



CONSULTATIVE PAPER ON POLICY PROPOSALS WITH
RESPECT TO RESIGNATION OF STATUTORY AUDITORS
FROM LISTED ENTITIES

A. Background and rationale for review

1. There have been a significant number of instances of abrupt resignation of Statutory Auditors from listed entities in recent times. In most of the cases, the statutory auditors have suddenly resigned without completing their assignments for the year, generally citing 'pre-occupation' as the reason for resignation.
2. Auditors play a significant role in ensuring unbiased, accurate, complete and timely disclosures of various information to investors and other stakeholders in the securities market. The investors in listed entities rely on the audited financial results for taking their investment decisions.
3. Resignation of an auditor is understandable in exceptional circumstances where, as per the auditing standards, "*the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation.*" However, resignation of an auditor due to reasons such as pre-occupation before completion of the audit of the financial results for the year seriously hampers the investor confidence and leaves the investors with lack of reliable information for taking their financial decisions.

B. Current regulatory provisions

Disclosure of reasons for resignation of auditors

1. Under Sec 140(2) of the Companies Act, 2013, the auditor who has resigned from the company is required to file a statement in the prescribed form with the company and the Registrar within 30 days from the date of resignation. The reasons for resignation are also required to be disclosed in the prescribed form for resignation which is required to be filed by the auditor under the Companies (Audit and Auditors) Rules, 2014.
2. Based on the recommendations of the Kotak Committee, amendments have been made to SEBI LODR Regulations requiring listed entities to disclose to the stock exchanges, detailed reasons for the resignation of auditor, as given by the auditor, within 24 hours. These amendments are effective from April 1, 2019.

Role of the Audit Committee

SEBI LODR Regulations prescribe a broad role for the Audit Committee in this matter which, *inter-alia*, includes the following:



- i. reviewing and monitoring the auditor's independence and performance, and effectiveness of audit process.
- ii. reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.
- iii. discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern.

ICAI's auditing standards (SA-705)

ICAI's auditing standards provide for situations under which an auditor may qualify the opinion, resign from the audit, disclaim an opinion, etc. The relevant extract is reproduced below:

"If the auditor is unable to obtain sufficient appropriate audit evidence, the auditor shall determine the implications as follows:

(a) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive, the auditor shall qualify the opinion; or

(b) If the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive so that a qualification of the opinion would be inadequate to communicate the gravity of the situation, the auditor shall: (Ref: Para A13-A14)

(i) Resign from the audit, where practicable and not prohibited by law or regulation; or

(ii) If resignation from the audit before issuing the auditor's report is not practicable or possible, disclaim an opinion on the financial statements.

If the auditor resigns as contemplated by paragraph 13(b)(i), before resigning, the auditor shall communicate to those charged with governance any matters regarding misstatements identified during the audit that would have given rise to a modification of the opinion. (Ref: Para. A15)"

C. Policy proposals:

These policy proposals focus primarily on the following two aspects with respect to resignation of auditors:

- a. Strengthening disclosures to investors
- b. Strengthening and clarifying the role of the Audit Committee

Strengthening disclosures to investors



1. It is seen that the commonly cited reason by the auditors while resigning is 'pre-occupation'.
2. Further, several auditors continue to resign before fulfilling their responsibilities of completing the assignments for the quarter/half year/ year. This leaves the investors and stakeholders with lack of reliable information for making better financial decisions.
3. Therefore, in order to enhance responsible behavior of auditors and strengthen the disclosures to investors and stakeholders, the following is proposed:
 - a. Conditions prior to resignation: If the auditor of a listed entity/ material unlisted subsidiary of the listed entity proposes to resign:
 - i. With respect to auditor of a listed entity-
 1. If the auditor has signed the audit report for all the quarters (*limited review/ audit*) of a financial year, except the last quarter, then the auditor shall finalize the audit report for the said financial year before such resignation.
 2. In all other cases, the auditor shall issue limited review/audit report for that quarter before such resignation (*i.e. previous quarter in reference to the date of resignation*).

