

---

## **Role of Independence in Ethics for SMP Accountants**

**CA. KISHORE S PESHORI**

*Department of Accountancy, Smt. Chandibai Himathmal College, Ulhasnagar.*

*“Ethics is all about our becoming and feeling responsible about everything that is around us. We are responsible only when we appreciate everything that is ethical and denounce all that is not ethical around us. I would like our membership to ensure that they always go for the stricter interpretation, foregoing the liberal one wherever and whenever they realise a presence of two interpretations on a matter of professional interest, despite both being legal. Such a courageous display of moral conduct will inspire not only generations of our professionals, but also those from other walks of life.” [Thomas More, in ‘Utopia’].*

*Past-President of ICAI, Shri R. C. Cooper also expresses the same feeling while writing the first preface to the ICAI’s Code of Ethics: ...practice of professional ethics is largely a matter of conscience and the determination of members to distinguish between what is right and wrong. Ethics is a state of the mind. He goes on to explain: ...there may be some acts which, though may not strictly fall under one of the items of the Schedule, may be one which may not be proper by any moral or ethical standards. Very intimately and yet with sincere concerns, he advises all of us to act in the larger interests of the Institute, and to search our hearts and conscience whenever in doubt.” (President of Institute Of Chartered Accountants of India in Editorial in ICAI Journal Of May 2013).*

*The increased pace of professional life, changing culture of business and paradigm shifts in regulations all around have brought the importance of ‘ethics’ to the fore. The need for professional accountants to practice ethics is herculean task, particularly for Small and Medium Practitioners (SMP) and that too, in developing countries where the life struggle for survival takes precedence over other values. The strength to practice ethics as expected stems from independence, one of the pillars of standards on quality of assurance services.*

*With unearthing of scams and Ponzi like schemes, the responsibility of audit and attest*

---

*functions have assumed importance like never before. Moreover in the modern era, where society is looking to auditors to discharge their attest function correctly, it is all the more important to ask whether the accountants are following literally and ethically, the rules set by society while discharging our responsibility. The importance of independence in discharge of attest function also needs to be evaluated with the measures that need to be adopted by accountants, society as well as regulators.*

*The paper will Focus on what is professional ethics and role of independence while conducting the audit and such attest function particularly by small and medium practioners in Indian metros. The research paper through questionnaire and sample study of published accounts of big companies, will conduct a survey of 50 SMP's and come to a finding of relevance of independence in professional ethics and the role of regulators in implementation and further suggest changes in code of ethics and regulations, if required based on findings*

**Key words:** *Audit, Auditor Independence, SMP, India, Regulators*

## **INTRODUCTION**

Ethics means moral values. The whole foundation of any profession is its credibility. The sole purpose of ethics is to ensure and uphold its credibility The concept of auditor independence changed during the late 19<sup>th</sup> and early 20<sup>th</sup> centuries. The concept of auditor independence has shifted in favor of objectivity and neutrality in reporting.

In India regulatory audit usually takes the following types:

- A) Corporate Audit: All corporates have to get their accounts audited compulsory
- B) Tax Audit: All assesses having turnover in Business exceeding specified Limit or Profession having Gross receipts exceeding specified limit have to get their books of accounts audited compulsorily
- C) Vat Audit: All dealers whose turnover exceed specified limit have to get their books audited by Chartered Accountant
- D) Audits of other entities required to be carried out under the statute regulating such entity, like Audit of Public Charitable Trust, Audit of Co-operative society, Audit of

---

societies registered under Societies Registration Act, 1860.

The Institute Of Chartered Accountants of India has been regulating the Profession since 1949. A member of ICAI may either be an Associate Chartered Accountant (A.C.A.) or a Fellow Chartered Accountant (F.C.A.) based on his experience. Further based on holding Certificate of Practice, they may also be classified as practicing and non-practicing Chartered Accountants. As of 29 June 2013, the Institute has 220,738 members out of which 146,365 are Associates and 74,373 are Fellows. The Small and Medium Practitioners in India, besides being in traditional audits render various types of managerial, taxation and related consultancy.

Gill and Cossoral (1996) have emphasized that independence is the cornerstone of the auditing profession. In absence of independence, the stature of profession will be of no or less value to the stakeholders. The reliance of audit report by the stakeholders or third party implies that an audit process is independent within its regulatory framework. Auditor independence can be defined as a reference to the independence of internal or external auditors from parties that might have a financial interest in the business being audited. The true benefits of audit are expected to flow from the independence of auditor conducting the audit in a free and fair manner.

