Role of auditors and audit committees in effective corporate governance: A comparative study of US UK and India

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Abstract—**Role of auditors countries in like USA, UK and India and audit committees have come to be questioned in the public fore of discussion in recent times. Certain structural reforms have been undertaken by the respective countries such as the passing of Sarbanes-Oxley Act in the US, the Cadbury Committee reforms in UK, Naresh Chandra and Uday Kotak Committees in India with respect to corporate governance including the role played by auditors and audit committees. The researchers have tried to bring in perspectives from these three jurisdictions such as the legal framework, rights, duties and liabilities if these auditors and audit committees including the laws governing them. Questions have been sought to be answered especially from the Indian perspective as to what the current regulatory framework lacks and what the other jurisdictions have in the offer for the Indian Legal framework. The researchers have looked into the key issue of auditor independence and that whether in the existing regimes of law is he really independent? The questions regarding how important is it for the auditor to be independent from the perspective of corporate governance have been tried to be answered.**

Index Terms—**Corporate Governance**

I. Introduction

The need for reforms within the corporate governance framework across jurisdictions of the world is not new. The demands for these reforms have been raised emphatically time and again post the corporate scandals around the globe, in US; after Enron and WorldCom failures while the need was felt post Satyam case in India. These events have pressed for a public re-evaluation of the way auditors have functioned within the scheme of corporate governance. Traditionally, the role of an auditor has been ascribed to that of a "watchdog over the finances of acompany". The need is even more so, in countries like India, mostly in having companies which are promoter-controlled or owners of publicly-traded shares. The question of public-money at stake raises the gravity of the issue along with dispersed share-holding patterns amongst the public who are mostly passive and vulnerable. Also failure of large public companies, which are mostly the subject of discussion in the corporate governance regime, has large-scale repercussions amongst the public at large.[1]The failure of a company of large scale inevitably results in loss of public trust in companies. Theconcepts of the Board of Directors (management) are"trustees" of the share-holders of the public at large is well known.In this regard they owe a duty towards the share-holders to prevent "information asymmetry" between owners

[1]Madhur Singh,"India tries to save jobs after Satyam Scam,(The Time,20 Jan 2009),(http://content.time.com/time/world/article/0,8599,1872883,00.html) last accessed on 24 August,2018

and various sections of share-holders, and auditors of a Company fulfil this role. Some jurisdictions have even gone to assign and hold via judicial dictums that auditors are ultimately responsible to the shareholders.[2]While large profits can be minted taking full use of this "information asymmetry" between the owners managers of the company and the various sections of share-holders in the short-run, a clear balance of interests of all stake-holders of a company goes on to ensure long term survival and growth.[3]A high amount of trust is usually placed by share-holders on the auditors to show the true and fair view of accounts of the company. Hence the huge responsibility of performing duties with extreme care and diligence falls upon the auditors at this juncture.

Modern-company law systems across the world have been using the principle that reliability of accounts and reports increases, if there exist a system of an independent-third party system of verification of them. Existence of a temptation to cook-up and present the accounts in a manner biased in favour of management is common and likely to affect all boards of directors at some time or other, the temptation will be at its highest, when the financial position of the company will be at its ebb and stake-holders such as share-holders, creditors and investors in dire need of access to the truth. The researchers have through this article have tried to trace the need, for auditors, and the role set out by legislations particularly in the domain of corporate governance in multiple jurisdictions of India, USA and UK.Questions of whether the current regulatory frameworks across these jurisdictions offer enough for the auditor to perform his role independently as required of him, also it will be seen by the researchers that whether such regulatory mechanisms resolve the question of conflict of interest situation of an auditor. Fourthly, the question of auditor independence has to be seen.Lastly, the researchers will look into an analysis of the efficacy of auditors across these three jurisdictions and whether the auditors have failed or fulfilled their respective roles in corporate governance regimes in these jurisdictions.

II. REGULATORY FRAMEWORK GOVERNING AUDITORS IN DIFFERENT JURISDICTIONS

It would be crucial to look into the legislative and regulatory framework governing the auditors in different jurisdictions in order to understand the concepts better, and hence we proceed jurisdiction wise for the same purpose.

A. THE UNITED STATES SCENARIO:

Major legislative changes were ushered in the US Corporate governance framework post the year 2002, which the researchers have sought to focus upon. This was a period of time, when the US was battling with corporate accounting scandals of some of its biggest named companies such as one Enron, a large energy

[2] Columbia Coffee&Tea Pty Ltd. V.Churchill (1992) 29 NSWLR 141

[3]**Audit Committee Mechanism to Improve Corporate Governance: Evidence from a Developing Country MadanLalBhasin**Bang College of Business, KIMEP University, Almaty, Republic of Kazakhstan p.856

company; where complicated derivative transactions, were used to boost not only revenues of the company but also profits. Hand-in-glove with the managers of the company were also the auditors, a large auditing firm named Arthur Anderson. Both the managers as well as the individual auditors were subsequently convicted in what turned out to be greatest corporate failures US had to witness in recent times. Another was the failure of WorldCom, a well-known telecom giant, who also was plagued by fraud committed by its CEO, including filing false documents with the American Securities and Exchange Commission.So,post such debacles, US enacted the Sarbanes-Oxley Act,2002.Key elements of this Act, worth mentioning are establishment of Public Company Accounting Oversight Board, to provide for independent oversight of public accounting firms (known as "auditors"),special emphasis was placed on "auditor independence", to limit conflict of interest. The Securities and Exchange Commission of the US has put in place certain rules to take the Act into effect in this perspective.[4]Senior Executives liability was fixated on the individual, for the accuracy and completeness of the financial statements.Another key provision which has been introduced is criminal penalty for manipulation, destruction or alteration or destruction of certain financial records of these companies .Certain specific provisions such as Section 303 of the Act have imposed civil as well as criminal liability on the persons trying to exercise improper influence on the conduct of audits, which includes influencing, coercing or misleading any chartered accountants engaged in auditing services.

Section 401 of the Act, of the Act, requires the disclosure of "off-balance sheet-terms", an instrument which is used for reporting financial position.

Section 404,is the most contentious part of the Act, which requires management and the external auditor to report on the adequacy of the company's internal control on financial reporting, a provision which is also imported within the Company Law Framework. This is a costly aspect of the legislation for companies to implement, as documenting and testing important financial manual and automated controls requires enormous effort.

Under the Sarbanes-Oxley Act, the "audit committee is directly responsible for the appointment, compensation, retention and oversight" of the statutory auditor and each statutory auditor must also directly report to the audit committee.

A similar provision of that sort, exists within the Indian Company lawframework, wherein the audit committees has been tasked with oversight functions and liasoning between what the external auditors and the management has to say.

B. THE UNITED KINGDOM SCENARIO

[4] Sarbanes-Oxley Rule making and Reports, (US Securities and Exchange Commission,25 June 2018),(http://www.sec.gov/spotlight/sarbanes-oxley.htm) last accessed on 24 August,2018

The UK Companies Act of 2006 provides for establishment of an audit committee for private companies and public companies except those companies which donot require audit committee requirement. The Cadbury Committee, a famous corporate governance reviewing committee of the UK,in its code for best practices, "The board should establish an audit committee consisting of three Non-Executive Directors with written of reference which deals with clear with its authority and duties". The Committee was formed in response to several high profile scandals in UK such as PollyPeck,BCCI cases.

Also, the Corporate Governance Code of UK provides that listed company boards in UK, should establish an audit committee of at least three person, for every listed companies, in case of smaller companies two, independent, on-executive directors.[5]

The new UK Corporate Governance Code of 2016 has provided for certain key changes, such as rather than relying solely on the work of the external auditor, must satisfy itself that the sources of assurance and information it has used to carry out its roles to review monitor and provide assurance or recommendations to the board are sufficient and objective.

