Companies Act: tough norms for auditors

With the government set to implement the new Companies Act, auditors may face stringent norms to operate in the country. The draft rules, released by the Ministry of Corporate Affairs on Monday to execute the new law, mandate rotation of individual auditors in five years, while that of a audit firm every 10 years.

As per the proposed rules, listed entities will have to implement the rule retrospectively and will have three years to replace auditors, who are working with them for 10 years or more.

Besides, the newly framed draft rules mandate that an incoming auditor or audit firm should not be associated with the outgoing one.

"The incoming auditor or audit firm shall not be eligible if such auditor or audit firm is associated with the outgoing auditor or audit firm under the same network of audit firms or is operating under the same trade mark or brand," the draft rules state.

Besides, the proposed rules prescribe penalty for auditors as well as audit firms if they are found involved in fraud. According to the draft rules, in case of conviction, auditors will have to refund the remuneration received by them and also pay damages to authorities as well as those affected by incorrect audit statement.

Experts say the tighter norms are because of the increasing number of corporate scams that have emerged in recent past, where auditing lapses are evident.

The proposed rules for rotation of auditors are also seen as boost for various small auditing firms and individual practitioners. However, large firms are likely to lose various clients once the rules are implement. Currently, the top auditing firms such as Pricewaterhouse, Ernst & Young and KPMG are the ones managing most leading companies.

The first set of draft rules, covering 16 of the total 29 chapters of the Act, also cover draft norms on corporate social responsibility, appointment of directors, declaration and payment of dividends and setting up of National Financial Reporting Authority.

<u>HIGHLIGHTS</u>

--Individual auditor can have a maximum term of 5 years

--An auditing firm can have a maximum term of 10 years

--In case the auditor has sufficient reason and information of fraud, he shall report the matter to the Central Government immediately but not later than thirty days of his knowledge or information.

--Incoming auditor should not be associated with the outgoing one

--certain classes of companies to appoint an internal auditor

--company can suggest rotation of auditing partner and team within the audit firm

(Business Standard)