MCA Paper on Auditing

What is the issue?

- The Ministry of Corporate Affairs (MCA) published a consultation paper whose success is predicated on a strong framework, engagement, etc.
- This article will examine certain key concepts that impacts audit quality, the central theme of the MCA paper.

Why it recommended audit reporting on subsidiaries' accounts?

- The paper tries to avoid the negative consequences of an auditor not having visibility over a corporate group.
- So, it wants a mandatory comment from the parent's auditor on its subsidiaries' accounts, which is inefficient in achieving this visibility.
- **Solution** - Replace the current national standard that allows reliance on the work of other auditors with the international standard ISA 600.
- [ISA 600 - Does not permit division of responsibility between auditors of the holding and subsidiary companies.]

What the paper wants to restrict the audit firm composition?

- The MCA paper considers limiting the number of audits and partners for a firm to improve quality.
- But, the market really wants **capacity building** i.e. larger firms with experience and diverse skill sets to serve large companies.
- Such firms will be better able to integrate their resources and respond to emerging complexities in the framework and technology.
- To achieve this quickly, smaller firms with varied capabilities need to consolidate, creating a positive correlation between larger firms and improved audit quality.

Why the paper wants to implement AQI?

- The MCA paper wants to implement the Audit Quality Index (AQI), as it rates each auditor considering qualitative and quantitative factors.
- AQI will help companies, including the unlisted ones, to identify the firms or auditors most suited to audit them.
- Relevant parameters need to be added in developing the AQI framework, complemented by specific needs of the companies or audit committees.

- If implemented properly, the AQI will lead to consolidation of smaller firms and building capacity, resulting in a natural "panel" of firms, without regulator intervention.
- It also means fewer firms for the regulator to regulate, leading to better quality regulation.

Why continuous engagement needs to be ensured?

- A greater engagement can repair the significant trust deficit between auditors and regulators.
- The paper recommends deterring improper audits through inspection that is indeed the right direction.
- Auditing involves the application of skill, expertise, judgement and experience; and goes beyond a checklist.
- Therefore, inspections should be robust and carried out by competent and experienced auditors.
- Auditors should go beyond audit files to cover the firm's quality-related processes.
- The auditor needs to know that the regulator is engaged, aware, and constantly monitoring the auditor.

Source: Business Standard

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