The audit committee has been mandated to ensure that the internal auditor has a reporting line that enables it to be independent of the executive and so as to exercise its independent judgement. The audit committee has also been mandated to ensure that the internal audit function has unrestricted scope and evaluates the effectiveness of the risk, compliance and finance functions as part of its internal audit plan.

The traditional British Approach to the accounts has long-focussed around the general principle, that accounts must give a "true and fair view" of the assets,liabilities,financial position and profit or loss". Auditor's have a right to access at all times to the company's books, accounts and vouchers. They are also entitled to require such information and explanations as necessary for discharge of their duties.[6]

However, unlikeIndia, where we have a separate provision dealing with a whistle-blower policy, under the Companies Act of UK,there is no general whistle blowing obligations of this type.However,the auditor needs to consider as per the accounting standards, whether "public interest" requires such action on the part of the auditor.[7]

C. THE INDIAN SCENARIO

As we have seen previously, the position of an auditor is like an intermediary agency between shareholders and management.The role of an auditor has been ascribed to be like that of a gatekeeper.[8]Scholars like

[5]ICAEW,(Audit Committees,20 May 2011)(https://www.icaew.com/archive/technical/corporate-governance/uk-corporate-governance/audit-committees)last accessed on 24 August 2018

[6] Gower and Davies,Principles of Modern Company Law,Thomson Sweet and Maxwell London ,Eighth Edition,P.791

[7] Gower and Davies,Principles of Modern Company Law,Thomson Sweet and Maxwell London ,Eighth Edition,P.793.

[8]Kshama V Kaushik,Rewa P Kamboj,(Study of State of Corporate Governance in India –Auditors) (http://iica.in/images/Auditors.pdf) last accessed on 24 August 2018

Kraakman and Coffee have gone on to define these gatekeepers as reputational intermediaries, including auditors who go on to provide verifications and certification services to the investors. They also suggest that these gatekeepers can be easily deterred from erring upon their professional services than their principals.[9]

The deterrence effect of legal regulatory framework will have a key role in preventing dereliction of duties and usher in transparency reforms. The agency viz. the statutory auditors, have to be technically qualified and also be independent. The provisions to accomplish these parameters are set out from ss.139-148 of the Companies Act,2013 of India.The researchers here will deal with few of the key provisions concerning auditors and how Indian Legal framework has sought to fix appointments, roles, duties and liabilities of auditors to ensure reforms within its corporate governance regime.

1. Under the Companies Act,2013:S.139 the Companies Act, 2013 deals with appointment of auditors. This section is a complete code and assimilates in itself provisions for a variety of situations

(a) Appointment of first auditors: The Board of Directors have the prerogative to appoint the first auditor or auditors within thirty days from the date of registration of the company. Such an auditor, when appointed shall be holding the office until the first annual general meeting concludes. If,the board is unable to appoint a first auditor, this has to be informed to the members of the company, who shall within ninety days from that day appoint an auditor through an extra-ordinary general meeting.The provision is a carry-forward from Companies Act of 1956 except the fact that in the previous Act, there was no time-limit for appointment by the share-holders in the extra-ordinary general meeting.This provision displays the urgency and gravity placed by the new Companies Act in appointment of auditor right from the start of a prescribed period, when the Company is incorporated and is indispensable as an over-sight mechanism within the company law framework in India.

(b) Appointment of auditors at the Annual General Meeting: This provision mandates that the auditor of a company (other than a Government Company)shall be appointed for a fixed term of five years starting from the conclusion of the first general meeting of the company and subject to ratification by share-holders at every AGM by way of passing of an ordinary resolution.The position is separate from that under the previous Companies Act of 1956 where the term of appointment of an auditor was from the conclusion of the annual general meeting at which he is appointed until the conclusion of the next annual general meeting.Thirdly, the sections have introduced a new requirement for the auditor to give a written consent for the appointment and a certificate is to be provided that he is duly qualified to be appointed as a director.Also all of the appointments of the auditors, including the filing of a casual vacancy, would be made after

[9]John C Coffee,'The Acquiescent Gatekeeper : Reputational Intermediaries, Auditor Independence and the Governance of Accounting 'Columbia Law and Economics Working Paper No.191(https://papers.ssrn.com/sol3/papers.cfm?abstract_id=270944) last accessed on 24 August 2018

recommendation of the audit committee.All of these provisions are clearly aiming to bolster the functioning of auditor and are reformatory corporate governance measures, to ensure that only well qualified

(c) <u>Rotation of auditors:</u>Audit Independence is one of the essential elements of Corporate Governance. Long and uninterrupted tenures bring a sense of complacency and which might be prejudicial to the requisite levels of independence and objectivity sought from the role of an auditor.[10]To check this problemmandatory requirement of auditor rotation after specified period has been brought in.Specific provisions have been mandated under S.139(2) of the Companies Act of 2013 belonging to such class/classes of companies as may be prescribed also under the Companies(Auditor and appointment of auditor Rules,2014) excluding one person Company and Small Company.There were clearly no provisions whatsoever,under the previous Companies Act of 1956 to ensure rotation of the auditors.In addition to whatever has already been described above, a cooling-off period of five years after the ceasing of audit services has been prescribed for both, individuals and audit firms before they can be appointed again.Now, S.140 of the Companies Act, 2013 deals with removal, resignation and giving of special notice to the auditors.Auditors fail to act professionally and exercise their judgement independently due to which most of the corporate failures occur.[11] This has been sought to be remedied by banning the auditor who acts fraudulently for a period of five years for any company. Liability will be sought to be imposed both on the partner and his firm.[12]

Further, in line with upholding his integrity, the auditor who has resigned is required to file within a period of thirty days from the date of resignation, a statement to in a prescribed formwith the Company and the Registrar of Companies indicating the reasons due to which he has resigned. This provision again seeks to improve the transparency in removal of an auditor and that that such an important decision is notified to important functionaries within the Company Law ambit like the Registrar.Also, the auditor concerned has to be given a reasonable opportunity of being heard.

Further,where a company intends to remove the auditor before the expiry of his term, an application is to be made in a form to the Central Government within 30 days of the resolution passed at the Board of Directors.[13]

Lastly, a new provision has been inserted that the National Company Law Tribunal can *suomoto* or on an application from the Central Government can direct the company to change its auditors, if they are satisfied that the auditors have directly or indirectly acted in a fraudulent manner with regards to the company in

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[10] N.Balasubramanian, 'Strengthening corporate governance in India: a review of Legislative and Regulatory Initiatives' IIM Bangalore, working paper no.447 (https://iimb.ac.in/research/sites/default/files/WP%20No.%20447%20(Revised)_0.pdf) last accessed on 24 August 2018

[11]Simon Mundy'PwC hit with 2year India Audit ban for Satyam',(Financial Times,11 Jan 2018), (https://www.ft.com/content/c1231f40-f695-11e7-88f7-5465a6ce1a00) last accessed on 24 August 2018

[12] N.Balasubramanian, 'Strengthening corporate governance in India: a review of Legislative and Regulatory Initiatives' IIM Bangalore, working paper no.447 (https://iimb.ac.in/research/sites/default/files/WP%20No.%20447%20(Revised)_0.pdf) last accessed on 24 August 2018

[13] RULE 7 OF companies(audit and auditor rules),2014

question.This section hence provides safeguards to make removal of conscientious and independent auditors difficult.

(d) <u>Eligibility, qualifications & disqualifications:</u>Now, coming to auditor's eligibility,qualifications and disqualifications these have been explicitly dealt under Section 141 of the Companies Act, 2013.Unlike the old Companies Act of 1956, the provisions concerning auditor independence have been tightened. A person is disqualified from being an auditor if he has

1. A business relationship with the company, or its subsidiary, or its holding or associate company, or subsidiary of the holding company, or an associate company.
2. A relative appointed as a director or employed as key managerial personnel.
3. Been convicted for an offence within last ten years.
4. Been concerned with a subsidiary or associate company or any with respect to prohibited consultancy or specialized services under section 144 of the Companies Act,2013.