Illustration: If the auditor of a listed entity makes a decision to resign in August 2019, the auditor shall issue the limited review/ audit report for the quarter ended Sep 30, 2019 before such resignation.
 - ii. With respect to the auditor of a material unlisted subsidiary of the listed entity, the auditor shall issue the limited review/audit report for that financial year/ quarter, as applicable, before such resignation (*i.e. previous financial year/ quarter in reference to the date of resignation*).

Illustration: If the auditor of a material subsidiary of the listed entity makes a decision to resign in Feb 2020, the auditor shall issue the audit report for the financial year ended Mar 31, 2020 before such resignation.
 - iii. If the reason for the auditor's resignation is the entity not providing information, the auditor shall provide an appropriate disclaimer in the audit report to that extent.

Explanation: The disclaimer as specified in this clause may be in accordance with the Standards of Auditing as specified by ICAI.

The proposed amendments to SEBI LODR Regulations on the above lines are placed at **Annex-A**.



b. Format of resignation:

- i. On resignation by a statutory auditor of a listed entity/ its material unlisted subsidiary before the completion of the term, it is proposed to require the auditor to submit details in a prescribed format which would include:
 1. Detailed reasons for resignation;
 2. Declaration by the auditor that there are no other material reasons other than those provided (similar to the requirement in case of resignation of independent directors);
 3. In case of any concerns, efforts made by the auditor prior to resignation (including approaching the Audit Committee).

- ii. The following information is also proposed to be included in the format if the auditor's resignation is because information was not made available to the auditor:
 1. Details of the information requested by the auditor which was not provided;
 2. Whether the inability to obtain sufficient appropriate audit evidence was due to a management-imposed limitation or circumstances beyond the control of the management;
 3. The auditor's assessment of the materiality - whether the lack of information would have significant impact on the financial statements/results.
 4. Whether the auditor could have performed alternative procedures to obtain appropriate evidence for the purposes of audit/limited review;
 5. Whether the auditor communicated the matter to the Audit committee / board (where Audit Committees are not mandated), as applicable before resignation;
 6. Whether the lack of information was prevalent in the previous reported financial statements/results. If yes, the basis of issuing previous audit/limited review ;
 7. The extent of audit/limited review work performed by the auditor prior to resignation.

The proposed format of disclosure of the resignation letter on the above lines is placed at **Annex-B**.

- iii. The listed entity shall ensure disclosure the aforesaid resignation letter to the stock exchanges. In case of resignation by the auditor of a material unlisted subsidiary, the subsidiary shall disclose the resignation letter to the listed entity which shall, in turn, disclose the same to the stock exchanges.

c. Disclosure of views of Audit Committee and the Board of Directors- It is proposed that the views of the Audit Committee and the Board of



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Securities and Exchange Board of India

Directors (of the listed entity/ unlisted material subsidiary, as applicable) be required to be submitted to the stock exchanges along with the disclosure of the resignation letter of the auditor in the aforesaid prescribed format.

Strengthening and clarifying the role of the Audit Committee:

1. While the broad role of the Audit Committee of the listed entity is already specified under SEBI LODR Regulations, there is no specific procedure laid down that is to be followed by the auditor or the Audit Committee, when there are significant concerns leading to the auditor resignation.
2. In order to strengthen the role of the Audit Committee in the matter, it is proposed to issue a circular/amend SEBI LODR Regulations, specifying the following as the procedure that may be followed in such cases:
 - i. The auditor shall approach the Chairman of the Audit Committee directly and immediately in case of any concerns with the management such as non-availability of information / any non-co operation by the management. The auditor shall not specifically wait for the quarterly meetings to take place in order to raising such concerns.
 - ii. The auditor shall bring to the Audit Committee’s notice, all the concerns the auditor has with respect to such resignation, along with relevant documents. In cases where the resignation is due to non-receipt of information / explanation from the company, the auditor shall enlighten the Audit Committee of the details of information / explanation sought and not provided by the management, as applicable.
 - iii. The Audit Committee shall deliberate on the matter and communicate its views to the management and the auditor. In communicating its views, the Audit Committee shall ensure that it fulfils its role as specified under the SEBI LODR Regulations. The listed entity shall ensure the disclosure of the Audit Committee’s views to the Stock Exchanges.

