Forensic Audits

Why in news?

The Securities Exchange Board of India (SEBI) has made minor tweaks to different laws.

What has been changed?

- These tweaks could go a long way in strengthening the safeguards for public investors in listed shares and bonds.
- The most important of these is the requirement for all listed entities to make compulsory disclosures to the stock exchanges.
- It initiated any forensic audits into their books along with the reasons for commissioning them.
- On completion, the final audit reports along with management comments need to be filed with the exchanges too.

What does this move mean?

- This is a welcome move because the initiation of a forensic investigation and an explanation on whether it was initiated by the regulator or the company's own Board, is price-sensitive information.
- It has a bearing on one's decision to invest in a stock.
- Making full public disclosures of forensic audit reports as soon as they are submitted is essential too.
- This would do away with insider trading and stock price manipulation based on half-baked leaks from such reports.

What happened in the past?

- In the past, listed companies such as ICICI Bank and Infosys have seen sharp stock price volatility.
- This happened after whistle-blowers accused their top managers of governance infractions.
- Their Boards, after initiating internal forensic audits, claimed that the auditors had unearthed no irregularities citing selective extracts.
- DHFL, after a sting operation by a media outlet, commissioned a forensic study by an auditor who promptly gave it a clean chit.
- A subsequent audit commissioned by the regulator unearthed evidence of

widespread diversion of loan funds.

What is the significance of public disclosure?

- Disclosing forensic audit reports to the public would remove all scope for selective interpretations.
- It allows analysts and investors in a company to make up their mind for themselves.
- Disclosing will prove instructive to investors and policymakers on the modus operandi used by fraudsters to divert public money.

What could be done?

- For better protection to bond and mutual fund investors, SEBI must extend the requirement on making forensic audit reports public to,
    1. Entities with listed shares,
    2. Entities with listed debentures and
    3. Entities dealing with public money in a fiduciary capacity — be it asset managers or rating agencies.
- The regulators such as SEBI and RBI should set an example by publishing the findings of these reports.

Source: Business Line

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