The objective and rationale here is to prevent a conflict of interest-situation for the auditor and that he must be free to exercise his independent skill and judgment from any economic or other influence that may obscure his impartiality.

(e) <u>Audit Committees:</u>Section 177 of the Companies Act,2013 and Rule 6&7 of the Companies (Meetings of board and its powers) Rules,2014 mandate the creation of an audit committee in case of :

i. All listed and public companies with paid-up capital of Rs.10 crore or above; or
ii. All public companies having a turnover of Rs.100 crore or more; or
iii. Public Co.having outstanding loans/borrowings/debentures exceeding 50 crores or more as per audited financial statements of the company.

These audit committees existed even in the scheme of the 1956 Act, however only for those companies having paid-up capital of 5 crores then.These audit committees have been crucial in flagging off key-financial mismanagement concerns since they consist of a majority of Independent Directors .The majority of the members of the committee including the Chairperson need to be financially literate. The functions of these audit committees include recommendations for the appointment, remuneration and terms of appointment of auditors; reviewing and monitoring auditor's independence and performance, and effectiveness of audit process; examination of financial statements and auditor's financial report; approval of any subsequent modification of transactions with related parties; scrutiny of inter-corporate loans and investments to name a few.

The audit committee has also got the power to call for comments of auditors about Internal Control Systems, which has been discussed by the researchers later in this article; it also has the power to decide ask for scope of audit and observations of auditors and review of financial statements before submission to the Board of Directors.These auditors and key-managerial personnel have also the right to be heard in meetings of audit committees.

The audit committees have also established a proper vigil mechanism for directors and employees to report genuine concerns. Audit Committees have the power to oversee vigil mechanism (to prevent victimization of employees and directors who take recourse to such a vigil mechanism) and in exceptional cases direct access to Chairperson of Audit Committee or a director who is a member of Audit Committee is also provided.

This is a whistle-blower mechanism within the corporate governance frame-work for disclosures of financial irregularities within the corporate governance framework. The details of such a vigil-mechanism shall be communicated within the organization. The details of such a vigil mechanism will be disclosed by the Company in the website, and if any, in the Board report.

Clause 49 of the Listing Agreement also mandates as per SEBI guidelines, that an audit committee has to be effectively established for all listed companies. This is a mandatory requirement.

The co-relation between the internal auditing and corporate governance is well-established. An audit committee plays a vital role in ensuring theindependence of the audit process. The internal auditor's role is in providing of information to the Board of Directors and to assist them in its governance. It acts like a Liaoning body with respect of information supplied by the management to the auditors and at the same time, to safeguard the auditors from the pressure of the management.[14]

In today's business environment, these internal auditors go on to provide the management with a far broader range of information concerning the organization's financial, operational and compliance related aspects to improve effectiveness, efficiency and economy of the organization's performance.[15]The issues of internal audit failure in India came to the fore in case of a lesser known company, known as National Peroxide,[16]in which thirty-six crores were expropriated by an employee and the internal audit committee failed to detect the same.A larger example is offered to the scheme of discussion in the case of a well-known company known as Toshiba, in Japan, which came to be known as the poster boy [17]of internal-audit failure.

[14] "Auditor and Audit Committee Independence in India", JayatiSarkar and SubrataSarkar p.19

[15] Internal Auditing as an effective tool for Corporate Governance, Journal of Business Management,Vol.2 Issue No. 1,2010, Authors Theofanis Karagiorgos1, George Drogalas2*, EvaggelosGotzamanis&IoannisTampakoudis P.19-20

[16]K S Badri Narayan,'Flaws in Internal Audit Functon come to the fore',(The Hindu Business Line,10 Nov 2017),(https://www.thehindubusinessline.com/markets/flaws-in-internal-audit-function-come-to-fore/article9953421.ece) last accessed on 24 August 2018

[17]Ashish K Bhattacharya,(The Business Standard, 9 Aug 2015),(https://www.business-standard.com/article/opinion/toshiba-a-case-of-internal-audit-failure-115080900760_1.html) last accessed on 24 August 2018

The researchers here, point out to that fact that inspite of the fact that such according to the law requires to have independent directors majorly on its board, it still remains prone to the influences of the management, a careful study of most of the endemic corporate accounting scandals will reveal. Greater amount of insulation is needed to make the audit committees a more effective tool in raising the standards of corporate governance across the board-rooms of companies.

(f)Rights and Duties of the Auditor under the Present Company Law Framework:

The position of an auditor is that the he has a fiduciary relationship *vis-a-vis* the share-holders as a body. However,he is not at all obliged to respond to letters from individual share-holders or disclose any information to individual share-holders.[18] The auditor has to safe-guards the interest of the share-holders.

The Companies Act, 2013provides for some-duties of the share-holder which are as follows :

- Right to access to accounts, books of the company-An auditor of the company has been empowered under the Act to complete access of books,accounts,vouchers etc.in any matter relating to any transaction or data relating to financial statement.[19]
- Right to obtain information or explanation –Section 143 read with Section 129 of the Companies Act, 2013 empowers the auditor to require from the officers of the company all information as he deems necessary for the performance of his duties.
- Right to inspect branch accounts- The auditor is empowered to audit the account of any branch office in any appropriate cases.
- Likewise,he also has the right to receive notices and of other communications relating to the general meeting of the company and the right to attend general meeting of the company under Section 146 of the Companies Act,2013.

(g)Duties of an Auditor: Auditor's duties can be broadly categorized under major three heads viz.:

Fig. 1. ***Statutory duties of the auditor under the Companies Act*:** The Companies Act,2013 has imposed certain statutory duties upon the auditor under Section 143. The main function is to provide a true and fair view of the financial position of the Company. He has to examine the accounts of the company and submit a report to the members of the company. Thus, share-holders are statutorily entitled to receive an audit report.[20]An auditor is also under a duty to give his opinion with respect to the degree of compliance with the profit and loss account and balance sheets with accounting

[18] A Ramiah's guide to companies act,2013 18th edition p.2663
[19] Section 143 of the Companies Act,2013.
[20] Section 129(3) of the Companies Act,2013.

standards[21] He also has to give his opinion about the degree of the compliance to mention the reasons to give any negative or qualified answer in its report.

Fig. 2. ***Duties of Auditor under the Chartered Accountant Act,1949:***An auditor owes certain specific professional commitments under the Chartered Accountant Act,1949.The Act mandates that he is required to required to follow two sets of rules. That is, generally accepted Accounting Standards and Generally Accepted Auditing Practices

Fig. 3. ***General Duties of Skill and Care:*** There are a plethora of case laws which clearly explain the standard of duties of care and skill needed to be adopted by an auditor. He is required by the law to protect the interest of the company and its share-holders.[22]It was further held that he is not an insurer and does not guarantee that that the books of the company. It was also held that duty he owes is,he must be honest and must not certify something, which he does not believe to be true.[23]An auditor is not bound to exercise more than reasonable care and skill. What is reasonable skill, care and caution depends upon the facts and circumstances of the case at hand .He is not expected to be a detective at on hand and even in the case of a suspicion.