D. Public comments

Comments on the above framework may be sent on or before August 08, 2019 in the following format:

Name of entity / person / intermediary/ Organization:			
Sr. No.	Issues	Suggestions	Rationale



Comments may be sent:

1. By email to Shri. Pradeep Ramakrishnan, GM at pradeepr@sebi.gov.in and/or Ms. Nila Salil Khanolkar, AGM (nila@sebi.gov.in) / Shri. Rajnish Prasad, AM (rajnishp@sebi.gov.in); or
2. By post to the following address:

Ms. Nila Salil Khanolkar
Assistant General Manager
Corporation Finance Department, CMD-I,
Securities and Exchange Board of India
SEBI Bhavan, Plot No. C4- A, "G" Block,
Bandra Kurla Complex, Bandra (East),
Mumbai - 400 051



Annex-A

Proposed amendments to SEBI LODR Regulations (with immediate effect):

Current provision in SEBI LODR Regulations	Proposed amended provision in SEBI LODR Regulations
No Specific provision	<p><u>Insertion of sub-regulation 33(9) :</u></p> <p><u>Conditions prior to resignation:</u></p> <p>33(9): If the auditor of a listed entity/ material unlisted subsidiary of the listed entity proposes to resign:</p> <ul style="list-style-type: none">a. With respect to auditor of a listed entity-<ul style="list-style-type: none">i. If the auditor has signed the audit report for all the quarters (<i>limited review/ audit</i>) of a financial year, except the last quarter, then the auditor shall finalize the audit report for the said financial year before such resignation.ii. In all other cases, the auditor shall issue limited review/audit report for that quarter before such resignation (i.e. previous quarter in reference to the date of resignation).b. With respect to the auditor of a material unlisted subsidiary of the listed entity, the auditor shall issue the limited review/audit report for that financial year/ quarter, as applicable, before such resignation (i.e. previous financial year/ quarter in reference to the date of resignation).c. If any information is not provided to the auditor, to that extent, the auditor shall provide an appropriate disclaimer in the audit report. <p><u>Explanation:</u> The disclaimer as specified in this clause may be in accordance with the Standards of Auditing as specified by ICAI.</p>



Annex-B

Format of resignation letter by a statutory auditor

1. Name of the listed entity/ material unlisted subsidiary:
2. Details of the statutory auditor:
 - a. Name:
 - b. Address:
 - c. Phone number:
 - d. Email:
3. Details of association with the listed entity/ material unlisted subsidiary:
 - a. Date on which the statutory auditor was appointed:
 - b. Date of which the term of the statutory auditor was scheduled to expire:
4. Detailed reasons for resignation:
5. In case of any concerns, efforts made by the auditor prior to resignation (including approaching the Audit Committee):
6. In case the information requested by the auditor was not provided, then following shall be disclosed.
 - a. Whether the inability to obtain sufficient appropriate audit evidence was due to a management-imposed limitation or circumstances beyond the control of the management.
 - b. Whether the lack of information would have significant impact on the financial statements/results.
 - c. Whether the auditor could have performed alternative procedures to obtain appropriate evidence for the purposes of audit/limited review
 - d. Whether the auditor communicated the matter to the Audit committee before resignation
 - e. Whether the lack of information was prevalent in the previous reported financial statements/results. If yes, on what basis the previous audit/limited review reports were issued.
 - f. Prior to resignation, the extent of audit/limited review work performed by the auditor.
7. Any other facts relevant to the resignation:

Declaration

1. *I/ We hereby confirm that the information given in this letter and its attachments is correct and complete.*
2. *I/ We hereby confirm that there is no other material reason other than those provided above for my resignation/ resignation of my firm.*

Signature of the authorized signatory

Date:

Place:

Encl: