldstein

Facts: The Bank of Credit and Commerce International collapsed in 1991. Thousands of investors (mainly Asian) lost some £800m in the crash, one of the biggest frauds in banking history, when corrupt managers illegally siphoned off funds.

An initial investigation into the BCCI auditors, accountancy firm PriceWaterhouse, was hauled by the Court of Appeal in 1993 because of pending litigation by the bank's liquidators against its management. The court case was settled in 1999 and a fresh JDS investigation is now under way - 11 years after the scandal. PriceWaterhouse (now part of PriceWaterhouseCoopers) became the auditor of the fraud-infested Bank of Credit and Commerce International (BCCI) by claiming it was a 'global' firm. In 1991, after the forced closure of BCCI, a committee of the US Senate conducted an inquiry into the $11b frauds and audit failures. It subpoenaed Price Waterhouse to produce its files, including the papers held by its UK offices. At this point, the US office of the firm claimed: 'The British partnership of Price Waterhouse did not do business in the US and could not be reached by subpoena.'

The firm added: 'The 26 Price Waterhouse firms practise, directly or through affiliated Price Waterhouse firms, in more than 90 countries throughout the world. Price Waterhouse firms are separate and independent legal entities whose activities are subject to the laws and professional obligations of the countries in which they practise. No partner of PW-US is a partner of the Price Waterhouse firm in the United Kingdom; each firm elects its own senior partners; neither firm controls the other; each firm separately determines to hire and terminate its own professional and administrative staff;. each firm has its own clients; the firms do not share in each other's revenues or assets; and each separately maintains possession, custody and control over its own books and records, including work papers. The same independent and autonomous relationship exists between PW-US and the Price Waterhouse firms with practices in Luxembourg and Grand Cayman.' In the investigation report of this case a detailed analysis was made about the role of the auditors.

The US Senate inquiry also learned that ultimate control of Price Waterhouse rested with Price Waterhouse Worldwide, based in Bermuda, which did not co-operate with the US Justice Department.

To cite another example of Price Waterhouse's conduct and co-operation in investigations carried out by statutory authorities, in 1996, the Justice Department pursued a fraudster operating a shell company, Merlin Overseas Limited, from Antigua. It consisted of little more than a fax machine in a Caribbean office of Price Waterhouse. The Manhattan district attorney prosecuted the fraudster, but could not get at Price Waterhouse. The district attorney's office asked Price Waterhouse in Manhattan for help, but was told that Price Waterhouse in Antigua is not the same legal creature as the one in New York.

ANICOM CASE

Name of the Firm	**PriceWaterhouseCoopers LLP**
Nature of Allegation financial statements	Reckless in certification of
Sued By	The shareholders of the company
Amount of penalty or compensation paid	$ 21.5 m
Source	Economic Times 30.10.02

Facts: PWC LLP agreed to pay $ 21.5 million to settle law suits by Anicom shareholders and creditors accusing the firm of recklessness in certifying Anicom's books up to Jan 2001

bankruptcy, court filing. The accounting firm decided the settle the suit to avoid the cost and uncertainty associated with protracted litigation. The payment is among the largest settlements to date, over an alleged audit failure by PWC.

HPL TECHNOLOGY GROUP CASE

Name of the Firm	PriceWaterhouseCoopers LLP
Nature of Allegation	False certification of financial statements
Sued By	Mr. Mark Harward, Mr. Brenda Stoner and Mr. Merrill Wertheiner
Amount of penalty or compensation paid/claimed	Sued for $ 100 m with UBS Warburg
Source	Business Line 19.10.02

Facts: Three HPL technologies Inc. shareholders slapped accounting firm PWC and UBS Warburg with a lawsuit in a bid to recover $100 million in damages, claiming the two firms assisted the software maker in overstating revenues. The law suit on behalf of Mr. Mark Harward, Mr. Brenda Stoner and Mr. Merrill Wertheiner filed in Dallas state district court alleged that PWC falsely certified HPL's financial statements. UBS Warburg, which underwrote HPL's IPO was named a defendant .The three plaintiffs in February sold their company Covalar Technologies Group Inc. and its subsidiary Test Chip technologist to HPL for a total of $10 million in cash and about $33 million in HPL stock, which traded at about $14 before the accounting irregularities were disclosed. But the trio estimates it lost about $30 million since HPL's share price plunged following the accounting scandal, said Mr Mark Werbner, lead counsel for the plaintiffs and the partner at law firm Sayles, Lidji and Werbner. A PWC spokesman said the firm does not comment on matters of litigation. UBS warbug, a unit of Switzerland's UBS AG, was not available for to comment. "We may later bring claims and HPL and potentially officers and directors, but for now, we want to focus on the responsibility of PWC and UBS because they were essential component to carrying out the fraud", said Mr Werbner. "It's inexcusable that an audit could have been done and not detected these irregularities."

THE POLLY PECK GROUP CASE

Name of the Firm	PriceWaterhouseCoopers LLP Touche Ross (part of Deloitte & Touche)
Nature of Allegation	Unethical Practices
Source	Extracted from Insolvency, Market Professionalism and the Commodification of Professional Expertise by:Patricia Arnold, University of Wisconsin-Milwaukee ;Christine Cooper, University of Strathclyde and Prem Sikka, University of Essex

Facts: With pre-tax profits of £161.4 million, net assets of £845 million and 17,227 employees, the Polly Peck group was one of Britain's major quoted companies. In October 1990, it collapsed. Insolvency practitioners from Coopers & Lybrand (now part of PricewaterhouseCoopers) together with Touche Ross (now part of Deloitte & Touche) were appointed joint administrators of the company. By June 1991, the firms had received £2.56 and £5.8 million respectively in fees. The ICAEW's code of ethics required that firms should avoid conflict of interests and not accept appointments that give rise to, or give appearance of, conflict of interests. Despite the code of professional ethics, Coopers did not reveal its extensive links with Polly Peck and its chairman Asil Nadir. For example, Coopers had acted as joint reporting accountants when Polly

Peck originally went public (Accountancy Age, 23rd April 1992, p 11). Three of Cooper's partners were reported to be shareholders and acted as directors of Vemak (Jersey), a company that ran Asil Nadir's stately home and other property investments (Accountancy Age, 6th December 1990, p 1). Coopers also acted as personal tax advisor to Asil Nadir (Accountancy Age, 6th December 1990, p 1). The Channel Island's practice of Coopers had acted as auditor of Restro Investments through which Asil Nadir held his one time majority stake in Polly Peck. Coopers had also been involved with the Polly Peck group through consultancy assignments (Accountancy Age, 20th June 1991, p 1). A recommendation from Coopers led to the appointment of Polly Peck's Finance Director (Accountancy Age, 19th March 1992, p 3). Coopers' special work income from the Polly Peck group is estimated to have been £1.5million from 1985 to 1989 (Accountancy Age, 27th February 1992, p 1). The firm received £262,000 from auditing Polly peck's Far East operations (Accountancy Age, 27th February 1992, p 1).

Despite what appeared to be a very public non-compliance with the ICAEW's code of ethics, the Institute took no action. In March 1991, Austin Mitchell MP raised the matter with the DTI and a lengthy exchange of correspondence began. Much of the correspondence also received visibility in the press (see Mitchell et al., 1994; Cousins et al., 2000). Eventually, the ICAEW responded to pressures and a disciplinary hearing was held, behind closed-doors, on 12th October 1992. Coopers & Lybrand partners were found guilty of breaching the ethical guidelines (Financial Times, 16th October 1992, page 10). The ICAEW did not issue a statement until 30th November as it wished to negotiate the wording with Coopers (Accountancy Age, 26th November 1992, page 1; Financial Times 1st December 1992, page 6). Coopers' partners were fined £1,000 each (then the maximum possible) and ordered to pay costs of £1,000 each. No other penalties were imposed on the partners or the firm as the ICAEW argued that its rules do not enable it to take any action against the firm. There was no investigation of the overall standards of the firm. No report on the episode, which might have explained the delay in holding the disciplinary hearing, has been published. The receivers themselves did not highlight the Polly Peck affair. It was not highlighted by the monitoring visits of the insolvency regulators. At the time of filing the report by the quoted source (December 2001), the Polly Peck bankruptcy has still not been finalized and Coopers & Lybrand (and its successor firm) are estimated to have received £30 million in fees (Cousins et al., 2000).

SEC AUDITOR INDEPENDENCE CASE

Name of the Firm	PriceWaterhouseCoopers LLP
Nature of Allegation	Violation of Auditor's independence
Sued By	SEC
Amount of penalty or compensation paid/claimed	$ 5 m
Source	SEC-Press Release 17.07.02

Facts: The Securities and Exchange Commission announced a settled enforcement action against PriceWaterhouseCoopers LLP (PwC) and its broker-dealer affiliate, PricewaterhouseCoopers Securities LLC (PwCS), for violations of the auditor independence rules. The auditor independence violations span a five-year period from 1996 to 2001 and arise from (1) PwC's use of prohibited contingent fee arrangements with 14 different audit clients for which PwCS provided investment banking services, and (2) PwC's participation with two other audit clients, Pinnacle Holdings Inc. and Avon Products Inc.,

in the improper accounting of costs that included PwC's own consulting fees.

The SEC's order found that, by virtue of PwC's independence violations, the firm caused 16 PwC public audit clients to file financial statements with the SEC that did not comply with the reporting provisions of the federal securities laws. The order also finds that, in connection with the improper accounting of its consulting fees, PwC caused two of those clients to violate the reporting, record keeping, and/or internal controls provisions of the federal securities laws. PwC and PwCS agreed to pay a total of $5 million and PwC agreed to comply with significant remedial undertakings as a result of its settlement with the SEC. PwC also agreed to cease and desist from violating the auditor independence rules and to be censured for engaging in improper professional conduct.

The SEC's order finds that PwC's independence violations involved 16 separate audits of 16 public companies:

- From 1996 to 2001, PwC and one of its predecessors, Coopers & Lybrand, entered into impermissible contingent fee arrangements with 14 public audit clients. In each instance, the client hired the audit firm's investment bankers, either PwCs or Coopers & Lybrand Securities, to perform the financial advisory services for a fee that depended on the success of the transaction the client was pursuing. These fee arrangements violated the accounting professions' own prohibition against contingent fee arrangements with audit clients and violated the SEC's independence rules. As a result, the SEC found that PwC lacked the requisite independence when it performed the audits for these 14 public companies.
- In 1999 and 2000, PwC participated in and approved of the improper accounting of its own non-audit fees by two public audit clients, Pinnacle and Avon:
- In 1999 and 2000, while accounting for a 1999 acquisition of certain assets of Motorola, Inc., PwC assisted Pinnacle in establishing more than $24 million in improper reserves and in improperly capitalizing approximately $8.5 million in costs, including $6.8 million in fees paid to PwC for consulting and other non-audit services that should have been expensed. In April and May 2001, Pinnacle restated its accounting for the 1999 acquisition, and in December 2001, the SEC issued a settled cease and desist order against Pinnacle
- In the first quarter of 1999 and in its 1999 audit of Avon's financial statements, PwC assisted in and approved of Avon's improper accounting of an impaired asset that included PwC's non-audit consulting fees. In April 1999, after nearly three years and an investment of approximately $42 million, Avon stopped an uncompleted order-management software project that PwC consultants had attempted to develop for Avon's internal use. Instead of writing off all of the project's costs in the first quarter of 1999, however, Avon improperly retained $26 million, which was comprised mostly of PwC's own consulting fees. PwC participated in and approved of Avon's improper accounting, and also contributed to Avon's misleading disclosures concerning the accounting.
- For both Pinnacle and Avon, the SEC found that PwC failed to exercise the objective and impartial judgment required by the independence rules. In consenting to the SEC's order, PwC agreed to perform significant remedial undertakings designed to prevent the type of independence violations found in the order. Among these undertakings, PwC agreed to:

- Review new fee agreements for non-audit services before they are entered into with audit clients, to ensure that any "value added" fee arrangements do not violate the independence rules;
- Require an "independent reviewing partner" appointed from among PwC's Risk Management partners to:
  - o Review audits of SEC-registrants in which the audit client capitalizes PwC non-audit fees, to ensure that the accounting for those fees complies with the accounting rules and that the audits were performed in accordance with generally accepted auditing standards, including the Independence rules.
  - o Perform the audit procedures required by the AICPA SEC Practice Section for certain other audits that will be identified by considering risk factors that include the relationship and magnitude of PwC audit and non-audit fees; and
- Provide annual training for all PwC professionals on auditor independence issues.