The use of the word “independence” on its own may create misunderstandings. Standing alone, the word may lead observers to suppose that a person exercising professional judgment ought to be free from all economic, financial and other relationships. However, this is impossible, as every member of society has relationships with others. Therefore, the significance of economic, financial and other relationships should also be evaluated in the light of what a reasonable and informed third party having knowledge of all relevant information would reasonably conclude to be unacceptable. Professional integrity and independence is an essential characteristic of all the professions but is more so in the case of accountancy profession. Independence implies that the judgment of a person is not subordinate to the wishes or direction of another person who might have engaged him, or to his own self-interest.

---

It is not possible to define "independence" precisely nor is it possible to implement it to the core. This has to be accepted as fact belying the audit. Rules of professional conduct dealing with independence are framed primarily with a certain objective. The rules themselves cannot create or ensure the existence of independence. Independence is a condition of mind as well as personal character and should not be confused with the superficial and visible standards of independence which are sometimes imposed by law. These legal standards may be relaxed or strengthened but the quality of independence remains unaltered. In India, regulator of audit profession, being Institute of Chartered Accountants of India, has time and again carried out various modifications so as to achieve the objective keeping the flexibility in ever changing laws and regulations governing the businesses.

There are two interlinked perspectives of independence of auditors, one, independence of mind; and two, independence in appearance.

The Code of Ethics for Professional Accountants, issued by International Federation of Accountants (IFAC) defines the term 'Independence' as follows:

"Independence is:

Independence of mind - the state of mind that permits the provision of an opinion without being affected by influences that compromise professional judgment, allowing an individual to act with integrity, and exercise objectivity and professional skepticism; and

Independence in appearance - the avoidance of facts and circumstances that are so significant a reasonable and informed third party, having knowledge of all relevant information, including any safeguards applied, would reasonably conclude a firm's, or a member of the assurance team's, integrity, objectivity or professional skepticism had been compromised."

Independence of the auditor has not only to exist in fact, but also appear to so exist to all reasonable persons. The relationship between the auditor and his client should be such that firstly, he is himself satisfied about his independence and secondly, no unbiased person would be forced to the conclusion that, on an objective assessment of the circumstances, there

---

is likely to be an abridgement of the auditors' independence.

In all phases of a Chartered Accountant's work, he is expected to be independent, but in particular in his work as auditor, independence has a special meaning and significance. Not only the client but also the stakeholders, prospective investors, bankers and government agencies rely upon the accounts of an enterprise when they are audited by a Chartered Accountant.

The idea of independence is instilled in the minds of Chartered Accountants from the commencement of their training under articles or audit service. It has to be applied in their day-to-day work and their success is dependent entirely upon their integrity, competence and independence of approach.

Dependent as it is on the state of mind and character of a person, independence, is a very subjective matter. One person might be independent in a particular set of circumstances, while another person might feel he is not independent in similar circumstances. It is therefore the duty of every Chartered Accountant to determine for him whether or not he can act independently in the given circumstances of a case and quite apart from legal rules, in no case to place him in a position which would compromise his independence.

The auditor should be straight-forward, honest and sincere in his approach to his professional work. He must be fair and must not allow prejudice or bias to override his objectivity. He should maintain an impartial attitude and both be and appear to be free of any Interest which might be regarded, whatever its actual effect, as being incompatible with integrity and objectivity. This is not self-evident in the exercise of the reporting function but also applies to all other professional work. In determining whether a member in practice is or is not seen to be free of any interest which is incompatible with objectivity, the criterion should be whether a reasonable person, having knowledge of relevant facts and taking into account the conduct of the member and the member's behaviour under the circumstances, could conclude that the member has placed himself in a Position where his objectivity would or could be impaired.

While performing audit functions, maintaining quality control is the objective of the quality

---

control and policies to be adopted by an Auditor shall ordinarily incorporate the following:

(a) Professional Requirements: Personnel in the firm are to adhere to the principles of Independence, Integrity, objectivity, Confidentiality and Professional Behaviors.

(b) Skills and Competence: The firm is to be staffed by personnel who have attained and maintained the technical standards and professional competence required enabling them to fulfill their responsibilities with due care.

(c) Assignment: Audit work is to be assigned to personnel who have the degree of technical training and proficiency required in the circumstances.

(d) Delegation: There is to be sufficient direction, supervision and review of work at all levels to Provide reasonable assurance that the work Performed meets appropriate standards of quality.