III. ROLE OF AUDITORS AND AUDITOR'S LIABILITY:A JUDICIAL APPROACH

India being, a common law country has borrowed most of its company law jurisprudence from the decisions of the courts in England. A few noteworthy decisions and important aspects of the role of an auditor are laid down below. These decisions supplements the law laid down in the provisions of the Companies Act, 2013.The audit report of the auditor is a certificate from him that the balance or profit and loss account in his opinion is true and is thus providing a fair view of the balance and sheet and profit and loss account for its financial year.[24]

Also, it is rightly said that the auditor's opinion represents "true and fair view of the financial state" of the company.Lindley L.J. a very famous judge noted that Auditor are appointed by the share-holders and that the auditor's opinion represents the "true and fair view" of the financial state of the company.[25]It is his duty to ascertain and correctly state the true financial position of the company at the time of audit done by him. The scope of his duty extends not only to the arithmetical verification of the balance sheet but also to view with substantial accuracy and that includes the particulars required by the Articles of the company, statutes and contain the true and fair financial position of the affairs of the company.[26]

[21] Section 129
[22] Leeds Estate Building and Investment Co. Vs. Shephard 36 Ch.D (1887)
[23] id
[24] Id.
[25] Re London and General Bank(1895) 2 Ch 673
[26]Dy.Secretaryvs S.N. das gupta AIR 1956 cal 414.

[1]*<u>An auditor is not an advisor</u>*: An auditor is not at all concerned with the policy of the company. As observed by Lindley L.J. again,[27]in his very own words, "It is no part of an auditor's duty to give advice, either to directors or share-holders, as to what they ought to do. An auditor has nothing to do with the prudence and imprudence of making loans with or without security.Likewise,he also has nothing to do whether the business of a company is being carried out prudently or imprudently".

[2]*<u>An auditor is not an insurer</u>*: The law also lays that an auditor is not an insurer and does not guarantee that the books of the company show the true-position of its affairs or that its balance-sheet is accurate according to its books. The law certainly however, places a duty to ascertain and certify to the share-holders the true-position of the Company at the time of the audit.[28]

[3]*<u>Auditor as an agent</u>*: The extent to which an auditor can be regarded as an agent of the company or the share-holders was considered by the House of Lords in *Spackman V. Evans*[29],where it was decided then that, the auditors could well be regarded as agents of the members appointed to carry out certain duties as laid down by the Act and confined by the Articles of the Company.

[4]*<u>Auditor is a watch-dog, not a blood-hound</u>*: This is probably one of the most-common statements or figure of speech, summing up what an auditor is expected to do. This was laid down by Lopes L.J. and he goes on to state in what is a notable decision,[30]that "the auditor is only a watch-dog and not a blood-hound, which casting the metaphor aside, means that his duty is verification and not detection. But does not verification extend to being vigilant? Is not watch-dog bound to bark and chase too, where necessary? If when, sniffing around, you hit the trail of something wrong, is exposed.As per the judgement of Lord Alverstone in(also referred to in Dicksee's Book on Accounting), it is the duty of the auditor, where suspicion is aroused, to probe the things to the bottom. The above view was re-iterated in a lot of Indian decisions.In one of the decisions[31] it was clearly stated that an officer or an employee of the company may not be appointed as an auditor. An auditor has to be *necessarily independent* of the Board of Directors of the Company. Again,it was also noted in a decision of the Supreme Court of India[32] that an auditor is expected to play the role of watch-dog on behalf of the share-holders of the company.

In the United Kingdom, a company undergoing an audit inevitably enters into a contract with the auditor for the provision of professional services.So,just like any other person who renders professional services, the auditor owe the company, an implied contractual duty of care in the proper performance of the audit.[33]

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[27] Re London and General Bank(1895) 2 Ch 673
[28] City Equitable Fire Ins. Co.Ltd.,Re. (1925) 1Ch 407
[29] In re Kingston Cotton Mills Co.(1896) 2 Ch 279
[30] Id
[31] CIT vs. G.M. Dandekar (1952) 22 Com Cases 356 (Mad)
[32] Hindustan Lever Employee's Union vs. Hindustan Lever Ltd.(1994) Comp LJ 250 at 268 (1995) 83 Com cases 30 (SC)
[33] Sealy and Worthington's text, cases and materials in Company law,11th Edition, Sarah Worthington,oxford University Press,P.484

Auditors as such are liable in tort for misstatement. This fixation of liability has seen much wavering by the Courts of UK.The researchers have tried to analyze the liability of the auditors as said by the courts there in three phases.

[1]***Pre-Caparo Position:***The question of liability of auditors comes with respect to third persons. The courts have usually been very restrictive in capping the scope of auditor's duty.The standard of care which is to be exercised by auditors as well as the duties of an auditor in determining whether any misfeasance or breach of duty has been committed; has been laid down, in an early decision,[34]which has gone to state that Auditor's must exercise reasonable care and skill, and must certify only to the members or share-holders what they believe to be true.

Later, in a subsequent judgment[35]the scope of an auditor's duty was elucidated upon, the UK Court of Appeal held in explicit terms that "It is no part of the duty of the duty of auditor's to repeat work already undertaken internally, in the absence of suspicion, auditors may rely on the assurances of a manager or other apparently responsible employee."

This judgment displays the passivity and reluctance of the court in holding the auditors liable, the court simply saw whether the auditor had relied on the assurance of manager and not whether he subsequently acted on his own to find out the truth.The auditor's duty underwent some further change in this judgment,[36]when this passivity was shed to some-extent and held that an auditor, when he had been, or ought to have been put on inquiry, was under a duty to conduct and make an exhaustive investigation.The question of against whom does the auditor's duty of careis, has been an elusive question for quite some time, particularly with respect to third persons. This question was sought to be answered by the House of Lords in the momentous decision of *Caparo Industries plc.*v.*Dickma*n.[37]

[2]***Caparo Position***: The House of Lords in this case expressly decided in negative with respect to duty of care owed by the auditor with respect to any members of public who relied on the accounts in deciding whether to invest in the company's shares. It was also held that auditor's owed nothing to even the company's members who rely on the accounts for the purpose of decisions in relation to present or future investments in the company.

Lord Bridge held that if such a duty of care were owed so widely, it would be clearly difficult to see any reason why that should not extend equally to other members of the society who relied upon such accounts in relation to other dealings with accompany as lenders or merchants extending credit to the company.

Another justification as to why the court was reluctant to hold an auditor under a duty of care to anyone lending money to the company by the reason that it would be foreseeable as highly probable that the

[34] Supra note 12
[35] Supra note 16.
[36] Re Gerrard& Son Ltd. (1968) Ch.45
[37] (1990) 2AC 605

company would borrow money at some time in the year following publication of its audited accounts.So ,this was the position of law laid down in *Caparo*verdict.

[3]***Post Caparo Position***: The position of the Courts has changed since the *Caparo*Verdict. There are cases which are going further towards fastening the liability of auditors even more. In *Barringsplc* V. *Coopers&Lyband(a firm)*[38], it was clearly held that auditors of a subsidiary owed a duty of care not only to the subsidiary but also to the parent company.

In the recent years, there have been increasing obligations placed on company auditors both by legislation and non-statutory measures in UK.The UK Corporate Governance Code requires that, as a matter of good practice, the board of a listed company should establish an audit committee of minimum three directors,all non-executive and (having a majority of "independent non-executive directors" whose duties should include keeping under review the scope and results of the audit and its cost-effectiveness, and the independence and objectivity of auditors.[39] The position is also similar to the one under Indian Companies Act, 2013 wherein statutory audit committees have been mandated with similar functions and composition.

Lastly, in a recent case[40], it was held by House of Lords that in case of frauds perpetrated by a" one-man company", the company cannot sue its auditors for negligence in failing to detect the fraud.