CASES INVOLVING KPMG

POWER SCREEN CASE

Name of the firm	**KPMG**
Nature of allegation	Accounting malpractices
Investigator	ICAI
Amount of penalty or compensation paid	£ 275000
Source	BBC News-29.07.2002

Facts: KPMG has been fined for failing to spot a hole in the accounts of the subsidiary of Northern Irish Engineering Firm, Power screen in 1997. The Institute of Chartered Accountants of Ireland also reprimanded KPMG as part of the investigation into Ireland's one of the biggest financial scandals. In 1997, Power screen reported, a pre tax profits of £ 23.6 million ($ 37 m) and raised 18 million pounds through share issue in the stock market. However a month later Power Screen announced that an accounting irregularity in its British subsidiary Matbro led it to provide for 47 million pounds against the pre tax profits. Regulators have ordered KPMG and Saunders Graham, an audit partner, to pay a sum of £ 275000 ($ 430000) to the institute towards cost of inquiry. The inquiry concluded that KPMG and the audit partner "Fell below the standards expected of an auditor regulated by ICAI".

XEROX CASE

Name of the firm	**KPMG**
Nature of allegation	Misleading financial statements
Sued by	SEC
Amount of penalty or compensation paid	Outcome awaited.
Source	Reuters-22.01.03 & Accounting Web 23.01.03 & 30.01.03, SEC

Facts: KPMG is now under investigation by the SEC for audits of Xerox Corp., which recently paid a $10 million fine to settle a charge that it inflated several years of pre-tax earnings. After this fraudulent conduct was investigated and exposed, Xerox, employing a new auditor, issued a $6.1 billion restatement of its equipment revenues and a $1.9 billion restatement of its pre-tax earnings for the years 1997 through 2000.

The Commission's complaint alleges that the defendants' fraudulent conduct allowed Xerox to inflate equipment revenues by approximately $3 billion and inflate pre-tax earnings by approximately $1.2 billion in the company's 1997 through 2000 financial results.

Individual partners named in the suit include Michael A. Conway, the lead worldwide Xerox

engagement partner for the 2000 audit. Mr. Conway has also been the national managing partner of KPMG's Department of Professional Practice since 1990. The others are Joseph T. Boyle, the "relationship partner" on the Xerox engagement in 1999 and 2000; Anthony P. Dolanski, the lead engagement partner on Xerox's audits from 1995 through 1997; and Ronald A. Safran, the lead engagement partner on the 1998 and 1999 Xerox audits.

According to the SEC's, other KPMG auditors assigned to the engagement repeatedly warned the above partners that Xerox was manipulating earnings and revenues. The senior partners voiced their concerns to top management. But Xerox management continued its manipulations despite KPMG's concerns, and the SEC says the senior partners issued unqualified opinions without demanding that Xerox justify its accounting tactics.

Statements issued by KPMG indicated that the firm agreed there was a problem with the "tone at the top" at Xerox, but disagreed with the SEC's assessment of an audit failure. "The basic issue," explains KPMG, "is the timing of revenue realized by Xerox on its leases and, at the very worst, this is a disagreement over complex professional judgments."

PIE MUTUAL CASE

Name of the firm	KPMG
Nature of allegation	Accounting malpractices
Investigator	DOI-Ohio
Amount of penalty or compensation paid	$ 9.9 million
Source	www.insure.com Joe Frey-website last updated on 03.11.00

Facts: PIE Mutual was Ohio's largest medical malpractice insurer till 1998, when the DOI seized control of the company because its liabilities exceeded its assets by $ 275 million. The DOI alleged that KPMG "failed to detect that PIE had fraudulently recorded a $ 58 million asset on its financial statements" in 1996 and is currently liquidating PIE Mutual, attempting to pay off the estimated $ 600 million to $ 800 million in outstanding claims. It has recouped approximately $ 240 million from the sale of PIE mutual assets and a settlement with KPMG for $ 9.90 million.

RITE AID CASE

Name of the firm	KPMG
Nature of allegation	Attesting false financial statements
Sued by	Shareholders of Rite Aid
Amount of penalty or compensation paid	$ 125 m
Source	Accounting Web-11.03.03 & 04.06.03

Facts: Big Four accounting firm KPMG has agreed to pay $125 million as a result of a class action lawsuit filed by shareholders of Rite Aid, one of the largest drugstore chain. The action resulted from allegations that officers of the drugstore company made false statements to shareholders in published financial statements for the purpose of driving up the price of the company stock. The financial statements in question, which were audited by KPMG, were for fiscal years 1997 through 1999. Indictments are pending against four Rite Aid executives. KPMG stated that the firm resigned from its audit of Rite Aid in 1999 after alerting Rite Aid's audit committee of weaknesses in the company's internal audit controls. KPMG denied wrongdoing and stated that it agreed to the settlements "for practical business reasons."

OXFORD HEALTH PLAN

Name of the firm	KPMG
Nature of allegation opinion	Issuing false and misleading
Sued by	Shareholders of Oxford Health Plans
Amount of penalty or compensation paid	$ 75 m
Source	Accounting Web-11.03.03

Facts: KPMG has agreed to pay $75 million to shareholders of Oxford Health Plans after a computer snafu at Oxford in 1977 resulted in collection and payment delinquencies. KPMG was accused in the lawsuit of giving a false and misleading opinion.

KPMG denied wrongdoing and stated that it agreed to the settlements "for practical business reasons."

JINZHOU PORT CO

Name of the firm	KPMG
Nature of allegation	Falsified Financial Statements
Sued by	Shareholder of Jinzhou Port Co-China
Amount of penalty or compensation paid	
Source	Accounting Web-24.02.03

Facts: For the first time a Big Four accounting firm faced a lawsuit in China. The legal action was brought by a Jinzhou Port Co's. shareholder who has sued the company and KPMG alleging she lost money due to falsified financial statements.

Accounting problems surfaced at Jinzhou Port Co. in 2001 when an audit conducted by the Ministry of Finance produced information about inflated revenue and assets and understated costs at the company. Last year Jinzhou issued revised financial statements for 1996 to 2000 showing a change of 367.18 million yuan or approximately US$44 million. The Ministry of Finance fined Jinzhou 100,000 yuan or approximately US$12,000.

CASES INVOLVING ERNST & YOUNG

THE CENDANT CASE

Name of the Firm	Ernst & Young
Nature of allegation	Accounting irregularities
Sued by	Shareholders
Amount of penalty or compensation paid	$ 335 million & Two partners suspended by SEC from auditing public limited companies.
Source	Associated Press & New York Law Journal-Daniel Wise-22.08.2000 & Accounting web 01.05.03

Facts: Cendant, whose brands include Days Inn and Ramada Hotels, the Avis car rental agency, saw its stock plummet after the announcement of accounting irregularities, wiping out investors wealth by about $ 14.4 billion in a single day on 16.04.98. Cendant announced that CUC international, which merged with HFS Inc to create Cendant in 1997, had used irregular accounting practices to inflate earnings as much as $ 640 million over the previous 3 years. This prompted a class action suit by two major pension funds "the California Public Employees Retirement System" and the "New York State Common Retirement Fund" on behalf of all shareholders, accusing the former directors and officers of Cendant of selling Cendant,s shares prior to disclosures of accounting problems. In turn Cendant has sued Ernst & Young LLP which agreed to pay $ 335 million towards settlement for certifying the irregular accounts. SEC Suspended two partners involved in the

audit from auditing public limited companies for a period of 4 years.

SUPERIOR BANK CASE

Name of the Firm	Ernst & Young
Nature of Allegation	Failed audit work
Sued by	Federal Deposit Insurance Corporation
Amount of penalty or compensation paid/demanded	$ 548 million
Source	Accountancyage.com - 04.11.2002

Facts: US government agency FDIC has sued Ernst & Young for $ 548 million for its audit work of failed financial institution, Superior Bank. The allegation was Ernst & Young deliberately withheld information that would have exposed Superior's dire condition in an effort to avoid jeopardizing an $11 billion sale of its consulting unit. "As a direct result of Ernst & Young's gross misstatement of Superior Bank's assets, the bank became insolvent, which ultimately required the FDIC to pay out in excess of $750 million," the FDIC said in its complaint.

Ernst & Young eventually acknowledged that its audits of the ailing thrift were faulty, but the firm maintains that its own actions did not cause the failure. Instead, it blames a down economy. "We intend to vigorously defend all claims against the firm," Ernst & Young said in a statement.

AOL TIME WARNER CASE

Name of the Firm	Ernst & Young
Nature of Allegation	Material misrepresentation of accounts, Overstatement of revenue.
Investigated/Sued by	Department of Justice & SEC, Investors including University of California
Amount of penalty or compensation paid	
Source:	Washington Post-18.07.02, Accounting Web 17.04.03

Facts: AOL Time Warner is being investigated by the US Justice Department (DoJ) over its accounting practices, which raised questions about the way; AOL had booked online ad revenue. AOL Time Warner, in fact, admitted that the Securities and Exchange Commission (SEC) was looking into certain transactions at the company's Internet division. In a prepared statement, the company also said that if the DoJ wanted to look at the facts the company would cooperate.

M/s Kaplan Fox, the lawyer firm taking up the cases of investor class, has filed a class action suit against AOL Time Warner, Inc and certain of its officers and directors and Ernst & Young, in the United States District Court for the Southern District of New York. This suit is brought on behalf of all persons or entities who purchased, converted, exchanged or otherwise acquired the securities of America Online ("AOL") between July 19, 1999 and January 10, 2001 and all persons who purchased, converted, exchanged or otherwise acquired the securities of AOL Time Warner, Inc. ("AOL Time Warner") between January 11, 2001 and July 17, 2002, inclusive (the "Class Period").

The complaint alleged that AOL Time Warner and certain of its officers and directors violated

the federal securities laws. The complaint alleged, among other things that during the Class Period defendants made material misrepresentations and/or omitted to state material facts relating to AOL's online advertising revenues. The complaint further alleged that, AOL and AOL Time Warner booked revenue form one-time payments received from online advertising clients as advertising revenue in order to artificially inflate their revenues derived from online advertising. The complaint also alleged that as a result of Defendants' false and misleading statements, investors were damaged, by purchasing AOL and AOL Time Warner securities at artificially inflated levels during the Class Period and that Ernst & Young, violated the federal securities laws by certifying AOL Time Warner's financial statements as incorporated in AOL Time Warner's Annual Report for its fiscal year 2001 filed with the SEC on March 25, 2002 even though it knew (or recklessly failed to discover) that AOL had counted in revenue sums received in connection with selling online advertising for online auction site eBay. When the truth was revealed regarding AOL in an article in The Washington Post on July 18, 2002, AOL Time Warner stock dropped to as low as $11.75, down from its Class Period high of $58.51.

As a result of Defendants' false and misleading statements, investors were damaged, by purchasing AOL and AOL Time Warner securities at artificially inflated levels during the Class Period.

Further, the University of California (UC) filed suit on April 14 against Ernst & Young and 32 other defendants, claiming it misrepresented the financial situation of America Online and Time Warner around the time of the firms' 2001 merger. In the suit, the university claims that E&Y, concerned with holding on to a fat contract, helped falsify financial facts and continued to offer an unqualified audit opinion of the company long after it was clear that the company was in trouble.

SAVINGS AND LOAN CASE

Name of the Firm	Ernst & Young
Nature of Allegation	Failure to warn of disastrous financial problems that caused some of the USA's biggest thrift failures
Sued by	Federal Government-USA
Amount of penalty or compensation paid	$ 400 million
Source	Los Angeles Times-24.11.1992

Facts: Ernst & Young was almost the first to be rocked by financial scandals and much before the Big Five started making a pattern in a litany of scams, way back in early 1990s, E&Y ran into problems resulting from its role in several S&L scandals. The company ended up paying out $400 million for its alleged mishandling of the audits of four failed S&Ls.

Ernst & Young paid, in Nov 1992, the federal government a record $400 million to settle claims that the company's auditors failed to warn of disastrous financial problems that caused some of the nation's biggest thrift failures.

Ernst & Young was the auditor at institutions involved in some of the most publicized and costly savings and loan association collapses, including Lincoln Savings & Loan of Irvine, California; Silverado Banking Savings and Loan of Denver; Vernon Savings of Dallas, and Western Savings of Phoenix.

But the aforesaid unprecedented Ernst & Young payment to the government focused on a special issue, the appropriate behaviour of professional accountants whose clients became enmeshed in the financial scandals of the past decade that brought down hundreds of thrifts and banks.

Federal financial regulators claimed that many accountants ignored laws and rules as well as ethical standards in their work at the failed thrifts and banks. Ernst & Young audited more than 300 banks and thrifts during the 1980s, and 40 failed institutions were the subject of close scrutiny by government investigators.

The charges against Ernst & Young included failure to make adequate allowances for loan losses, improper accounting for mergers, improper counting of income from phony sales, and failure to disclose dubious deals between the S&Ls and some major customers. At Lincoln, for example, Ernst & Young "failed to challenge Lincoln's fictitious sales of real estate, which were used to inflate Lincoln's profits," according to the OTS.

PNC FINANCIAL SERVICE CASE

Name of the Firm	**Ernst & Young**
Nature of Allegation	Issuance of materially false and misleading statements.
Sued by	Pomerantz Haudek Block Grossman & Gross LLP
Amount of penalty or compensation paid	
Source	www.pomerantzlaw.com & SEC Press Release 18.07.2002

Facts: Pomerantz Haudek Block Grossman & Gross LLP (www.pomerantzlaw.com) has filed a class action lawsuit against PNC Financial Services Group, Inc. ("PNC" or the "Company") (NYSE: PNC), on behalf of all those persons or entities who purchased the securities of PNC during the period between May 15, 2001 and January 28, 2002, inclusive (the "Class Period"). The case was filed in the United States District Court for the Western District of Pennsylvania. The Complaint alleges that PNC, one of the largest diversified financial services and banking institutions in the United States, three of the Company's senior officials, and Ernst & Young, an accounting firm which provided PNC with auditing and consultant work throughout the Class Period, violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 by issuing materially false and misleading statements to the market concerning PNC's earnings prospects, results and reductions in loans, which mislead investors and concealed PNC's true financial condition.

In particular, it is alleged that during the Class Period, defendants failed to recognize the impairment of certain loans or charges related to PNC, and instead shifted these problem loans off PNC's books and into three separate investment entities created by the American International Group ("AIG") for the sole purpose of receiving such loans during each of the quarters during the Class Period. As a result, defendants misrepresented PNC's earnings as well as the Company's ability to reduce its liabilities related to non-performing assets. In fact, defendants' failure to conform to Generally Accepted Accounting Standards ("GAAP") produced inflated earnings and misled investors as to PNC's true financial condition.

The complaint further alleged that while acting as auditor and a consultant for PNC, Ernst & Young was also acting as a consultant for AIG. In fact, as PNC's auditor, Ernst & Young approved PNC's transactions with AIG and issued a written statement approving the accounting for them.

On January 29, 2002, PNC announced that the Federal Reserve Board ("FRB") had demanded that the Company consolidate its financial results with the investment entities created by AIG, effectively requiring the Company to reflect the true nature of these loans. In addition, the Company announced that the FRB and the Securities and Exchange Commission ("SEC")

were making inquiries about PNC's transactions. As a result of the FRB's actions, PNC was compelled to reduce its 2001 net income by approximately $155 million. In addition, the Company further announced that it will revise fourth quarter 2001 results and restate earnings for the second and third quarters of 2001.

Final outcome of after the investigations, SEC Ordered PNC to Cease and Desist From Violating Antifraud, Reporting and Record-Keeping Provisions of Federal Securities Laws The Commission's investigation is continuing as to others.

PEOPLESOFT CASE

Name of the firm	Ernst & Young
Nature of allegation	Independence compromised due to a partnership with a client
Investigator	SEC
Amount of penalty or compensation paid	Possible ban on bringing new publicly traded companies for 6 months
Source	New York Times-21.05.02, Accounting web-29.05.03, SEC Litigation release 13.11.02

Facts: Concerned about the erosion of auditor independence, securities regulators sued Ernst & Young accusing the firm of violating ethics rules by having a seven-year business partnership with a client, PeopleSoft.

In a complaint filed by the Securities and Exchange Commission, government lawyers said that while Ernst & Young was auditing PeopleSoft, a maker of computer software, the firm's tax department and PeopleSoft jointly developed and marketed a computer program to help clients manage payroll and tax withholding for overseas employees. As part of the joint venture, Ernst & Young agreed to pay PeopleSoft royalties of 15 percent to 30 percent from each sale of the program. The firm also earned "hundreds of millions of dollars in consulting revenues" from its sale of the software to clients, the complaint said.

Ernst & Young issued a statement saying it was "surprised and disappointed" by the complaint and vowed to fight the accusations before an administrative law judge.

"We did carefully consider the potential independence implications of our consultants' actions before they undertook them," said Leslie Zucke, a spokesman for the firm. "We correctly concluded at the time that the actions were permissible under the profession's rules and that they were commonplace. Therefore, we are confident that our conduct was entirely appropriate, and we will defend ourselves vigorously."

Mr. Zucke said the relationship had not created any errors on PeopleSoft's financial statements, which SEC officials acknowledged. Mr. Zucke described the issues raised by the complaint as "purely technical" and out of date. PeopleSoft is no longer a client of Ernst & Young, the licensing arrangements between the two companies are no longer in effect, and Ernst & Young sold its consulting business to Cap Gemini two years ago.

But government officials said that the violations were serious because they compromised the independence of the auditors.

"The accountants are gatekeepers and are essential to the integrity of the system," said Paul Berger, a lawyer in the enforcement division of the SEC. "When they engage in joint ventures with clients, the entire audit process is subverted." Stephen M. Cutler, the enforcement director of the agency, said that the violation was significant and that it did not matter that the relationship had not led to errors on the financial statements that Ernst had audited. "When an

auditor enters into a joint business relationship to generate revenue, its independence is fundamentally impaired," he said.

Officials said the SEC was calling for the firm to give back audit fees, which amounted to less than $1 million a year for the licensing period. If Ernst & Young is found to have violated the independence rules, it could receive sanctions ranging from censure to disbarment from performing work for companies that make filings with the commission.

This lawsuit against Ernst & Young is the second time in recent years that the S.E.C. has accused it of violating auditor independence rules. In 1991, Ernst & Young was sued by the agency over business dealings that its partners had with the Republic bank Corporation, a former Texas banking company, and the Cullum Companies, a supermarket chain. That case settled in 1995, with Ernst consenting to a final order under which it agreed to comply with the auditor independence rules. Ernst & Young is currently fighting SEC charges that it violated conflict of interest rules when it developed and marketed accounting software with PeopleSoft Inc., which at the time was also an audit client of Ernst & Young. The company settled similar allegations several years ago. At the time the company promised to follow the rules. If the latest charges prove true, Ernst & Young could be barred from auditing companies listed on the stock markets.

BANK OF CANTONALE

Name of the firm	Ernst & Young
Nature of allegation	Failure to evaluate the risk from 1994 onwards
Sued by	State of Geneva, Switzerland
Amount of penalty or compensation paid/sued	$ 2.2 b
Source	Accounting web-04.03.03

Facts: The trend of sueing accounting firms extended to other parts of Europe, this time in Switzerland. Aided by the results of a year-long study performed by PricewaterhouseCoopers, the Swiss state of Geneva has demanded 3 billion Swiss francs (US$2.2 billion) from Big Four firm Ernst & Young for damages from audits stemming from 1994 to the present.

According to the PwC report, E&Y used a method of risk evaluation that was "outside legal norms" when issuing statements concerning the merger of audit client Banque Cantonale de Geneve with another bank.

The report claimed that E&Y made insufficient provision for risks associated with the merger and continued to certify statements each year that failed to reflect the actual financial condition of the bank.

Bank Cantonale de Geneve was bailed out in 2000 by the state of Geneva. Geneva authorities claimed E&Y deviated from generally accepted accounting principles in their certification of the bank's financial statements. "These acts caused the state damage of more than three billion francs, which it is reclaiming from Ernst & Young," read a statement issued by the state.

A similar investigation is pending into the audits of another regional Swiss bank, Banque Cantonale Vaudoise. E&Y is also the auditor of that bank.

JOHN J.SULLIVAN JR'S ESTATE CASE

Name of the firm	Ernst & Young
Nature of allegation	Miscalculation of potential estate tax
Sued by	Beneficiaries and Trustees of John J Sullivan's estate
Amount of penalty or compensation paid/sued	
Source	Accounting web-21.03.03

Facts: Big Four firm Ernst & Young faces a court battle in the Circuit Court of Jackson County, Missouri, where beneficiaries and trustees of an estate claim the firm cost them millions due to a miscalculation of potential estate tax.

At issue in the estate of the late Kansas City banker John J. Sullivan Jr. is the valuation of bank stock owned by the decedent. The estate was valued at approximately $23 million at the time of Mr. Sullivan's death in 1999. Nearly 80% of the estate was in Mercantile Bank stock.

Ernst & Young and the estate's law firm, Elder & Disability, advised estate trustees to hold the Mercantile Bank stock for six months after Mr. Sullivan's death and then sell, thus enabling the stock to qualify for an alternate valuation date for purposes of determining the value of the estate. Approximately 2/3 of the Mercantile Bank stock was held in the estate and not sold right away in order to take advantage of the alternate valuation date.

The purpose of the alternate valuation date is to protect estates from a sharp decline in the value of estate holdings. If the stock drops considerably in value after the date of death, instead of using the stepped up basis for valuing the stock as of the date of death, the stock can be valued at its market value six months after the date of death.

By using the lower value for the stock, the estate can pay less in estate taxes than it would by using the value at the time of death.

This was the plan in the case of Mr. Sullivan's estate. Unfortunately, while the stock did as expected and dropped in value from $28.37 per share in November 1999 to $17.50 per share in March 2000, E&Y advised the estate's trustees that the stock did not qualify under the alternate valuation date rule and thus estate taxes would have to be paid using the stock value at the time of death. Meanwhile, the stock had decreased in value so that when it was sold there was much less money available to pay the estate taxes and the residual amount distributed to heirs was depleted.

E&Y and the Elder & Disability law affirm both deny any wrongdoing in the case. E&Y claims the trustees lost money from investment decisions they made.

BAAN COMPANY CASE

Name of the firm	Ernst & Young
Nature of allegation	Violation of Auditor's Independence
Charged by	SEC
Amount of penalty or compensation paid/sued	$400,000 civil penalty
Source	SEC Press Release 27.06.2002

Facts: In the first-ever auditor independence case against a foreign audit firm, the Securities and Exchange Commission today brought a settled enforcement action against Moret Ernst & Young Accountants ("Moret"), a Dutch accounting firm now known as Ernst & Young Accountants. The case arises from Moret's joint business relationships with an audit client. In today's order, the SEC censured Moret for engaging in "improper professional conduct" within the meaning of Rule 102(e) of the SEC's Rules of Practice, and ordered Moret to comply with certain remedial undertakings, including the payment of a $400,000 civil penalty. This is the first time that the SEC has ordered any audit firm to pay a civil penalty for an auditor independence violation. Moret consented to the order without admitting or denying the SEC's findings.

As described in the SEC's order, Moret audited the 1995, 1996, and 1997 financial statements of

Baan Company, N.V., a business software company headquartered in the Netherlands, whose stock at the time was quoted on the Nasdaq National Market. During this period, according to the SEC, consultants affiliated with Moret had joint business relationships with Baan that impaired Moret's independence as auditor. Most of these joint business relationships were established to allow Moret consultants to assist Baan in implementing its software products for third parties. The joint business relationships included a Dutch government-subsidized project for Moret and Baan to jointly develop faster software implementation tools; an agreement to coordinate global efforts in implementing Baan software products for third parties; joint marketing activities emphasizing the "partnership" and overall coordination between Baan and Moret in the implementation of Baan software products; and Baan's use of Moret consultants as subcontractors and temporary employees in servicing Baan's clients. Altogether, the SEC found that Moret consultants billed Baan approximately $1.9 million from these improper joint business relationships during the years in question. According to the SEC's order, Baan disputed, and ultimately did not pay, approximately $328,000 of these billings, which further impaired Moret's independence as auditor.

The SEC also found that, when Moret audited Baan's 1997 fiscal year financial statements, Moret improperly used and relied on audit work performed by its affiliated firm in the United States, Ernst & Young LLP. At the time, according to the SEC, Ernst & Young also lacked independence from Baan due to joint business relationships it had with Baan. As described in the SEC's order, the work performed by Ernst & Young was purported to be "internal audit" work relating to Baan's U.S. subsidiary, but in fact resulted in Ernst & Young's significant participation in the year-end external audit being conducted by Moret. For example, the SEC found that Ernst & Young performed extensive procedures in the areas of revenue recognition and accounts receivable, which were used and relied upon by Moret in conducting its external audit of Baan. The SEC further found that Moret cited Ernst & Young's work repeatedly in its audit working papers, and used that work to confirm the accuracy and appropriate scope of similar work being contemporaneously performed by a small accounting firm in California that had been engaged as the external auditor for Baan's U.S. subsidiary. Finally, the SEC found that because Ernst & Young lacked independence from Baan, Moret's independence was impaired when its used and relied upon Ernst & Young's audit procedures in connection with the audit of Baan's 1997 fiscal year financial statements.