(e) Consultation: Whenever necessary, consultation within or outside the firm is to occur with those who have appropriate expertise.

(f) Acceptance and Retention of Clients: An evaluation of prospective clients and a review, on an ongoing basis of existing clients is to be conducted in making a decision to accept or retain a client; the firm's independence and ability to serve the client properly are to be considered.

(g) Monitoring: The continued adequacy and operational effectiveness of quality control policies and procedures is to be monitored.

Thus a member performing professional work must recognize the problems created by personal relationships or financial involvement, which by reason of their nature or degree might threaten his independence.

Standing alone, the word "Independence" may lead observers to suppose that a person

---

exercising professional judgment ought to be free from all economic, financial and other relationships. This is impossible, as every member of society has relationships with others. Therefore, the significance of economic, financial and other relationships should also be evaluated in the light of what a reasonable and informed third party having knowledge of all relevant information would reasonably conclude to be unacceptable.

Many different circumstances, or combination of circumstances, may be relevant and accordingly it is impossible to define every situation that creates threats to independence and specify the appropriate mitigating action that should be taken. In addition, the nature of assurance engagements may differ and consequently different threats may exist, requiring the application of different safeguards. A conceptual framework that requires chartered accountants to identify, evaluate and address threats to independence, rather than merely comply with a set of specific rules in the public interest.

#### **TREATS TO INDEPENDENCE**

The Code of Ethics for Professional Accountants, prepared by the International Federation of Accountants (IFAC) identifies five types of threats. These are:

Self-interest threats, which occur when an auditing firm, its partner or associate could benefit from a financial interest in an audit client. Examples include (i) direct financial interest or materially significant indirect financial interest in a client, (ii) loan or guarantee to or from the concerned client, (iii) undue dependence on a client's fees and, hence, concerns about losing the engagement, (iv) close business relationship with an audit client, (v) potential employment with the client, and (vi) contingent fees for the audit engagement.

Self-review threats, which occur when during a review of any judgment or conclusion reached in a previous audit or non-audit engagement, or when a member of the audit team was previously a director or senior employee of the client. Instances where such threats come into play are (i) when an auditor having recently been a director or senior officer of the company, and (ii) when auditors perform services that are themselves subject matters of audit.

---

Advocacy threats, which occur when the auditor promotes, or is perceived to promote, a client's opinion to a point where people may believe that objectivity is getting compromised, e.g. when an auditor deals with shares or securities of the audited company, or becomes the client's advocate in litigation and third party disputes.

Familiarity threats are self-evident, and occur when auditors form relationships with the client where they end up being too sympathetic to the client's interests. This can occur in many ways: (i) close relative of the audit team working in a senior position in the client company, (ii) former partner of the audit firm being a director or senior employee of the client, (iii) long association between specific auditors and their specific client counterparts, and (iv) acceptance of significant gifts or hospitality from the client company, its directors or employees.

Intimidation threats, which occur when auditors are deterred from acting objectively with an adequate degree of professional skepticism. Basically, these could happen because of threat of replacement over disagreements with the application of accounting principles, or pressure to disproportionately reduce work in response to reduced audit fees.

### **SAFEGUARDS TO INDEPENDENCE**

The Chartered Accountant has a responsibility to remain independent by taking into account the context in which they practice, the threats to independence and the safeguards available to eliminate the threats.

To address the issue, Members are advised to apply the following guiding principles: -

For the public to have confidence in the quality of audit, it is essential that auditors should always be and appears to be independent of the entities that they are auditing.

In the case of audit, the key fundamental principles are integrity, objectivity and professional scepticism, which necessarily require the auditor to be independent.

Before taking on any work, an auditor must conscientiously consider whether it involves



---

threats to his independence.

When such threats exist, the auditor should either desist from the task or, at the very least, put in place safeguards that eliminate them. All such safeguards measure needs to be recorded in a form that can serve as evidence of compliance with due process.

If the auditor is unable to fully implement credible and adequate safeguards, then he must not accept the work.

In order to ensure independence, the law has made certain provisions which either prohibit the appointment of a person as auditor in certain circumstances or place certain restrictions on his appointment as auditor or put third parties on guard against the possibility of an abridgement of independence by requiring certain disclosures to be made. These provisions are briefly outlined below:

1 Section 226 of the Companies Act, 1956 prohibits the appointment of a Chartered Accountant as auditor of a Company if he is:

- (i) an officer or employee of the Company;
- (ii) a partner of a person in the employment of an officer or of an employee of the Company;
- (iii) a person who is indebted to the company for an amount exceeding Rs. 1000;
- (iv) a person who has given any guarantee or provided any security in connection with the indebtedness of any third person to the company for an amount exceeding Rs. 1000;
- (v) a person holding any security of that company.