*Caparo*thus represented a firm rejection by the House of Lords of the proposition, that negligent auditors were liable to those who it was reasonable to forsee would rely on the audited accounts and who suffered loss as a result of such reliance.[41] While the case laws after *Caparo* established and concentrated on seeking to determine the basis or bases upon which,it might be possible for the "claimants" to establish a special relationship", on the part of the auditor to towards the claimant. Thetest, is an objective one and it all depends upon the facts and circumstances before the Court.[42]

IV. PROBLEMS WITH ACCOUNTING AND AUDITING IN INDIA

The researchers will like to bring to the fore the problems with accounts and auditing, in this regard "Asian Corporate Governance Association, Hong Kong"[43] has brought to the public domain the problems faced. These suggestions and recommendations have been discussed further in this paper. In India, the audit profession is highly fragmented. Most of the audit firms in India have minuscule capacity and it is very difficult to distinguish between small and medium accounting firms. The resultant consequence is that even

[38] (1997) 1BCLC 427 CA

[39] Sealy and Worthington's text, cases and materials in Company law,11th Edition, Sarah Worthington,Oxford University Press,P. 492

[40] Stone and Rolls Ltd(In Liquidation) V. Moore Stephens(A Firm) (2009) UKHL 39.

[41] Gower and Davies,Principles of Modern Company Law,Thomson Sweet and Maxwell London ,Eighth Edition,P.805

[42] Gower and Davies,Principles of Modern Company Law,Thomson Sweet and Maxwell London ,Eighth Edition,P.806

[43]Ummakanth Varottil,(ACGA Working Paper on Corporate Governance,Jan.20.2010),(https://indiacorplaw.in/2010/01/acga-white-paper-on-corporate.html) last accessed on 24 August 2018

large companies which are listed on overseas exchanges and are top Fortune 500 companies are audited by these small, miniscule firms with limited auditing capacity. These small firms are unable to handle the accounts of companies properly due to lack of in depth knowledge to handle these matters. These firms are also incapable of scrutinizing the internal controls and risk-management process of their respective client at all.

India is one country, wherein a recent survey shows that at least 89 percent of the companies were affected by at least by one instance of fraud, while 33 percent admitted revenue losses to the tune of 7 percent due to these financial frauds.[44]The Companies Act, 2013 has introduced for the first time, "Internal Financial Systems[45]"in an effort to curb financial frauds in India. This includes a set of policies and procedures adopted by the Company to ensure adherence to the company's policies, safeguarding of its assets, prevention and detection of financial frauds, accuracy of the firm's financial records and timely preparation of reliable financial information.

The Institute of Chartered Accountants of India (ICAI) has also issued a guidance note[46], which mandates involvement of an external auditor in the compliance process.The note goes on to state that the auditor's objective in an audit of internal financial controls is to express an opinion on the effectiveness of company's internal financial controls and that the procedures are carried on along with an audit of the financial statements. Also along with the auditor, a responsibility has been cast on the manager's to consider the Internal Controls to cover all the aspects of the management of the company. The Act requires the directors' responsibility statement to state that the directors responsibility statement, in case of a public listed company, to lay down the internal control systems of the company and observe that such internal controls are operating effectively and efficiently.[47]

At the present moment, the ICAI is totally helpless take effective legal action against the auditor on their professional misconduct. The most plausible explanation for this the plethora of committees which look into disciplinary action and the high chances of litigation over them.[48]Any penal action imposed by the ICAI could be challenged by an aggrieved auditor in the court of law. This not only burdens ICAI financially but also a very lengthy court process which turns out to be non-feasible for ICAI.

[44]Rohini Singh, (India Briefing, June 28 2018)'Internal Controls,Anti-Fraud strategies for companies in India,(https://www.india-briefing.com/news/internal-controls-anti-fraud-strategies-companies-india-17148.html/) last accessed on 24 August 2018

[45] Section 134 of the Companies Act,2013.

[46] ICAI guidance note on "Audit of Internal Financial Reports over Financial Resporting or ICFR"

[47] Section 134(5)(e) of the Companies Act,2013.

[48] ACGA white paper on corporate governance in India,January,19,2010.

Meanwhile,ICAI's weak position in taking action against its the very chartered accountants (auditors) it is supposed to take action against has reached the Supreme Court,the Courtfaulted the ICAI for not taking appropriate action against such auditors, especially Multinational Accounting Firms.[49].

However, the capital markets regulator SEBI has of late, shown some interest in reigning in on errant auditors of listed companies. The proposed move is in light with several high profile corporate accounting scandals which have popped up recently notably, the SATYAM scam in 2009, the KINGFISHER case in 2017 and PNB fraud in 2018.

A consultation paper is being proposed with all relevant stake-holders and also to prevent the disparity of accurate information regarding the financial position of the company.[50] The consultation paper named "Review of Corporate Governance Norms in India"[51] by SEBI has taken into account all such measures taken by it with respect to corporate governance measures in listed companies such as introduction of Clause 49 in listing agreement which mandates formation of an audit committee.

Also, veryimportantly, recently back in 2017,a corporate reviewing committee had suggested that SEBI should be given clear powers, to act against such errant and fraudulent auditors.[52] Moreover, SEBI as of March, 2018has accepted certain recommendations with respect to audit committees The Kotak Committee had recommended regarding the role of audit committees, nomination and remuneration committees, and risk management committees, which have now been accepted by SEBI. The role of an audit committee has now been enhanced to include the review of the utilization of loans and/or advances /investment by the holding company in the subsidiary (including foreign subsidiaries), exceeding INR 100 crore, or 10% of the asset size of the subsidiary, whichever is lower. The terms of references and roles of the audit committee, nomination and remuneration committee, and risk management committee, are also to be clearly disclosed in Offer Documents of public issues. The enhanced role of the audit committee, nomination and remuneration committee, and risk management committee will also have to be approved by the board of listed companies, and accordingly the same to be disclosed in such Offer Documents.[53]

Another emerging problem which has come to the fore concerning the auditors, is the massive spate of resignations from large public listed companies(as many as 30 companies have resigned from their respective companies) flagging off concerns about auditing standards and also fearing backlash from regulatory bodies

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[49]KR Srivats,(The Hindu Businessline,Feb 25 2018)(https://www.thehindubusinessline.com/news/national/apex-court-says-its-time-to-regulate-multinational-accounting-firms/article22852001.ece) last accessed on 24 August 2018

[50](The Week,March 21,2018),'Frauds at listed firms,SEBI to reign in erring-auditors-valuers)(https://www.theweek.in/news/biz-tech/2018/03/21/fraud-at-listed-firms-sebi-to-rein-in-erring-auditors-valuers.html) last accessed on 24 August 2018

[51]SEBI Consultative Paper on Corporate Governance in India,(https://www.sebi.gov.in/sebi_data/attachdocs/1357290354602.pdf) last accessed on 24 August 2018

[52]Uday Kotak Commitee Recommendations 2017.

[53]Oishik Bagchi,(Khaitan&Co. 9April 2018)'The SEBI Board Meeting on the adoption of the Kotak Committee's recommendations'(https://www.khaitanco.com/PublicationsDocs/Mondaq-KCOCoverage9Apr18Oishik.pdf) last accessed on 24 August 2018

like the Ministry of Corporate Affairs,SEBI.[54]The issue here is also relevant in respect of the fact that all is not well within these companies with respect to the financial accounting standards and the level of corporate governance is not up to the mark.

It will be interesting to note what the Ministry of Corporate Affairs, the key regulatory body of Companies does, report suggest that since the events, it has already swung into action.[55] Also ICAI has formed a group to investigate into what led to these massive resignations in a short-frame of time.[56]Big auditing firms like Price Water Coopers who were the auditors for Vakranjee resigned stating “absence of adequate and relevant information” for purposes of auditing. Again something like this was stated with respect to a company named Atlanta, aninfrastructure and engineering firm, when Price Water Coopers resigned assigning “significant information” and “observations by Tax Authorities” were not provided. These examples are illustrative of few but numerous examples of auditing concerns raised by auditors with respect to corporate governance standards prevalent amongst companies in India.