Based on these findings, the SEC concluded that Moret's conduct constituted an extreme departure from the standards of ordinary care that resulted in violations of the auditor independence requirements imposed by the SEC's rules and by generally accepted auditing standards. In addition to censuring Moret, the SEC ordered Moret to comply with a number of remedial undertakings, including the payment of $400,000 civil penalty.

CASES INVOLVING ARTHUR ANDERSEN

The following cases cited against Arthur Andersen, will once again shatter the myth & awe of the multinational accounting firms. In fact, after the failure of Enron, some of the erstwhile partners admitted compromising position the firm took over the years in respect of its money spinning clients. To cite an example, Ms Barbara Ley Toffler in her book Final Accounting: Ambition, Greed, and the Fall

of Arthur Andersen, narrates how a culture of arrogance and greed led to the downfall of the 88-year-old accounting firm. Ms.Toffler tells her tale from an insider's perspective. She was the founder and partner-in-charge of Andersen's Ethics and Responsible Business Practices Consulting Service from 1995 to 1999.

Ms. Toffler offers insights into what went wrong at Andersen. She tells how employees became "Androids," and how "everyone followed the rules and the leader." She writes that there was considerably pressure for consultants to sell as many services as possibly and to "bill our brains out." She was even encouraged to overcharge clients.

Ms. Toffler admits that she went along with the firm's demands because she liked the money. But eventually she began to believe the company was spinning out of control. In 1998, one year before she resigned, Ms. Toffler helped form a risk-management committee, which issued a memo, advising employees to perform tougher audits. (Accounting Web 03.03.03)

Another facet of Andersen's attitude towards subversion of the law of land could be found in the report of US senate's joint committee on taxation, where in cited about the harmful tax practices adopted by Enron which were designed by leading Wall Street firms including Bankers Trust (now Deutsche Bank), Chase Manhattan (now part of J.P. Morgan Chase & Co., Inc.), and signed off on by accountants at Arthur Andersen and Deloitte & Touche and lawyers at Vinson & Elkins, Shearman & Sterling, King & Spalding, and Akin Gump Strauss Hauer & Feld.

Enron paid millions of dollars for opinion letters prepared by the lawyers and accountants, attesting to the legality and legitimacy of the shelters. Before going under, Enron created 881 offshore subsidiaries as part of its strategy to shelter tax dollars. (Accounting web 18.02.03)

THE SUNBEAM CASE

Name of the firm	**Arthur Andersen**
Nature of allegation	Sunbeam Corporation Case
Investigator	SEC
Amount of penalty or compensation paid	Partner in charge of the audit denied the privilege of appearing or practicing before the Commission as an accountant for a period 3 years.
Source	New York Times-16.05.01, SEC Litigation Release dated 27.01.2003

Facts: SEC charged that Albert J Dunlap, the former CEO of Sunbeam Corp, directed an accounting fraud in which a partner of Arthur Andersen aided him. Dunlap, best known for ruthless turnaround plans and Sunbeam's stock leaped nearly 50% the day he was hired to run the company in 1996. SEC, in the suit filed in US district court in Miami, said the Sunbeam turnaround directed by Dunlap was a sham. Sunbeam, now in bankruptcy reorganization, settled administrative proceedings filed by the SEC, accepting a cease-and-desist order barring further violations of securities law. Philip E Harlow, the Andersen partner in charge of audit of Sunbeam, was denied the privilege of appearing or practicing before the Commission as an accountant for a period 3 years. Harlow consented to the entry of the order without admitting or denying the findings therein.

THE WASTE MANAGEMENT CASE

Name of the Firm	**Arthur Andersen**
Nature of Allegation	Waste Management Inc. Case-Fiddling the books of account
Investigator	SEC
Amount of penalty or compensation paid	$ 7 million
Source	Richard Walker, US watchdog, Associated Press-John Kelley-18.01.02.

Facts: SEC alleged that the accountants filed false and misleading audits of the US firm Waste Management, North America's biggest rubbish hauler, to the extent of revenue overstatement by more than $ 1 billion. Without admitting or denying the allegation, Arthur Andersen has also agreed to an injunction that means it will face stiffer sanctions for future violations. This is SEC's first fraud case against big five accounting firm. Arthur Andersen was hoping that the payout will finally sweep the embarrassing episode under the carpet. It stated "this settlement allows the firm and its partners to close a very difficult chapter and move on". Four audit partners involved are barred from doing accounting work for public companies between one to five years. SEC has warned that it will not "shy way from pursuing accounting firms when they fail to live up to their responsibilities to ensure the integrity of the financial reporting process"

THE ENRON CASE

Name of the Firm	**Arthur Andersen**
Nature of Allegation	Enron Corporation Case-Certifying inaccurate accounts
Investigator	SEC & Congressional Investigation
Amount of penalty or compensation paid	$60 million to University of California and others & $5 million for obstruction of justice. Andersen has informed the Commission that it will cease practicing before the Commission by Aug. 31, 2002, unless the Commission determines another date is appropriate.
Source	Bloomberg News-13.11.2001, Associated Press-David Carpenter - 17.01.02, Associated Press-H. Josef Hebert-18.01.02, Washington Post-Peter Bahr and David S Bilzanrath-03.04.2002, Washington Post-Carrie Johnson-16.10.02 Page E 04, Washington Post-Carrie Johnson and Peter Behr-16.06.02, Find Law-legal and News commentary, Accounting Web 03.03.03 & 01.04.03 & SEC

Facts: Andersen, the world's fifth largest accounting firm, served as Enron's outside auditor for more than a decade. The company in Oct 01, 2001 has stated that its revenue had been overstated by $ 586 million over 4 ½ years, inflated shareholder equity by $ 1.2 billion because of an accounting error and further failed to consolidate results of three affiliated partnerships into its balance sheet.

The shareholder's equity was inflated by giving common stock to companies created by Enron's former CFO in exchange for notes receivable, and then improperly increased shareholder equity on its balance sheet by the value of the notes. A novice in accounting would not commit a mistake of recording equity without receiving the cash for it. Is it a mystery or deliberate action that the company violated and auditors also missed such an error and overstatement to extent of $ 1 billion? Andersen released full page ads in the national newspapers blaming Enron for the fiasco and promised to overhaul its practices. The SEC, the next day of this disclosure opened an inquiry into Enron with request for further information.

On being alerted by Enron of the SEC inquiry, Andersen partners launched a wholesale destruction of documents at Andersen's office in Houston, Texas, instead of preserving the same for SEC's inspection. Andersen staffs were instructed to stay overtime to complete the destruction. The shredding equipment at

Andersen's office at the Enron building was used virtually constantly and to handle the overload, dozens of large trunks filled with Enron documents were also sent to Andersen's main Houston Office to be shredded. A systematic effort was also undertaken and carried out to purge the computer hard-drives and e mail system of Enron related files. Apart from the destruction of documents at Houston office, instructions were also given to other offices in Portland, Oregon, Chicago, Illinois and London to destroy the Enron related documents. On 8.11.2001, SEC served Andersen with anticipated subpoena relating to its work for Enron. In response, members of the Andersen team on the Enron audit were alerted finally that there could not be any further shredding because the firm has been officially served the subpoena. Andersen all along maintained that shredding was according to its internal policies and it had not done with the intention of obstructing justice. It further stated that the moment it was subpoenaed it stopped the shredding in order to co-operate with the investigators.

For the above acts, Andersen was charged with obstruction of justice on the following grounds. On or about and between October 10, 2001 and November 9, 2001 within the southern district of Texas and elsewhere, including Chicago, Illinois, Portland, Oregon and London, Andersen, through its partners and others, did knowingly, intentionally and corruptly persuade and attempt to persuade other persons with intent to cause and induce such persons to (a) withhold records, documents and other objects from official proceedings, namely regulatory, criminal and investigations, and (b) alter, destroy, mutilate and conceal objects with intent to impair the objects, integrity and availability for use in such official proceedings.

When the news of destruction of documents by Andersen was out, it blamed and fired lead partner on Enron account David Duncan and three other partners who worked on the assignment were sent on leave. But the internal memos released by the audit firm indicated that its own accounting experts who challenged the methods used by Enron corp. were overruled on several occasions by the accounting firm's Enron audit team. The memos include a series of e-mails written by Carl E bass, a member of Andersen's professional Standards Group. These documents indicate the tensions between Bass's unit and Enron audit team, whose members worked day by day with Enron executives on accounting issues. Bass was removed from his oversight position last year after a compliant by a senior Enron executive. This was revealed by congressional investigators after they interviewed Bass. Duncan pleaded guilty in the trial which Andersen contends that it was done out of fear of a stiff prison sentence if he went on trial and lost. Companies numbering more than 100, that have dealt with Enron also sued Andersen, accusing it of fraud and negligence in Enron's collapse. A series of disclosures involving Andersen's role in Enron's demise has hurt the accounting giant's reputation(?) and ultimately Andersen did not survive as an accounting firm and was convicted on obstruction of justice charges, against which it has now appealed in the US 5th circuit court of appeals.

THE COLONIAL CASE

Name of the Firm	**Arthur Andersen**
Nature of Allegation	Signing overly rosy forecasts for the Colonial Realty Co's real estate venture in Hartford.
Sued by	Investors
Amount of penalty or compensation paid	$ 92.50 million
Source	Associated Press-John Kelley-18.01.02

Facts: Andersen paid $ 90 million to investors and $2.5 million to Connecticut to settle claims the company knowingly signed off on overly rosy forecasts for Colonial Realty's real estate ventures in Hartford. Connecticut state officials have stated that Andersen auditors took cash, tips and other gifts from Colonial executives. Investors lost more than $ 300 million on Colonial.

THE HOME STATE SAVINGS BANK CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Wrong certifying of accounts of the failed Home State Savings Bank
Sued by	OHIO state authorities
Amount of penalty or compensation paid	$5.5 million
Source	Associated Press-John Kelley-18.01.02

Facts: Andersen paid Ohio state $ 5.5 million to cover taxpayers' losses on insured deposits at the failed Home State Savings Bank rather than challenging the government's claim that Andersen was negligent in reviewing the thrift's books.

AMERICAN CONTINENTAL CORPORATION

Name of the Firm	Arthur Andersen
Nature of Allegation	Misrepresentation of financial health of American continental Corp
Sued by	Arizona State
Amount of penalty or compensation paid	$ 24 million
Source	Associated Press-John Kelley-18.01.02

Facts: Andersen agreed to pay a minimum of $ 24 million in settlements over alleged misrepresentation of the financial health of Arizona based American Continental Corporation and its subsidiaries, which included Charles Keating's failed Lincoln Savings and Loan.

OAKLAND RAIDERS CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Destruction of evidence
Sued by	Oakland Raiders
Amount of penalty or compensation paid	
Source	Associated Press- 27.01.02

Facts: Lawyers of Oakland Raiders have revived claims that accounting firm Arthur Andersen destroyed evidence that could call its lies in 1995 when it assured the team of sell outs at the Oakland Coliseum. Revelations that Andersen destroyed documents of bankrupt Enron and congressional investigations into the company have rekindled the interest in this case. The coliseum management hired Andersen in 1995 to track applications for 10 year personal seat licenses at Raider games. The project was the centre piece of the San Francisco Bay Area's attempts to bring the Raiders back to Oakland from Los Angeles. The football team sued in 1998 for $ 1.1 billion, claiming Raiders boss Al Davis was assured of stadium sell outs by Andersen representatives and by coliseum and city officials. Raiders management claims that perennially poor attendance at home games has crippled the team financially. The lawsuit insisted that Andersen helped coliseum officials conceal information.

HIH INSURANCE CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Failure to detect the collapse of HIH Insurance.
Sued by	Australian Government & Australian Securities and Investments Commission
Amount of penalty or compensation paid	
Source	USA Today-Andrew Backover-28.01.2002

Facts: Australian officials are investigating what responsibility Arthur Andersen will bear in the collapse of HIH Insurance. HIH filed for bankruptcy protection due to $ 2.75 billion in net liabilities in March 2001. Only months earlier, Andersen certified its books for the fiscal year ended on 30.6.2000 and it stated a net asset of $ 500 million. At HIH, three board members were former Andersen Partners and two had been on the audit committee. HIH attempted to show profits as major parts of its business eroded. HIH did not set aside enough reserves to cover future insurance claims and overvalued some assets.