2 A person who is disqualified from becoming auditor of any body corporate under the above rules is also disqualified from appointment as auditor of such body's subsidiary, co-subsiary or holding company.

3. Section 314 of the Companies Act, 1956 makes separate provision for the case where an

---

auditor of a Company (whether public or private) is a relative of a director, or manager of a private company of which the director of the company is a director or member. In the case of such a person he may be appointed as auditor of a company only if such appointment is approved with the consent of the company in general meeting obtained by a special resolution.

4. It will be observed from the above that the Act has specifically provided for cases where the independence of an auditor maybe affected by his connection with the company and prohibited or restricted him from acting as auditor under those circumstances.

5 A question often arises as to whether an indebtedness (as referred in para (iii) above) arises in cases where in accordance with the terms of his engagement by a client (e.g. resolution passed at the general meeting) the auditor recovers his fees on a progressive basis as and when a part of the work is done without waiting for the completion of the whole job. In these circumstances, where in accordance with such terms the auditor recovers his fees on a progressive basis he cannot be said to be indebted to the company at any stage.

6 A question of indebtedness may also be raised where an auditor of a company purchases goods or services from a company audited by him. In such a case, if the amount outstanding exceeds Rs.1000/- irrespective of the nature of the purchase or period of credit allowed to other customers the provisions concerning disqualification of auditor as contained in Section 226 (3)(d) of the Companies Act, 1956 will be attracted.

7 Another question which arises for consideration is whether a partner is disqualified from appointment as auditor when the firm of which he is a partner is indebted to the company in excess of the limit prescribed and whether the firm is disqualified from appointment as auditor when a partner of the firm is indebted in excess of the prescribed limit. In both cases, the disqualification will apply, because when a firm is appointed as auditor, each partner is deemed to be so appointed and when a firm is indebted, each partner is deemed to be indebted.

8 There may also be situations in which, though the appointment is in the individual name

---

of a partner, the work, is, in fact, carried out by the firm and the fees are credited to the account of the firm. In such situations, the firm will be deemed to be acting as auditor and the disqualification will be attracted.

Apart from above, the provisions of ensuring independence also is included in laws regulating other forms of entities as detailed below:

#### Maharashtra Public Trust Act

A reference can be made to the provisions of section 33(2) which require:

33(2) – The accounts shall be audited annually by a person who is a chartered accountant within the meaning of the Chartered Accountants Act, 1949 or by such persons as the State Government ,may, subject to such conditions, authorise in this behalf Provided that no such person is in any way interested in or connected with public trust.

Similar provisions exists in Societies Registration Act, 1860 in sub-section (4) of section 12D as follows – 12D. Maintenance of accounts and their balancing and auditing

(4) The accounts shall be audited annually in such manner as may be prescribed by rules and by a person who is a chartered accountant within the meaning of the Chartered Accountants Act, 1949 or by such other persons as may be authorised in this behalf by the State Government.

Almost similar provisions exist in Multi State Co-operative Societies Act, 2002 governing all the co-operative societies operating in the country in section 72 .

Thus, it would be pertinent to note that the provisions of retaining ‘independence’ of auditor exist in almost all the laws regulating different forms of business entities and in any case, the regulators have referred and relied on the regulator of auditing profession in India, viz. The Institute of Chartered Accountants of India for ensuring such independence and disqualifications flowing from non-compliance thereof.

Provisions contained under the Chartered Accountants Act, 1949, Chartered Accountants

---

Regulations, 1988 and under Code of Ethics to ensure Independence of Auditors

1 Clauses (10) of Part I of the First Schedule to the Chartered Accountants Act, 1949 prohibits acceptance of, what have been described as contingent fees, i.e., fees, which are either based on percentage of profits or otherwise dependent on the finding or the results of employment.