Further, the auditing firms have started to be extra-cautious regards choosing clientele, are investing significant time in doing diligence research of the portfolio of clients. The banning of auditing firms like Price Water Coopers by SEBI from issuing audit certificates for any listed company for two years has already sent shudders down the spine of auditors; as a result more cautious approach is to be seen by them.[57]

The white paper discussed previously by the researchers, has also recommended that for the creation of an independent audit regulator. The ICAI is at best, a self-regulatory body, but is not completely independent from the profession, itregulates, and therefore there is an urgency to establish an independent audit regulator. It would not only bring India closer to the international norms and solve a host of problems relating to auditing firms. For ex: It is very difficult to present time for an auditor to individually examine the bank statement of the company because bank does not respond to furnish such information promptly, at times even evading to answer even. Heavy reliance is placed on the bank account information provided by the company. An independent regulator can clearly take care of all these issues.

V. INDEPENDENCE OF AUDITORS:A KEY ISSUE FOR DEBATE

A. THE NEED FOR AUDITORS

[54]Vinod Mahanta,(The EconomicTimes,June 2,2018)’Manpasand Decoded:Nearly 30 auditors resigned from Indian Companies this year’(https://economictimes.indiatimes.com/industry/services/consultancy-/-audit/30-auditors-resigned-from-indian-companies-this-year/articleshow/64422972.cms) last accessed on 24 August 2018

[55]CA Amresh Vahisht(Tax Guru,19 Aug 2018)’Auditor’s resignation raises critical eyebrows’(https://taxguru.in/chartered-accountant/auditors-resignations-raises-critical-eyebrow.html) last accessed on 24 August 2018

[56] Id.

[57]Vinod Mahanta,(The EconomicTimes,June 2,2018)’Manpasand Decoded:Nearly 30 auditors resigned from Indian Companies this year’(https://economictimes.indiatimes.com/industry/services/consultancy-/-audit/30-auditors-resigned-from-indian-companies-this-year/articleshow/64422972.cms) last accessed on 24 August 2018

The two most fundamental and defining characteristics of a corporation form of business enterprise is the 'divorce between ownership and management'[58], and the 'limited liability principle'[59]. Since, the shareholders are not aware and acquainted with the day to day activities of the corporation and these activities are dealt with by the managers; a reasonable doubt arises in the minds of the shareholders regarding the truthful discharge of managerial functions because humans are inherently selfish by nature. Moreover, the history of corporate world has largely witnessed corruption of the powers vested in the management in the form of numerous corporate scandals such as Enron Corporation, Global Crossing Limited in the United States, and Satyam in the Indian context, to name a few, leading to enormous decline of public faith and investments in these large corporations. These corporate frauds have been significant enough to draw the attention of the public towards the misguidance of the public by the managers and the misuse of the public funds by the corporations. Hence, the need for overseeing the functions performed by the managers by an external third party arises so that the same may be authenticated and the shareholders may be assured of their trueness. Thus, a need for an external auditor or a statutory auditor comes into the demand.

Furthermore, the present and existing rules of accounting provide some sort of flexibility to the managers of a company to decide upon the representations of financial information of a company. However, the freedom accorded to the managers, also opens up the possibility of misrepresenting the financial conditions of a company in a way so as to inflate the profits and assets, and also undervalue the losses and liabilities, which causes serious information risk for the users of financial statements.[60] In order to curb this possibility of misrepresentation of financial statements, which does not allow the financial statements to exhibit a true and fair view of the financial conditions of a company, it is often statutorily required that such statements must be audited by external statutory auditors to ensure the authenticity and genuineness of the financial statements so audited.[61]

B. THE NEED FOR INDEPENDENCE OF AUDITORS

The rudimentary aim of conducting audit is to ensure that the activities of an enterprise are carried out by the managers in good faith in the best interest of the company and the resources are not being used to satisfy the selfish desires of the managers. A reference to the various corporate scandals and frauds highlights

[58]As per the popular and predominant view, the corporation form of business entity is collectively owned by the entirety of the shareholders (different views prevails in regards to the ownership of a company), but the management of the company is often entrusted to a limited number of persons who are technically sound and professionally equipped to deal with the day to day affairs of the business, i.e., the Board of Directors.

[59]The limited liability principle restricts the liability of a member of a corporation to the amount unpaid on the number of shares held by him, or to the amount undertaken by him at the time of incorporation of a corporation. It is also a logical extension of the principle of separate identity concept as it distinguishes between liabilities of the corporation as against the personal liability of the members of the corporation.

[60]There are various users of a financial statement of which the most prominent are the shareholders and the creditors.

[61]SreetiRaut, Corporate Governance- Concepts and Issues, http://www.iodonline.com/Articles/Corporate%20Governance%20and%20Sustainability%20Concepts%20Sreeti%20Raut.pdf, accessed 18-08-2018, 7.

that the auditors and the auditing process as a check against the misdeeds of the management has utterly failed because of the lack of independence of the auditors. Hence, a significant call for effective corporate governance is, time and again, felt as there exist a positive relationship between corporate governance and audit independence, which implies effective corporate governance lead to greater auditor independence.[62]

As mentioned before, there exists a positive relationship between corporate governance and financial reporting. This implies that a corporate world witnessed by effective corporate governance regime is characterized by rigorous financial reporting which when mingled with crucially significant independent audit, creates an environment of trust and confidence of the users of financial statements in regards to those financial statements. Not only that, a direct relation is also exhibited between corporate governance and shareholder value, which implies that capital markets under the control and supervision of a strong corporate governance regime will have better investment than those under the garb of an inefficient corporate governance with low levels of performance standards. This is because the quality and standards audits performed by an independent third party or an external auditor ushers confidence in the investors. Therefore, it is utterly important that external auditors shall be as well as appear to be independent from the companies they audit.

Thus, the primary goal of an auditor is to reasonably ensure that the financial statements have been represented fairly and are free from any form of substantial misstatement due to any fraud or deliberate or unintentional error on the part of the accountants and the auditors shall express their genuine, unbiased and objective opinion in the auditor's report. In certain jurisdictions, the auditors are also required to ventilate their opinion on the effectiveness of the internal control system which in time will effectively improve the operation of the company. Hence, the independence of the external auditor in both fact and appearance is once again underlined.

C. MEANING OF AUDITOR INDEPENDENCE

The concept of auditor independence is not a straightforward concept to define. It has multiple dimensions and various definitions of auditor's independence include one of its dimensions and misses out at another. Hence, there are multiple definitions of auditor's independence which is not incorrect completely, but at the same time cannot be even considered as comprehensive.The International Auditing Practices Committee of the International Federation of Accountants equates the independence of auditors with qualities like honesty, sincerity and straightforwardness in their approach towards professional work. An independent auditor is expected to be essentially fair and not allowing biasness or prejudice to override his neutrality. He shall maintain an objective and independent attitude and shall not only be but also appear to be free from all

[62] Mahdi Salehi, Corporate Governance and Audit Independence: Empirical Evidence of Iranian Bankers, International Journal of Business & management, Vol. 3 Issue 12, December, 2008, p 44-51, 46.

forms of interest, in order to be compatible with the notions of objectivity and integrity.[63] Independence of auditor has even been defined as the ability of an auditor to avoid partiality and to render objective, authentic and reliable opinion on the financial statements, with the assurance that any deviance from the set and established norms will be reported on detection.[64]

D. THREATS TO INDEPENDENCE OF AUDITORS

The most prominent challenges to the independence of auditors are the threats of self-interest, self-review and familiarity. The reasonable expectation of benefitting through subsistent financial interest in the audited company denotes the self-interest threat to independence. This usually becomes prominent when an economic or financial relationship exists between the auditor or auditing firm and the audited company. Thus, it is most common when the non-auditing services are rendered by the auditor as there exists an interest of the auditor in subsisting the relationship with the audited company, even at the cost of independence. The self-review challenge encompasses the intricacy and complexity of remaining objective and impartial at the time of evaluating the work performed by the self. Existence of relationship between the auditor and the audited is necessary to effectively perform audit, however, an intense or extremely friendly relation between the two often hinders the objectivity and allows the managers to influence the report of auditors. Such instances are an exhibition of the familiarity challenge.[65]