BFA CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Failure to detect fraud in the accounts of Baptist Foundation of Arizona (BFA)
Sued by	Arizona State
Amount of penalty or compensation paid	$ 217 million
Source	BBC News Online's North America Business Report-David Schepp-30.04.02

Facts: In the biggest non profit institution 'BFA's collapse, investors allege the failures of Andersen to detect fraud perpetrated by the BFA. Investors in BFA lost an estimated $ 590 million after the organization filed chapter 11 bankruptcy protection in 1999. Investigators have stated that the foundation was a scam aimed at cheating thousands of elderly investors millions of dollars. Though the firm admitted no wrongdoing, it agreed to pay $ 217 million as settlement. BFA sold investment products offering higher interest than what could be earned in banks. Unable to service the same at a higher rate, funds from new investors were used to service the old investors. Arizona authorities suspecting fraud in the schemes, ordered BFA to stop selling its products, it filed bankruptcy proceedings. Andersen was implicated a year later by the investigators for its failure to detect the fraud.

DE LOREAN CAR COMPANY CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Failure to predict the financial collapse
Punished by	UK Government
Amount of penalty or compensation paid	£21 million
Source	BBC News online-Ollie Stone-lee -3.01.02

Facts: De Lorean car company which made the wing door cars collapsed in UK, the then prime minister Margaret Thatcher was furious with Andersen for its failure to prevent the fiasco. She not only barred Andersen from working for the government but also sued Andersen for about £200 million, which was ultimately settled for £21 million. When the Labour government was returned to power under Tony Blair, the sanction was lifted.

AMERICAN TISSUE CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Aiding the American Tissue to defraud its lender to the tune of $ 300 m & Obstruction of Justice
Punished by	Case investigated by FBI
Amount of penalty or compensation paid	Possible 10 Year imprisonment to the partner involved in the audit.
Source	NY Times-11.03.03, Accounting Web 12.03.03

Facts: In yet another black mark against the defunct accounting firm of Arthur Andersen, a former senior auditor of the firm was arrested in connection with the audit of American Tissue, the nation's fourth-largest tissue maker.

Brendon McDonald, formerly of Andersen's Melville, NY office, surrendered Monday at the United States Courthouse in Central Islip, NY. He could face as much as 10 years in prison for his role in allegedly destroying documents related to the American Tissue audits.

Mr. McDonald is accused of deleting e-mail messages, shredding documents, and aiding the officers of American Tissue in defrauding lenders of as much as $300 million. American Tissue's chief executive officer and other executives were also arrested and charged with various counts of securities and bank fraud and conspiracy.

According to court documents, American Tissue inflated income and diverted money to subsidiaries in an attempt to make the company eligible to borrow additional money. In 2000 and 2001- a period during which American Tissue offered and sold $165 million of securities to investors. The company inflated American Tissue's revenues and earnings in periodic reports filed with the Commission by, among other things, improperly capitalizing expenses as assets, overvaluing the Company's inventories and creating millions of dollars in phony revenue and accounts receivable through bogus "bill and hold" sales. By engaging in this scheme, the Company was able to conceal its financial weakness and thereby induce its lenders to continue to extend commercial credit and advances based on, among other things, the Company's bogus receivables and the Company's overstated reported financial condition and operating results.

"The paper trail of phony sales transactions, bogus supporting documentation and numerous accounting irregularities ended quite literally with the destruction of the falsified documents by American Tissue's auditor," said Kevin P. Donovan, an assistant director of the Federal Bureau of Investigation.

WORLD COM CASE

Name of the Firm	Arthur Andersen
Nature of Allegation	Fudging of Accounts during 2001 to the tune of $ 3 b & 2002 to the tune of $ 800 m
Investigated by	SEC
Amount of penalty or compensation paid	
Source	Accounting Web 26.06.02, SEC Litigation Release 26.11.02

Facts: Andersen has found itself at the center of an alleged $3.8 billion fraud at telecom giant WorldCom. If true, this could be the world's biggest accounting scandal to date. Chief financial officer Scott Sullivan has been fired after an internal audit discovered that transfers from operating expenses to capital accounts amounted to $3 billion in 2001 and $800 million in the first quarter of 2002. This increased cash flow and profit margins, and led to a net loss being reported as $1.4 billion profit. Without

these transfers, the company's reported EBITDA would be reduced to $6.3 billion for 2001 and $1.4 billion for first quarter 2002, and the company would have reported a net loss for 2001 and for the first quarter of 2002. WorldCom reported a profit of $1.4 billion for 2001 with the transfers.

On June 24 2002, then-auditor Andersen told WorldCom that, in light of the inappropriate transfers of line costs, Andersen's audit report on the company's financial statements for 2001 and Andersen's review of the company's financial statements for the first quarter of 2002 could not be relied upon.

The audit firm reportedly said that it was unaware of a breach in accounting rules.

KPMG - WorldCom's recently-appointed auditor - has been asked to conduct an audit of the company's financial statements for 2001 and 2002. As such, the group may well have to restate results for the past five quarters.

John Sidgmore, appointed WorldCom CEO on April 29, 2002, said that the senior management team was "shocked" by these discoveries.

Cutting capital expenditures significantly, and cutting 17,000 jobs, are moves intended to safeguard the future of the company.

Meanwhile, the SEC has asked WorldCom for a detailed account of what happened.

The following statement was issued by Arthur Andersen in response to the announcement by WorldCom. "Our work for Worldcom complied with SEC and professional standards at all times. It is of great concern that important information about line costs was withheld from Andersen auditors by the chief financial officer of Worldcom. The Worldcom CFO did not tell Andersen about the line cost transfers nor did he consult with Andersen about the accounting treatment. Upon recently learning of the transfers, Andersen conferred with the Worldcom audit committee and new management, and advised the company that Worldcom's financial statements for 2001 should not be relied upon".

The Securities and Exchange Commission announced that a judgment of permanent injunction was entered on 26.11.02, in its pending civil enforcement action against WorldCom, Inc. The Commission's investigation into matters related to WorldCom's financial fraud is continuing.

CASES INVOLVING DELOITTE & TOUCHE

ADELPHIA CASE

Name of the Firm	Deloitte & Touche
Nature of Allegation	Failure to prevent pillaging during the audit
Sued by	Client Adelphia
Amount of penalty or compensation paid	
Source	Business Line 08.11.02

Facts: Bankrupt cable television operator Adelphia Communications Corp filed a suit against Deloitte & Touche, accusing its former auditor of negligence and fraud for failing to stop the top Adelphia's executives from pillaging the company. Deloitte either knew or should have known through its audit process that the company's co-founder and former chief executive, Mr. John Rigas and two of his sons, alleged shifted funds from the company to their own pockets, the suit said. Mr. Rigas and his sons, also former Adelphia executives have been indicted on criminal fraud charges. According to the suit filed in the court of common pleas in Philadelphia, this is an action against Deloitte for professional negligence, breach of contract, fraud and other wrongful conduct arising out of

Deloitte's role in one of the most egregious instances of corporate self-dealing and financial chicanery in United States Corporate history. Had Deloitte informed Adelphia's audit committee of the Rigases' actions, "the committee could have, and would have, acted to stop and remedy the misconduct".

BARING'S PLC CASE

Name of the Firm	Deloitte & Touche & Coopers & Lybrand (C&L-now part of PriceWaterhouse Coopers)
Nature of Allegation	Frustrating the investigations in fraud
Sued by	
Amount of penalty or compensation paid	$ 50 m with Coopers
Source	Observer 28.07.02, Accounting, dishonour and a dash of bad manners-Robert A Spira & Shirley Goldstein

Facts: On 26 February 1995, amid revelations of £827 million fraud, Barings Plc collapsed. For many years it had been audited by Coopers & Lybrand (C&L - Now part of PricewaterhouseCoopers) in Singapore and also by Deloitte & Touche (D&T). The Bank of England's inquiries were frustrated. Its 1995 report said: 'We have not been permitted access to C&L Singapore's work papers ... or had the opportunity to interview their personnel. C&L Singapore has declined our request for access, stating that its obligation to respect its client confidentiality prevents it assisting us. We have not been permitted either access to the working papers of D&T or the opportunity to interview any of their personnel who performed the audit.'

Major accountancy firms have devised careful corporate structures to avoid showing their files to regulators. The governments know that despite securing 'global' appointments and fees, these firms are avoiding their responsibilities.

They could pass laws requiring auditors to show their working papers to named regulators. They could fine and shut firms obstructing fraud inquiries. Instead of exposing audit failures and increasing protection for stakeholders, governments have done nothing to call 'global' firms to account.

KENTUCKY CENTRAL LIFE INSURANCE COMPANY CASE

Name of the Firm	Deloitte & Touche
Nature of Allegation	Engaged in reckless practices
Sued by	Department of Insurance, State of Kentucky
Amount of penalty or compensation paid	$ 23 m
Source	Accounting Web 20.02.03

Facts: A lawsuit initiated in 1994 ended this week with Big Four auditor Deloitte & Touche agreeing to pay $23 million to the State of Kentucky's Department of Insurance on behalf of Kentucky Central Life Insurance Company.

Deloitte, auditor for Kentucky Central for 23 years, was accused of engaging in reckless practices that resulted in the liquidation of Kentucky Central. The firm was charged with professional recklessness regarding its audits of Kentucky Central's financial statements.

Kentucky Central collapsed in 1993 and was taken over by the State of Kentucky's Department of Insurance. At that time Kentucky Central had a deficit of $141 million. Several lawsuits were filed and about $227 million was recovered for Kentucky Centrals shareholders, policyholders, and investors.

In the company's biggest lawsuit, five former Kentucky Central officers and directors along

with Deloitte and the firm's legal counsel were sued for $200 million. Deloitte was accused of negligence that enabled Kentucky Central's directors to engage in "self-dealing and reckless practices" that resulted in the demise of the insurer. Deloitte's engagement partner endured a 29-day deposition, and nearly 3 billion pages of documents were examined in the course of the eight-year legal battle.

Kentucky Central endured losses on mortgage and real estate loans that allegedly were not included in the company's financial statements.

At one time the lawsuit against Deloitte was dismissed because it was not filed within the required statute of limitations. But in 2001 the Kentucky Court of Appeals reinstated the suit, stating that the statute didn't begin at the time of liquidation but instead began when the damages were fixed and non-speculative which, in this case, was when the Kentucky Central went into rehabilitation.

ROYAL AHOLD CASE

Name of the Firm	Deloitte & Touche
Nature of Allegation	Issuance of false and misleading financial statements
Sued by	Wolf Haldenstein Adler Freeman & Herz
Amount of penalty or compensation paid	
Source	Accounting Web-25.02.03 & 03.03.03

Facts: The New York law firm of Wolf Haldenstein Adler Freeman & Herz has filed a lawsuit against Deloitte Touche Tohmatsu claiming that the Big Four firm violated federal securities laws by aiding in the issuance of false and misleading financial statements for Dutch consumer giant, Royal Ahold, the world's third largest retailer. Deloitte is the auditor for Royal Ahold. The Wolf Haldenstein lawsuit is one of as many as a dozen legal cases already pending on behalf of Ahold investors. The lawyers are seeking class-action status for the case.

Dutch consumer giant Royal Ahold, the world's third largest retailer after Wal Mart and France's Carrefour SA, has announced an accounting irregularity in its U.S. division that amounts to at least $500 million. The company plans to restate financial statements for 2000 and 2001. The irregularities, which were discovered in the company's U.S. division, stem from local managers booking higher promotional allowances, provided by suppliers to promote their goods, than they actually received in payment. Ahold's U.S. business consists primarily of a distribution service that delivers food to restaurants, schools, and prisons. Ahold also owns the U.S. Stop & Shop chain and Giant supermarkets. Besides the company CEO and CFO, several U.S. senior executives have been suspended pending further investigation.

Dutch evening newspaper NRC Handelsblad characterized Ahold as ranking "on the list featuring companies such as Enron, Arthur Andersen and Worldcom."

NEW TEL CASE

Name of the Firm	Deloitte & Touche
Nature of Allegation	Domenic Martino, CEO of the Australian arm of Deloitte Touche Tohmatsu, may be charged for raising funds for New Tel, knowing its insolvency position
Sued by	
Amount of penalty or compensation paid	
Source	Accounting Web 31.03.03

Facts: Domenic Martino, CEO of the Australian arm of Deloitte Touche Tohmatsu, resigned last week in the wake of publicity surrounding his role as director of failed telephone company, New Tel. The possibility exists that criminal charges may be brought against Mr. Martino and other directors of New Tel if it is determined that the company's directors knew of New Tel's insolvency, possibly for as long as 12 months. Described by daily newspaper The Australian as "one of Australia's more breathtaking corporate collapses," there is speculation that New Tel raised more than A$100 million all the while knowing the company was insolvent.

Mr. Martino stated he believed an investigation into his role at New Tel will show he "properly fulfilled his duties as a director." He resigned his directorship at New Tel in February 2002. New Tel went into liquidation in December, 2002.