E. IMPORTANCE OF AUDITOR INDEPENDENCE

It has been widely recognized that the independence of an auditor is somewhat equivalent to a pre-requisite for the general public to repose their trust and confidence in the reports made by auditors as it significantly enhances the reliability and authenticity of their reports which are taken up very seriously by the investors as a guide for making investments.[66] It is to be noted that the reliability of an auditor's report is judged by the knowledge, competence, experience and skill of the auditor on one hand, and by his independence on the other hand as it is independence only, which allows the auditor to be unaffected by any form of threats or influences and maintain an impartial view with an objective approach and report the deviations in the financial statements if found without any fear or favour. The independence of auditor takes the central stage in the discussion of auditors in the larger public interest as auditor report is often used by many as a guide for investments[67] and the public largely depends upon the report of the auditors as a true

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[63] Mahdi Salehi, Corporate Governance and Audit Independence: Empirical Evidence of Iranian Bankers, International Journal of Business & management, Vol. 3 Issue 12, December, 2008, p 44-51, 47.

[64]DeAngelo, E. L. (1981). Auditor Independence, "Low Balling", and Disclosure Regulation.*Journal of Accounting and Economics, 3, 113-127.*

[65] Financial Reporting Council, APB Ethical Standard 5, Non-Audit Service Provided to Audited Entities, 2011.

[66]Mahdi Salehi, Corporate Governance and Audit Independence: Empirical Evidence of Iranian Bankers, International Journal of Business & management, Vol. 3 Issue 12, December, 2008, p 44-51, 47.

[67] Mahdi Salehi, Corporate Governance and Audit Independence: Empirical Evidence of Iranian Bankers, International Journal of Business & management, Vol. 3 Issue 12, December, 2008, p 44-51, 47.

indicator of company's financial strength and soundness. Thus, lack of independence would greatly harm the interest of the investors and would lead to disruption of markets, bringing detrimental loss to the economy of the nation.

F. THE GREAT DEBATE ON AUDITOR'S INDEPENDENCE AND NON-AUDITING SERVICES

Non-audit services refers to all those professional services, other than the auditing of the financial statements that are rendered by an auditor or an auditing firm in respect to the audited entity, its affiliates or any other undertaking in respect of the audited entity.The statutes regulating the functions of the auditors often provide a restriction on the variety of services to be performed by the auditors.[68] Thus, the auditors are often statutorily prevented from discharging non-audit services. A reasonable doubt in regards to the independence of auditors arises in the minds of the public if they discharge auditing functions as well as other non-auditing functions such as accounting or book-keeping services or management services because the integrity of the financial statements is sacrificed once the auditors are seen to be under the pressure of the client or appeasing the management. Moreover, the power of the management to appoint and dismiss auditing firms or auditors often compels the auditors to satisfy the management rather than giving a qualified report on unfair and untrue financial statements, and puts the very essence of independence of auditors in jeopardy.[69]

The intense debate on whether the discharge of non-auditing services by the auditors has an adverse impact upon the independence of the auditors or impairs the independence of the auditors could not see the light of a definite conclusion for long. Two divergent opinions have been vehemently propounded in this regard on an equally strong footing. On one side, it is argued that the performance of non-auditing services by the auditors is actually a boon as it allows a comprehensive understanding of the functioning of the audit client to the auditor and hence, makes the audit more effective and revealing.[70] Contradictorily, it is argued that the performance of non-auditing services by the auditors in order to gain extra revenue and other perquisites often creates a robust economic relationship between the auditors and the audited company, deeply blighting the independence of the auditors.[71] There has always been an equal contest between the two sides of this great debate.[72] If allowing non-auditing services to the auditors creates an impression of invalidating the notion of independence of auditors,[73] not allowing the same to the auditors or auditing firms has raised questions on the possibility of their extinction from the markets. History has witnessed many efforts been put into this regard

[68]For instance, Section 144 of the Companies Act, 2013 of India provides for certain services not to be rendered by the Auditors. Similarly, Section 210(g) of the Sarbanes Oxley Act, 2002 provides for the same.
[69]SreetiRaut, Corporate Governance- Concepts and Issues, http://www.iodonline.com/Articles/Corporate%20Governance%20and%20Sustainability%20Concepts%20Sreeti%20Raut.pdf, accessed 18-08-2018, p. 7.
[70]Simunic, D. 1984. Auditing, consulting, and auditor independence.Journal of Accounting Research 22 (2): 679–702.
[71]Sikka, P. (2009). Financial crisis and the silence of the auditors.*Accounting, Organizations and Society, 34, 868-873.*
[72] Schneider, Church, & Ely, 2006
[73]Hall, W. D. 1988.An acceptable scope of practice. CPA Journal 58 (February): 24–33.

in the form of various researches been conducted, but without any conclusive proof or substantial evidence in the favour of either of the sides of debate.[74] Out of the various researches that have been conducted, two researches that has been carried out in the very recent past has attracted the attention of the researchers and seems to be based on most objective indicators and apt in their approach.

In the year 2014, a study has been conducted by Monika Causholli, Dennis J. Chambers and Jeff L. Payne which has revealed that there exists a negative relationship between the non-auditing services and the independence of the auditors implying that discharge of wide varieties of non-auditing services by the auditors have significantly impaired their independence and hence, has negatively affected their quality of audit. This research was primarily based on two research yardsticks, viz. abnormal accruals[75] and classification shifting[76]. The research revealed that there is substantial relation between the two research indicators and the amount of non-auditing services. The research showed that abnormal accruals were more and more instances of classification shifting were found in companies, which has received non-auditing services from their auditors, implying that the partnership of the auditors with non-auditing services has an enormously adverse effect on the independence of the auditors.[77] The research also revealed a model of promotion prevalent among the auditing firms which granted greater compensation and vocational benefits to auditors who managed to sell the non-auditing services to their audit clients. This immensely encouraged the auditors to act in the most favourable way as to appease their audit client[78] in order to gain non-auditing service contracts from them and in pursuance of those efforts, they often overlooked the flaws in the financial statements and turned a blind eyes to the accounting flaws with their independence being compromised in their vocational advancing pursuits. It also adversely affected the quality of audit as auditors with better salesman skills were preferred and advanced over those who were technically sound but were not proficient in selling non-auditing services.[79]

[74]Brandon and Mueller (2009); Frankel, Johnson, and Nelson (2002); Ashbaugh, La Fond, and Mayhew (2003); De Fond and Francis (2005); Francis (2006); Schneider, Church, and Ely (2006); Bloomfield and Shackman (2008); Lim and Tan (2008); Habib (2012).

[75]It refers to the variance between the expected accruals and the observed accruals. It acts as a measure of auditor independence in the sense that the consent of the auditor to unexpectedly abnormal accruals exhibiting higher or lesser net profits reveals substantial evidence of compromised independence of the auditor.

[76] Classification shifting is measured in reference to the core expenses, which is significant for financial analysts and investors. It is usually done by misrepresenting the core expenses of the company as special expenses and thereby, does not allow the financial reports to reveal the true, fair and correct state of affairs of the company. It is also in contradiction to the established and generally accepted principles of accounting and auditors are required to take actions against such misrepresentations in the form of qualified reports.