Lynn Odland, former Chairman of the Australian Deloitte, was appointed interim CEO while the firm looks for a permanent replacement for Mr. Martino. Since Mr. Martino's resignation from Deloitte the firm changed its policy regarding directorships in public companies, stating that now partners and employees of the accounting firm may no longer hold such directorships.

It is evident from the recital of the facts relating to individual MAFs that there is wide difference between their public image and the reality about them. It is necessary in the larger interest of the Indian business and the Indian economy and also in the interest of the Indian accounting profession that these facts are known to all stakeholders in the Indian economy.

CHAPTER IX

MAFs IN INDIA AND THE INDIAN CA PROFESSION -- A STUDY IN CONTRAST

Outside the Western Hemisphere the Indian accounting sector is the most developed and has consistently and successfully benchmarked itself with best standards and practices on composite professional requirements. It is the only national accounting talent bank which can challenge the supremacy of the west, particularly the MAFs, in this sector. Further, this is one service sector that has a great potential for exports leveraging its comparatively lower costs and excellent all round skills. The Indian Chartered Accountants, an army of about 110,000 is one of the most accomplished population of professionals in the field of accounting, auditing, bookkeeping and general business consulting. So this is one sector in which India has global competence and global potential to be globally competitive. If this national competence is weakened at home, it will be a great loss to the nation. It will also deprive the world business of the entrepreneurial instincts and skills of a highly competent and competitive accounting force, which has the potential to drive down the high cost of accounting services.

The MAFs entry into India virtually through the back door under the garb of consultancy companies and ahead of the normal calibrated schedule for opening the Indian economy followed by the government for all sectors and also ahead of the WTO schedule, has almost been like a coup and an invasion which has taken the Indian accounting profession by shock. Even before the Indian accounting profession could absorb the shock and respond, the MAFs have begun dominating the Indian consultancy market and also begun infiltrating into the audit and certification work. This has weakened the Indian accounting professional firms in their own country. This has undoubtedly eroded their capacity to emerge as a global power even as the global economy is opening up through the WTO. In fact the MAFs have succeeded in their game to weaken the Indian accounting firms at home before the western countries opened their accounting and consulting sectors to foreigners including Indians so that the Indian firms do not have the opportunity to grow at home to challenge them abroad.

It is well known that the opening of the Indian economy, which had been controlled by the State for decades before the 1990s, brings in its wake professional opportunities the experience in handling which is essential to become globally competent. This is where the MAFs struck at the Indian profession. They saw to it that the highly Indian profession did not have the opportunity to handle the new avenues of professional assignments which emerged on the opening as allowing them to handle the new assignments would mean allowing them to become an entrepreneurial power to handle such assignments at the global level. So they struck first by entering India ahead of all other economic forces of the west. They are almost successful in seizing the ground in India thereby preventing a nationally powerful Indian accounting entrepreneurship from emerging which has the potentiality to threaten them in future.

In these circumstances, it is surprising that the Indian government opened up the Consulting sector for the select set of MAFs prior to 1992,

even before the coming into force of the WTO regime. This autonomous liberalization program of the Government of India was done without consulting the most important stakeholder, ICAI, and without ensuring any reciprocal arrangement to the advantage of the Indian Chartered Accountants. Unilaterally, the Government had allowed these MAFs to set up commercial presence in India as consulting firms. And these firms are now infiltrating into other areas of the profession through devious methods. An intriguing portion of this opening up was to allow these firms to practise in corporate form and restrict their business to that of consulting, while they were in essence Accounting and Auditing firms all across the globe. This flexibility given to these firms in their form and in the nature of their business was ostensibly to circumvent the prevailing law of the land relating to regulating the Indian CA profession.

Critical questions arise on the entry of the MAFs into India considering the timing of their entry, which is premature, and the mode of their entry, which is stealthy and through the back door, and the authority that allowed the entry, which did so without consulting the most affected stake holders namely the Indian CAs. The inevitable questions which arise are:

- ★ Who authorized their entry?
- ★ How such an entry was allowed and under what terms and conditions?
- ★ What were the stipulations laid on these firms?
- ★ How these consulting companies are monitored? This remains a mystery even as on date
- ★ Whether the ICAI was informed on their entry and what was its official response?
- ★ What was the reciprocal benefit to the Indian economy and to the CA profession on their entry?
- ★ What is the amount repatriated by these firms abroad, to whom and under which head?

It is well known that the profession of accounting and auditing has co-existed with the business of consulting in India, but the only difference is that the audit profession was not a side show and a vehicle to solicit consultancy work as the MAFs do. Consequently the opening up of the consultancy sector to the MAFs has placed the multinational consulting companies, (by allowing them to carry on the business of consulting in India) in direct competition to the domestic Chartered Accountants in the field of consulting. As already stated over the last decade this has abridged the professional space for domestic CA firms, who could not avail of the opportunities which the opening up of the economy unfolded.

But more was to follow. Another dimension to this issue was that these consulting firms after the establishment of their business in India, in gross violation of the Regulations laid down by the ICAI, entered into an arrangement with certain domestic Chartered Accounting firms. As consultants and being corporate entities these firms could not render audit and attest functions, as the law of the land expressly prohibited them from rendering these services. Hence they had to resort to these "surrogate arrangements". Thus if one could name the consulting firm, one could name the Chartered Accounting firm, which rendered attest functions. This in effect meant that the position of an absence of a de jure prohibition by the Government of India on the entry of MAFs was converted by this arrangement into de facto permission.

The website of the MAFs which are just consulting firms, proudly proclaim that they do accounting, audit and assurance services though their Indian associates. The ICAI clearly stipulates that CA firms should not have any

form of association with any other non-CA firm, neither advertise nor provide assurance service in the corporate form. This arrangement has thus ensured that these firms as well as their CA associate could operate in India without any let or fear, as they do not fall within the ambit of any regulators.

Further, by engaging in crass commercialisation, these consulting firms have acted as an agent for their Accounting counterpart. By offering to provide assurance services through their associates these consulting firms have acted as a facilitator for the appointment of their associate audit firms. This arrangement has wide ramifications and damages the independence of the Auditors as much as it has on the principles of corporate governance. The existence of a broker however sophisticated is the middleman, in Auditor-client relationship is a matter of great concern and militates against the fundamentals of corporate law and accepted professional principles relating to independence of auditors.

The foreign consulting firms are able to advertise and canvass work for their accounting counterpart as a part of their Indian and global conglomeration. They have a logo and/ or a trademark accompanied by their 'cosmetic like' brand equity, which makes it easy to market their services in the corporate form. They bear the same names as the accounting firms, making it easy to advertise, benefiting both the consulting company and the accounting arm. And since these consulting firms are NOT Accounting firms duly registered with the ICAI or for that matter with any authority, they need not adhere to the discipline of the ICAI. The advertisements are released in the name of the consulting companies. This dual-existence, inadvertently created by the entry of these firms into India has been described by the ICAI, as mentioned earlier, in its June 2002 issue of its Journal as "a Circumvention of the Law of the Land".

While the country seemed to assure itself that it had not yet opened the Indian Accounting, Audit and Assurance services for foreign players even as on date, this arrangement of the Multinational firms has made a mockery of such positioning of the Indian establishment. It may be noted that as on date India has not yet opened for cross-border rendering of accounting services within the GATS -WTO regime. The arrangement mentioned above between the domestic firm of CA and the foreign consulting company has completely rendered the GATS negotiations in the WTO relating to the opening of the Accounting sector meaningless, as even before the accounting sector is to be formally negotiated for opening up the Multinational Accounting firms have already entered India and set up their commercial presence. This has actually collapsed the structure and distorted the level playing field within the profession within India.

Another dimension that needs to be discussed here is that there seems a conflict between the definition of accounting services as defined under the domestic legislation in India and that of the GATS-WTO regime. The state of affairs in the Accounting sector in India which is heavily loaded against the India CA firms, may be summed up as follows:

- ★ The opening up of the Accounting sector through the consulting route without any reciprocal benefits to the domestic CA firms has gravely prejudiced their interests
- ★ The entry of the firms ahead of the WTO schedule has jeopardized the negotiating space for India in the on going GATS negotiations
- ★ Their presence in corporate form competing with the domestic CA firms in significant

areas of practice relating to management consulting distorts the level playing field

- ★ The definition of the accounting services within the domestic legislation is significantly different from that within the GATS-WTO regime. This anomaly needs to be addressed.
- ★ Their exclusive association with certain domestic firms and thereby rendering of Accounting and assurance services circumvents the law of the land and the well intended Regulations of the ICAI
- ★ The premature entry and this arrangement of the multinational firms, who carry on their activities as a business entity, has set out an unequal war between them and the domestic firms who carry on their activities as a professional firm. This is neither in national interests nor in the interest of the domestic CA firms
- ★ The crass commercialisation of the consulting arm, which also doubles up as a facilitator for the audit arm, mocks at the concept of the independence of auditors
- ★ The unrestricted commercial presence allowed to these Multinational Accounting Firms, based on their organization and financial strength, endangers the survival of the domestic service providers.
- ★ This dwindling of opportunity resulted in the migration of student talent from the profession of accounting-audit-bookkeeping to other profession considered lucrative. This has given a body blow to the one of the most advanced professions within the country.

It is obvious that the Indian CA firms suffer from lack of level playing field in more than one sense. This has hampered their growth; their confidence; their potential to emerge as a global power. So there is urgent need to address these issues. It is to highlight the need to address these issues and to help the profession of accounting in India to avoid and escape the distortions which are plaguing the MAFs who represent the commanding heights of the western accounting profession.

THEY ARE ON THE RUN IN THEIR OWN TURF

As already explained in detail, due to the spate of financial sector scams world over, the MAFs who were regarded as the moral policeman of the business class, have come under close scrutiny by governments, regulatory, pro bono publico, and the media for the past couple of years. Even the Wall Street Journal and The Economist magazine which have been the cheer leaders of the MAFs not in the very distant past have already pronounced the verdict that the reputation of accounting-audit professionals has been tarnished, and tarnished beyond repair if one may add. It is a contrast as it was the media that essentially built up the image of the MAFs. Their industry is under the scrutiny of the lawmakers in the US. The grave charge against them is that they, because of their extraneous and unethical nexus, and compulsions of their global alliance, consistently and deliberately failed to give a true and correct picture of accounts to the millions of investors who take their word as gospel. They as professionals have failed in the sublime test of maintaining the highest levels of ethics and independence at the altar of greed, money and self-interest.

Keeping a lid on the conflict of interest arising from being connected with investment banking firms which do extensive and lucrative business with the listed companies, an MAF have acted in many cases as a conduit and becomes a cheerleader for those firms by dragging the value of the stocks to unjustified levels so that both the investment bankers and the company and in-turn these audit professionals can make money on the sly profiting from the bullish propaganda.

As already explained in detail, with their innovative accounting letting down the corporates, the conduct of the auditing and accounting Big Five (Anderson, Deloitte & Touche, Ernst & Young, KPMG and PriceWaterhouseCoopers) has become suspect in the eyes of the public and discerning professionals. For, the question uppermost in everyone's minds -- wherever these know-alls spread their tentacles -- is: How could it be possible to throw dust in the investors' eyes with such impunity and temerity without a measure of complicity, connivance and collusion on the part of auditing heavyweights looking into the accounts of companies concerned?

The western governments, especially the US has turned the heat on these firms. The senate and SEC have initiated numerous investigations into harmful practices followed by these firms. A recent report of the accounting web as on 25.04.03 states that the U.S. Senate Permanent Subcommittee on Investigations has launched an investigation into the potentially abusive tax shelter schemes marketed and sold by Big Four firms Ernst & Young and KPMG. The agency has requested documents from the firms relating to the shelters.

The investigation follows on the tails of a similar investigation into the validity of tax shelters being conducted by the Internal Revenue Service. In addition, both KPMG and E&Y are facing lawsuits from clients who have participated in shelters that have been found by the IRS to be illegal tax evasion strategies.

The Senate subcommittee claims the two firms have participated in schemes to help hundreds of companies and individuals avoid paying income taxes through their participation in improper tax shelters. A spokesman from E&Y indicated that the firm is cooperating with the Senate subcommittee, while KPMG refused comment about the investigation.

The Permanent Subcommittee on Investigations has a broad jurisdictional mandate to investigate government operations and national security issues as well as matters relating to the efficiency and economy of operations in all branches of the U.S. government. The agency's colorful past included the anti-communist investigations of the 1950s performed under the leadership of then Subcommittee Chairman Senator Joseph R. McCarthy and the 1960s hearings on racketeering headed up by Subcommittee Chief Counsel Robert F. Kennedy.

Not to be left behind in the race to eliminate the harmful accounting practices, the public interest organizations have also taken initiative in this regard. As per a report appeared in the accounting web as 30.04.03, the American Federation of Labor/Congress of Industrial Organizations (AFL-CIO) is urging Sprint shareholders to vote against the continued appointment of Big Four firm Ernst & Young as Sprint's auditor. The AFL-CIO effort is part of a large movement nationwide to encourage shareholders to demand more corporate accountability.

In the case of Sprint, union advisors suggest that Ernst & Young's relationship with Sprint management constituted an "egregious conflict of interest." AFL-CIO Secretary Treasurer Richard Trumka pointed out the fact that E&Y received more in fees from Sprint managers for tax shelter advice the firm earned in audit revenue from Sprint in 2000. In addition, Sprint paid E&Y more for non-auditing services than for auditing. "Sprint allowed Ernst & Young to cross the line, and we are now calling on shareholders to respond," said Mr. Trumka.

Sprint's former president and chief operating officer, Ronald T. LeMay, was removed from office earlier this year for his participation in a personal tax shelter in which he avoid paying taxes on more than $100 million in income.

William T. Esrey, Sprint's former chairman, resigned over issues relating to his participation in the same tax shelter. Mr. Esrey used the tax shelter to postpone income taxes on $159 million in profits from stock options during 1998, 1999, and 2000.

The Internal Revenue Service is investigating the shelter in which Messrs. LeMay and Esrey participated. "Ernst & Young played the well-documented role of tax avoidance advocate for management," said Mr. Trumka in calling for the shareholders to oust E&Y.

CHAPTER X:

AN ILLUSTRATION OF THE PUBLIC OUTCRY AGAISNT THE MAFs IN THE WEST, AS CONTRASTED WITH HOW THEY ARE CELEBRATED IN INDIA

In India, with total ignorance of the harmful practices of the MAFs, we hold them in high pedestal, blissfully oblivious of these facts. Produced here below are two samples of public outcry the MAFs in the US.

First: An Open Letter to the "Big 4" Audit Firms By William K. Black

Who is Mr William Black? William K. Black Assistant Professor, LBJ School of Public Affairs UniversityofTexasatAustinVisiting Scholar, Markkula Center for Applied Ethics Santa Clara UniversityContact Information: O: 408/551-6025 bblack@scu.edu H: 650/593-5921 SNLDEBACLE@ATTBI.COM

This is how Mr Black describes himself.

I was litigation director of the Federal Home Loan Bank Board and Senior Deputy Chief Counsel for Enforcement and Litigation of its successor agency, the Office of Thrift Supervision, during the S&L debacle. I teach courses in microeconomics, advanced topics in public financial management and regulation, and White-collar crime. My J.D. is from the University of Michigan (1976) and my Ph.D. in Criminology is from the University of California at Irvine (1998). My areas of specialization include White-collar crime, financial regulation and corporate governance.

This is what Mr Black has written about the MAFs in the wake of the accounting scandals beginning from Enron which rocked the world and made the MAFs, as Mr Black says, naked.

Here's some free advice from a lawyer who sued auditors for a living: You folks are making it too easy. My regulatory colleagues and I collected hundreds of millions of dollars in damages from you for the taxpayers during from the S&L debacle. You obviously learned no useful lessons from that experience. Don't tempt me to leave academia and take up my former calling.

Your latest move has been to try to prevent John Biggs, the highly regarded head of one of the largest pension funds in the world from being named to run the newly created accounting oversight body. Your concern is that he will be too vigorous a supervisor. But nothing could be better for the accounting profession than the appointment of a vigorous supervisor known for his toughness and integrity.

Your failure to vigorously police yourselves is what got you into your current predicament. You had the greatest deal any accountants in the world ever had - you got to regulate yourself in the richest nation in history in a financial system that mandated that every publicly traded company hire an external auditor. You have now aided so many CEOs in looting "their" firms that you have succeeded in getting yourself expelled from this financial Eden.

I won't preach at you about the public interest and what the "P" in "CPA" is supposed to stand for. I'll limit my advice to your naked self-interest. You may have noticed a missing chair at the table in your club. Arthur Andersen (AA), perhaps the proudest of the one-time "Big 8" is no more.

I know you blame the Justice Department for AA's demise. If only AA had not been prosecuted so successfully perhaps it would still be in business giving clean opinions to the top control frauds (frauds by controlling persons).

Here's what you need to hear: AA committed suicide; the Justice Department did not kill it. AA killed itself by ignoring all the advice its own for-hire consultants would have given their clients on how to manage a company.

AA was one of three of the then-Big 8 firms that paid many scores of millions of dollars of damages as a result of the S&L debacle. It did extraordinarily bad things on behalf of Charles Keating's Lincoln Savings in both its roles as a consultant and auditor. (As consultant, it prepared, years after the fact, documents that were stuffed into Lincoln's loan files so they would look like contemporaneous underwriting. The purpose was to deceive the federal examiners and disguise the fraud.) We got hundreds of millions in damages from AA and its peers arising from the debacle.

The way that AA and its peers reacted to the S&L debacle was suicidal. Virtually all of the energy went into trying to avoid being sued - not by curing the deficiencies that led to the suits, but through "tort reform" designed to make it far harder and less attractive to sue audit firms. There was zero recognition that clean opinions from Big 8 firms for well over 100 control frauds - even though they were deeply insolvent and engaged in massive accounting irregularities - might indicate that the system was broken.

Instead of reforming, the top audit firms made things worse. The pressures on audit partners to bring in high-fee clients and push consulting services have intensified.

You could have prevented many of the current financial scandals and the resultant trashing of the world financial markets. Indeed, all the scams that have come to light at this time, just like all the S&L scams, were easy calls as a matter of accounting. Every accountant, internal and external, who worked on the Enron partnerships, the broadband swaps and the capitalizing of expenses at WorldCom, for example, knew that the sole purpose of the transactions was financial alchemy. Of course, you can't admit that publicly because you would be admitting that you should be liable for billions of dollars of damages.

So what should you do now? Here's the proverbial bottom line: Weak regulation hurts not simply investors but the most reputable members of your profession. So let's hear from that wing of the profession. How many of you support Mr. Biggs?

Second: Berardino, the former CEO of Arthur Anderson warns the MAFs of smugness

Former Andersen chief executive told an American Institute of Certified Public Acountants conference in Phoenix that he was "humbled" by the loss of his firm - and sounded a warning about the attitude of the remaining Big Four firms.

"I come before you in humility, humbled by the loss of my firm," Berardino told the gathering. Having talked to leaders in the other global accountancy firms, Berardino said they thought what had happened to Andersen could not happen to them.

"Talk to me a year ago and I would have said the same thing," he said.

The potential for prejudicing evidence in outstanding civil suits prevented Berardino from going into specifics about what happened at Andersen. But his talk showed that corporate governance and financial reporting had dominated his thoughts since his old firm disappeared.

According to our sister site Accountingweb.com, Berardino identified five underlying factors in the US business environment that contributed to the current crisis of confidence:

- ★ More and more Americans are investing in the stock market through pension schemes and mutual funds that expose them to effects of Enron-style corporate collapses.
- ★ Executive pay has become linked to performance, so bottom line figures determine how executives are rewarded.
- ★ Media coverage of quarterly announcements has given corporate performance reporting a higher profile.
- ★ Hedge funds have expanded the opportunities for companies to take financial risks.

These factors have increased the potential for conflicts of interest to arise during reporting and auditing, and made them more visible, Berardino said. To cater for this level of interest, he recommended the introduction of "graded" audit opinions to provide better quality assurance.

While this proposal has not featured highly on the agenda for reform in the UK, the ICAEW and other bodies would welcome Berardino's support for a move away from rules-based accounting to a principles-based model.

"We can help prevent business failures," he said. "And we must increase our ability to detect fraud."

SOURCE: AccountingWEB 14-Nov-2002

Association for Accounting and Business Affairs and other MAF watch groups

Apart from the above conscientious individual sentinels, many MAF watch groups are studying and creating awareness against the harmful practices of the MAFs. One such group, about which reference has already been made, is 'Association for Accountancy & Business Affairs (AABA)', based in UK an independent non profit making body. AABA is devoted to broadening public choices by facilitating critical scrutiny of the major accounting firms. This is achieved by publication of books after a considerable research. Some of the books published by this organization which highlights the harmful practices of these MAFS are 1) Dirty Business: The unchecked power of major accountancy firms. 2) No accounting for tax heavens. 3) BCCI cover up 4) No accounting for exploitation 5) Auditors: Keeping the public in the dark. The study conducted by AABA titled 'Dirty Business: The Unchecked Power of Major Accountancy Firms' has been of immeasurable help to the CAAC in preparing the White Paper. The CAAC records its deep gratitude to the authors Mr Austin Mitchell and Prem Sikka who had kindly agreed to allow the CAAC to use the information and extracts from the study also provided the digital version of the work to facilitate its use. The CAAC also expresses its gratefulness to Unison the largest trade union in UK from whose study this White Paper has drawn heavily on. The CAAC also thanks the sponsors of the website The Catsbird Seat for the valuable catalogue of information and news about the MAFs which also has been of considerable assistance to the CAAC to prepare the White Paper.

CHAPTER XI

THE ROLE OF THE GOVERNMENT, MEDIA, CORPORATES, AND ICAI AND HOW IT HAS AFFECTED THE INDIAN CA PROFESSION

PATRONAGE BY THE INDIAN GOVERNMENT AND ITS AGENCIES

Governmental patronage and actually reverential welcome to foreign consulting companies in India has been the principal drive of the agenda of the MAFs to conquer the Indian market. This patronage has been in the form of creamy assignments in planning commission, advisory role in disinvestments, advisory role in implementation new taxation structures (for example, implementation study of VAT) and advisors in Foreign Direct Investments matters etc. While the extent of patronage is immeasurable in quantitative terms, a mere look at the list of disinvestment and its advisors, demonstrably shows the distinct bias of the governments to hire foreign consulting firms.

Sl. No	Name of the PSU	Advisor (Foreign)	Advisor (Indian)
1	Air-India	JP Morgan Stanley	
2	CMC Limited	KPMG	
3	Hindustan Copper	Sumitomo Bank	IDBI
4	Hindustan Insecticide		A F Ferguson
5	Hindustan Organic Chemicals Ltd		A.F. Ferguson
6	HTL	KPMG	
7	Hindustan Zinc Limited	BNP Paribas	
8	Indian Airlines	ANZ Grindlays	IDBI
9	IBP Limited	HSBC Securities	
10	HPCL	Warburg Dillion Read	
11	ITDC	Lazard	
12	Madras Fertilizers	Bank of America	
13	National Fertilizers Limited	Rabo Finance Limited	
14	Pradeep Phosphate Limited	DTT	
15	Sponge Iron India Limited		A.F. Ferguson
16	VSNL	CS First Boston	SBI Caps
17	Bharat Heavy Plates and Vessels		S.B.Billimoria
18	Bharat Pumps and Copm		S.B.Billimoria
19	Hindustan Cable Limited		ICICI
20	Hindustan Salts		SBI Capital Markets
21	Instrumentation Limited		IDBI
22	Jesop & Co		A.F.Ferguson
23	NEPA		SBI Capital Markets
24	Scooters India	PWC	
25	Tungabhadra Steel		IDBI

Source: The February 2002 Journal of the ICAI

UNDUE PATRONAGE BY INDIAN FNANCIAL INSTITUIONS, BANKS, PUBLIC SECTOR UNDERTAKINGS & CORPORATES, AND ALSO THE MEDIA

Besides the government of India, the biggest promoters of the MAFs in India have been the public financial institutions and banks and also the public sector. There have been instances of the public financial institutions pressuring the assisted companies to engage the MAFs as auditors and consultants or as internal auditors and attesters of the corporate accounts, in some cases including statutory audit. In fact the government itself has been greatly encouraging the MAFs in the past and it continues even today.

The Indian media hyped the entry of these MAFs, as if their presence in India is a cure to all economic evils. It published the interviews of CEOs of these firms with awe and sometimes, even sidestepped the official body ICAI on matters concerning the profession. By this process the media gave these MAFs the status of official spokesperson of the accounting profession, which in fact is the sole domain of the ICAI. Indian Media conveniently ignored the much of the publicized failures of these MAFs barring a few reports here and there.

Not to be left behind by the government and the media, the corporates either individually or in the form of chambers hired these MAFs to prepare study reports about their industry. The corporates believed in the myth that if their accounts are certified by these MAFs it has recognition and acceptability worldwide. These MAFs unashamedly participated in any event that gave them the publicity, courtesy the corporates and the media. To cite a few instances, Cricket rating by the one the MAFs, Certification of the selection process in a game show conducted by a popular film artiste, etc.