[77] Monika Causholli, Dennis J. Chambers, and Jeff L. Payne, Does Selling Non-Audit Services Impair Auditor Independence? New Research Says, ‘‘Yes’’, Current Issues in Auditing, American Accounting Association, Volume 9, Issue 2, 2015, Pages P1–P6

[78]This was also pointed out by Goldwasser in his studies in the year 2002 as he stated that the expectation of earning in the future greatly blights the independence and objectivity of the auditor and puts his independence in serious peril at Goldwasser, D. L. 2002. The accounting profession’s regulatory dilemma. CPA Journal 72 (May): 8–13.

[79] Monika Causholli, Dennis J. Chambers, and Jeff L. Payne, Does Selling Non-Audit Services Impair Auditor Independence? New Research Says, ‘‘Yes’’, Current Issues in Auditing, American Accounting Association, Volume 9, Issue 2, 2015, Pages P1–P6; this was also propounded earlier by Coffee in 2006 at Coffee, J. C. Jr. 2006. Gatekeepers: The Professions and Corporate Governance. New York, NY: Oxford University Press.

Another study that was pretty appropriate in its approach and objective in its selection of research yardsticks was carried out by Caroline More and Sofie Berg in the recent year of 2016, which considered the accounting reports and financial records and data of eleven companies from the wholesale and retail sector in the food industry[80] and considered the big four[81] as pioneer of the auditing firm as their sample size for a considerable period of time[82]. The five research indicators that were used to assess the auditor independence included the providing of non-auditing services to those who are already audited by the auditor; the tenure of the auditor; the ratio of Non-auditing services to total services rendered; the ratio of tax services to non-auditing services rendered and the revenue of the Big Fours. The research unearthed that almost all the companies contracted for non-auditing services with their auditors.[83] If the researcher has to highlight the point of findings relevant to the present context, it may be stated that the research conducted by More and Berg revealed emphatically that revenue generated by the non-auditing services by the auditing firms far exceeds the amounts generated by discharging auditing functions. The researcher brought to the forth that the revenue generated by non-auditing services were significant part of the total revenues and in certain financial years, it even exceeded the revenue generated by the core activity of the firm, i.e., auditing services.[84]Thus, on the comprehensive analysis of the research findings, it can be deduced that the auditing firms relied heavily on their non-auditing services in order to draw the life-blood of their economic organization, i.e., finance. Since, greater revenue is generated by the non-auditing services, the auditors often put their independence and objectivity in danger in order to retain the non-auditing services contract with them, resulting in the decline of quality and reliability of audit and making the entire process of audit futile.

Thus, the above discussion along with the various researches conducted in the past, including the two that has been elaborately discussed within this research project amply highlights that the discharge of non-auditing services adversely impacts the independence of the auditors and sacrifices their objectivity which has even culminated into the unpopular corporate frauds. After these unimpressive corporate scandals and frauds in the United States of America as well as in India, such as the Enron Scandal, the Satyam Scam respectively, and others, the statutory framework regulating the corporate structure and the position of auditors in that framework has undergone sea-change. In the context of United States of America, the enactment of Sarbanes Oxley Act in the year 2002 has significantly changed the scenario as it prohibits and restricts the discharge of a wide variety of non-auditing services by the auditors.[85] In addition to it, the United States Securities and

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[80] These eleven companies from the food industry, inter-alia, includes Booker Group PLC, Crawshaw Group PLC, SSP Group PLC, Ocado Group PLC, Sainsbury, Greggs, Tesco, Snacktime PLC to name a few.
[81] The Big Four Accounting Firms whose financial information was looked into for the purpose of research included Deloitte, PwC, KPMG and Ernst and Young.
[82] The accounting information of the eleven companies from the food industry was taken for the period of 2007-2014; whereas in regards to the big fours, the financial information from 2012-2014 was considered.
[83]As per the research conducted by L. Abbott, S. Parker and D. V. Rama in the year 2007, 96% of the public listed companies contracted with their auditors for the discharge of non-auditing services in the year 2000.
[84] Caroline Moré& Sofie Berg, The Effect of Non-Audit Services on Auditor Independence, Jonkoping University, International Business School, May 2016.
[85]Section 210(g).

Exchange Commission has issued rule[86] in the year 2003 to do away with the framework that promoted partners in the auditing firms on the basis of their ability and success in selling non-auditing services to the audit clients, which enormously encouraged the auditors to sell non-auditing services to the audit clients at the expense of their independence. Similarly, in the Indian context, the Companies Act of 2013 introduces a novel provision[87], which has no corresponding provision in the erstwhile 1956 Act which provides a strict prohibition on the discharge of a wide variety of non-auditing services by the auditors in order to preserve their independence. Thus, this is another exhibition of the fact that the discharge of non-audit services by the auditors was fatal to their independence and objective approach.

VI. CONCLUSION

The researchers have analysed the corporate governance framework regime within the US, wherein the Sarbanes-Oxley Act of 2002 introduced significant changes post 2002 Enron scam. Some of the key changes which India lacks as of now compared to US, is the lack of an Independent body to oversee auditing process of public companies in India, like that of a Public Company Oversight Auditing Board in the US. Criminal penalties are harsh along with civil liabilities for fudging up the accounts and interfering audit works in the US, a provision which is quite loose in the Indian Jurisdiction. Also “auditor independence” has been emphasized to a broad extent on the US, while the India position has only offered a mere “lip-service” to the provisions, there is lack of real-teeth in the provisions.

Coming to the UK position, the Indian Courts have rarely gone beyond the extent of assigning the auditor as “a watchdog”, the Courts in India need to start thinking as per the post *Caparo*verdicts, in assigning and fixing the liability of the auditors with respect of third-persons. The Corporate Governance Code of UK(2016) has provided for the induction of those persons into auditor’s committee of the company, who have relevant experience in the fields of another company which the present company is dealing with. A provision of this sort is pending in Indian perspective .This will bring relevant auditing perspective in to the Company. Also, the Company law of UK has given much importance as well as independence to the task of an audit committee, something which has been verily missing in Indianperspective.The researchers have shown in Indian light, the cases where independence and integrity of the audit committeeswere breached a lot of times. Coming to the Indian perspective,the researchers have tried to show as to how the Present Company Law framework has tried to usher in new reforms and also how they still might just be insuffiecient.SEBI has tried to act on its behalf in plugging the gaps as far as auditor’s liability is concerned for listed companies after high profile scandals such as SATYAM came to the fore.The need for urgent reforms within the auditor and audit committee regulations is pressing ass highlighted by the researchers with need for more stringency in action as shown in case of ICAI, the apex Chartered Accountants Body is failing in discharging its expected functions .Further the researchers have tried to pour in suggestions similar to what the Asian Corporate Governance

[86]Rule no. 33-8183 of 2003
[87]Section 144 of the Companies Act, 2013.

Association,Hong Kong had proposed back in 2010 with repect to auditing and accounting practices in India. The researchers have also tried to take relevant suggestions of the Uday Kotak Committee in suggesting for taking immediate steps to ensure auditor independence ,something which sounds very ironical.

With the respect to the issue of independence of the auditors , the researcher suggest that the role of independent auditing in making the markets well regulated and efficient does not need to be exaggerated. It is only the independent audit which enhances the authenticity and reliability of the financial statements. It lies at the core of the accounting and auditing profession on which the infrastructure of respect for the profession is built upon.[88] Any sacrifice with the fundamental stone of independence may cause the entire superstructure of the profession of auditors to fall apart. The legislatures in different jurisdictions have taken wide range of steps in order to augment the instances that encroach upon the independence of the auditors such as restrictions on the discharge of non-auditing services by the auditors, compulsory rotation of the auditors and others to discard threats of self-interest, self-review and familiarity threat to independence of auditors. All this has been done in order to prevent the auditing process from being reduced to a futile practice and to restore the dignity and confidence of the public in the profession of auditors by according the supreme attention to retain objectivity and independence in the approach of auditors while auditing the financial statements of an entity.

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