THE POSITION OF THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA [ICAI]

The ICAI is not designed to handle a situation like the one which arose on the sudden and un-notified entry of the MAFs into India. Despite being apparently an independent body the ICAI is a body whose internalised culture is to function on consensus. It is not like the Bar Council of India which is based on the directly elected leader leading the profession. The 30 member ICAI council is not a body which has taken a position against the government, unlike the Bar Council which can and has taken positions even against the government. It may be said that the ICAI did not work out any elaborate strategy to face the consequences of the entry of the MAFs into India. But once the government, which is the guardian of the people of India, decided to permit the MAFs without consulting and without having regard to the consequences of the entry on the accounting profession in India the ICAI could do precious little.

The council of the ICAI is also a split and not a cohesive body. It is not a team. Its members are elected for a term of three years. The election process today does not always throw up the right kind of leadership, given the fact that the elections today have declined in quality. All this reflects on the functioning of the ICAI. The surreptitious entry of MAFs as consultancy firms has helped the foreign firms to tap the high end of the market of consultancy leaving the more respectable but less remunerative segment of Audit and Attest function to the Indian Chartered Accountant firms. Perhaps this arrangement of the Attest function being exclusively reserved for the members of the ICAI had lulled the members into a false sense of security.

One of the reasons why the ICAI could not effectively tackle the invasion of the consultancy business by the multinational accounting and

consultancy firms is that these MAFs came through the grant of license by RBI under the Foreign Exchange Regulations. But had the ICAI fought to regulate the business of consultancy by Chartered Accountants organising through a corporate and had it been regarded as an accounting function; the RBI could not have easily allowed the foreign consultancy bodies to enter India without consulting the CA institute. This is particularly because the issue of opening up of profession of accountancy for the foreign firms is normally a matter of reciprocity between the CA bodies of the concerned countries or based on the negotiations and commitments arising between different countries.

This failure of the ICAI is one of the causes for the entry of foreign firms into India to set up office for consulting business even before the profession of accountancy is opened under bilateral or multilateral agreements. Had the consulting business through corporate form of organisation been within the purview of the ICAI, the Institute would have had the locus to cite the disciplinary regulations of the Institute to contend that foreign consultants being outside the purview of the profession, their entry would create another kind of professionals, who are not subject to any regulations. This could have effectively stopped foreign CAs and their outfits entering India as consultants. With the result a high value professional area has slipped out of the hands of the Indian CAs in to the control of MAFs.

IMPACT OF THE MISPLACED PATRONAGE

Presently the "creamy layer" assignments in the form of, for example, disinvestment advisory services and management consultancy assignments of large public sector undertakings etc., are taken away from many of the Indian firms by prescribing conditions on their net worth, number of professional employees and so on, which many Indian CA firms would obviously find difficult to fulfil and which at times look like an attempt to keep the Indian firms away. This would ensure that a brilliant professional corps will not be in a position to take advantage of the opening of the services sectors under the GATS due to enforced lack of experience, and expand to its full potential.

CHAPTER XII:

WHAT SHOULD THE INDIAN CAs DO?

The most adverse impact of the entry and occupation of the Indian consultancy market by the MAFs and their infiltration into the audit and attestation segments has been the erosion in the confidence of the Indian accounting firms, and also generally in the accounting profession. This has also impacted on the authority and prestige of the ICAI as the legitimate spokesman of the accounting profession and on accounting issues. With the advent of the powerful MAFs on the Indian scene, the authority of the ICAI has faded to a great extent in different areas.

While the situation is very discouraging to the national accounting profession, the first and the foremost thing the Indian CAs should do is to realise that because of their inaction and lack of organisation not only has their collective interest been impaired but also that the national interest has suffered. So the first requirement is to organise themselves and sensitise themselves and also other stakeholders in the Indian business, and also the government and the general public. The CAAC is endeavouring to help the Indian CAs to organise themselves. This is the first step.

Second they should regain their confidence, which has been considerably eroded by the marginalising the national accounting profession and granting legitimacy to the MAFs. They can regain their confidence only if they sensitise the nation about what is happening in the accounting sector as much of what is happening is because of the ignorance of the critical decision makers in the government and in the corporate sector, besides in the establishment of the Indian accounting. But removing the ignorance is possible only by creating awareness. The very fact that the MAFs have become an issue today and the issue of level playing field is being discussed in the open is because of the awareness of the public spirited members of the profession who became active in the CAAC.

Third, the members of the profession must begin to talk and talk openly. They should not be carried away by such slogans as globalisation means opportunities for Indians outside India, and so on. They should not be scared by any one charging that they are against liberalisation or globalisation. They must be bold enough to say that globalisation and liberalisation cannot take place on the agenda framed by the interest groups in the west and on the schedule insisted upon by such vested interests.

Fourth, the Indian CAs should give up the dream that they can progress and become prosperous if the MAFs dominate the Indian market. There have been some initial hopes that the entry of MAFs will increase the employment opportunities for Indian CAs. But all this has been belied. This is no more valid than the suggestion and the hope that the entry of Coke and Pepsi would increase the employment in India! The Indian CAs must think that they have the right to dominate the Indian accounting profession not as employees but as entrepreneurs and employers. This reorientation is a pre requisite for their success.

Fifth, the Indian CAs should not feel hesitant about demanding incorporation of legal bulwarks against the profession being swamped by powerful and pretentious foreign counterparts.

Sixth, the Indian CAs also should enlist the support of different stakeholders in the Indian economy to expose the practice of foreign collaborators, funding agencies, and institutions,

such as the World Bank and the IMF imposing auditing firms nominated by them on Indian corporates.

Seventh vigorous awareness campaigns should be launched, which should expose the MAFs. The Indian corporates should be persuaded to engage only Indian consulting and auditing firms which are better placed to gauge the business and legal environment and are also less expensive, more skilled in handling issues and more rigorously trained. In sum, self-pride and courage to stand up to pressure should be the motto. For this purpose the Indian CAs should network with other professional firms, like lawyers, consultancy firms, and offer one stop service to the corporate and others. They should promote their brands by collective work and networking.

In line with the above, Indian chartered accountants should demand that:

★ No further Multinational accounting firm should be allowed to be come in and establish business whether as consulting companies or Accounting firms - This should come as an official policy announcement.

★ Pending the outcome of the negotiation of GATS within the WTO, revoke the licenses given to these firms to operate in India.

★ In the alternative the Government must ensure that those who are already here should come under restrictions like:

  i. Their services should be limited to foreign companies who have made investments in India and who are used to avail their services.

  ii. No Indian company should avail of their services unless insisted upon by their foreign investors.

★ No Indian financial institution and no Government agency should engage them except under circumstances mentioned above.

★ The Government converts the existing commercial presence of the Multinational Accounting firms into cross border presence.

★ Cross border presence should be allowed only if the domestic laws, regulations and constraints are applicable to the Foreign Service Provider in a manner that would be applicable to a domestic firm.

★ The presence of the consulting company should be deemed to be the commercial presence of the Multinational Accounting firm and thus the indirect opening up of the Accounting services within India, violating the GATS Agreement and GATS discipline.

★ The principle of "National Treatment" should be extended to the foreign arm of the commercial presence of the accounting firms in India. The same restrictions as are placed on the Indian CA firms should apply to them as well. They should give unconditional undertaking to subject themselves to local/ municipal laws / regulations.

★ The arrangement of the consulting firms with the domestic firms of Chartered Accountants should be scrutinised and wherever necessary the ICAI should initiate disciplinary proceedings against these firms. The foreign firms should not be permitted to do any attestation services.

★ They should not be allowed to enter in to any royalty or consultancy arrangement with local accounting / consultancy firms.

★ The question of repatriation of national resources by way of precious foreign exchange by these firms to their global counterpart should be comprehensively examined and remedial measures taken

against money laundering, collusive and the deals and the like.

- ★ Circumstances leading to the change of auditors in the past three or four years where the in coming auditor has been the associate of these consulting firms and the party and those privy to the violation of the concept of independence of these auditors should be investigated.
- ★ The consulting firms that have already come in should be asked to declare full details of their parentage, ownership etc.

None of these is achievable unless the Indian CAs organise themselves. They must demand that the ICAI shall act in their interest. They must sensitise the Government to understand their problems. The Indian CAs, by organising themselves, should become a force to reckon with like the Indian legal community. This is in the collective interest of the Indian accounting professionals. They must realise that their collective interest approximates to national interest. They must also network and join forces with other professionals.

Finally this is a war. This cannot be won without high national spirit and without perceiving the confluence of national interest with the collective interest of the CA profession or for that matter the collective interest of any segment of the Indian economy. The idea of globalisation as defined by the west and accepted by most of our elites and economists outlaws the idea of national interest. At least that was how, when globalisation made its appearance in India, it was articulated.

Even the accounting profession in India was guilty of viewing the idea of globalisation in the same way. But the very concept and structure of globalisation and global institutions like the WTO implies that globalisation is a competition between countries, not between individuals of one country with the individuals of another. Globalisation is collective game. Individuals and corporates of one country engage in trade and business the individuals and corporates of another country and in the engagement the governments of the two countries are their guardian and the guardian of the economic interest of the nation concerned. Thus the Indian CAs must introspect and understand this key element and organise themselves to ensure that the establishment does not disregard its interest and also that the system does not disregard the national interest.

A FINAL WORD

India comprises one sixth of humanity. Its English-knowing population is larger than the population of say UK. It is the only effective competitor to the West in intellectual areas of business, particularly those like software, e-exports and accounting and consultancy, to cite a few examples. The Indian CA community is the third largest in the world. It is increasing at a pace which is likely to take India to the second place in the next few years. Some of the best minds in the country entered this profession before the software boom began to compete with it and took away talent previously flowing to the CA community. So the Indian CA community is a potential global player and a global power. In fact India's global agenda is linked to the Indian CA profession's emergence at the global level. But a profession which has been weakened at home cannot emerge as a global player. The Indian CA profession has been weakened at home in the last decade.

The Indian CA community suffered the worst consequences of the socialist regime. Its potential could not be realised then because of the enormous pressure the system had built on the community which was considered to be the appendage of the business community which in turn was treated as an outcaste by the socialist polity. But when the country took to the path of liberalisation the CA community could not get its due share, or for that matter, any share in the opportunities which emerged, because of the invasion by the MAFs. So the Indian CA community has to realise that it has a large national role, not as employees, sub-contractors and surrogates of the MAFs but to emerge as the front line players at home as a prelude to emerging at the global level. It must realise that it has the potential. It must also realise that it is a challenge. It must also understand that like its software cousins it has the opportunity to dominate the world. But it can only do it, if it acquires the entrepreneurial mind set, experience and initiative. It cannot acquire these traits if it were to play a subordinate role to the MAFs in India.

India must act first if the world economy were to be saved from this crass commercialisation of the corporate consultancy and auditing, the two important tools of investor protection. Mere systems are incapable of achieving this. It needs a profound philosophy which does not reject material thrust, but which is not entirely driven by it. The west largely relies on systems to control human lust. This is the mainspring of its failings which are showing up. The Indian CA profession should emerge as the alternative model and not the carbon copy of the western ones. Its global responsibility is its global opportunity. It has the potential to change the global rules of the game of auditing and consultancy from being driven purely by money which is the guiding philosophy of the MAFs. It has the cultural heritage to emphasise and illustrate a larger philosophy. But it must acquire the will which it lacks a present.

It must also be stated that the Indian Government and the Indian corporate sector also have to play an effective role to ensure that the Indian CA firms which have potential to emerge as global player and even a global power are not weakened at home. The Indian Government and corporate sector are giving undue importance to the MAFs. This has a pernicious effect on the confidence of the Indian CA firms to handle the MAFs in the market. It is necessary that the Government reviews its policy and also advises its different departments, the state-controlled financial sector and the public sector undertakings not to favour the MAFs in any manner and without regard to

merit as they are doing at present in total disregard of the professional credentials of the Indian CA firms. The Indian corporate sector also should review its assumptions about the MAFs and should not blindly accept the suggestions and pressures of the MNC JV partners and the Indian state controlled financial institutions to engage the MAFs for different professional assignments. This is in the larger interest of Indian corporate sector and the financial sector; and also in the general interest of the national economy.

Nothing like this large agenda is possible without collective and national commitment in the CA community. This is the commitment the CAAC calls upon the CA community to demonstrate. It does not mean sacrifice of material aspirations or of the opportunity for success. It is actually investment to build greater opportunities for higher material aspirations and more material success. It is an investment to build intellectual moral and social capital to emerge on the top of the table. This is the agenda of the CAAC. This is its goal. "India First' is its mantra.