2 What distinguishes a profession from a business is that professional service is not rendered with the sole purpose of a profit motive. Personal gain is one but not the main or the only objective. Professional opinion, therefore, frowns upon methods where payment is made to depend on the basis of results. It is obvious that a person who is to receive payment in direct proportion to the benefit received by his client, may be tempted to exaggerate the advantage of his service or may adopt means which are not ethical. It will have the effect of undermining his integrity and impairing his independence. Therefore, the members are prohibited from charging or accepting any remuneration based on a percentage of the profits or on the happening of a particular contingency such as, the successful outcome of an appeal in revenue proceedings.

3 Professional services should not be offered or rendered under an arrangement whereby no fee will be charged unless a specified finding or result is obtained or where the fee is otherwise contingent upon the findings or results of such services. However, fee should not be regarded as being contingent if fixed by a Court or other public authority.

4 The Council of the Institute has framed Regulation 192 which exempts members from the operation of this Clause in certain professional services regarding restriction on fees on a percentage of profits.

Attention of the members is invited to the provisions of Clause (4) of Part 1 of the second Schedule to the Chartered Accountants Act, 1949 which provides that a Chartered Accountant in practice shall be deemed to be guilty of professional misconduct if he expresses his opinion on financial statements of any business or any enterprise in which he, his firm or a partner in his firm has a substantial interest, unless he discloses his interest also

---

in his report.

If the opinion of auditors is to command respect and the confidence of the public, it is essential that they must disclose every factor which is likely to affect their independence. Since financial interest in the business can be one of the important factors, which may disturb independence, the clause provides that the existence of such an interest direct or indirect should be disclosed. This is intended to assure the public as regards the faith and confidences that could be reposed on the independent opinion expressed by the auditors.

The independence of mind is a fundamental concept of audit and/or expression of opinion on the financial statements in any form and, therefore, must always be maintained. Nothing can substitute for the essential and fundamental requirements of independence. . In fact, it is necessary that he should bear the same degree of integrity and independence of mind in all spheres of his work. Unless this is done, the accounts of companies audited by Chartered Accountants or statements made by them during the course of assessment proceedings would not be relied upon as correct by the authorities. The Members are not permitted to write the books of accounts of their auditee clients. A statutory auditor of a company cannot also be its internal auditor, as it will not be possible for him to give independent and objective report issued under sub-Section 4A of Section 227 of the Companies Act, 1956 read with the Companies (Auditors' Report) Order, 2003. Clause (8) of Part 1 of First Schedule to the Chartered Accountants Act, 1949. emphasized the requirement of mandatory communication with the previous auditor in all types of audit viz., statutory audit, tax audit, internal audit, concurrent audit or any kind of audit and it is equally applicable to audits of both government and non-government entities. Clause (9) of Part 1 of First Schedule to the Chartered Accountants Act, 1949 provided that an auditor of the company before accepting the appointment should ascertain from the auditor whether the requirements of Section 225 of the Companies Act, 1956 in respect of such appointment have been duly complied with. Section 224 of the Companies Act, 1956 contains several provisions in the matter of appointment of auditors in different circumstances and situations whereas Section 225 laid down the procedure which must be followed whenever a company desires to change its auditor. Also that the validity of the appointment of an auditor is not challenged or objected to by

---

shareholders or the retiring auditors at a later date, it has been made obligatory to ascertain from the company that the appropriate procedure in the matter of appointment has been faithfully followed. Independence of auditor is a concept to be addressed through its all the possible aspects and the message of Clause (8) & (9) is to ensure that an auditor should be conscious about this aspect from the very point of accepting the position of an auditor. The Council feels that there are adequate safeguards provided in the Companies Act, 1956 as well as in the Chartered Accountants Act, 1949. The Council is of the view that independence, being a state of the mind, is not necessarily affected by the fact of mere relationship any more than it should be existence if the relationship did not exist. In any case, lest there may be any feeling in the public mind that relationship would affect the independence of auditors, the Council suggests that where, due to near relationship of an auditor, with a Managing or a Whole-time Director the independence of an auditor is likely to be jeopardized, he should use his good sense, and acting in the best traditions of the profession, refrain from accepting the appointment.

If the opinion of chartered accountant is to command respect and the confidence of the public, it is essential that they must ensure their independence to assure the public as regards the faith and confidence that could be reposed on them. The Chartered Accountant should ensure his independence in all assurance services including concurrent audit, tax audit and internal audit. The chartered accountant should make it certain that his independence is not jeopardized. Where he feels that his independence is jeopardized, he should refrain from accepting the assignment. To be and to remain independent the auditor has to maintain high professional ethics. Given The background Of International Federation of Accountants and Institute Of Chartered Accountants of India it is time to test that whether ethics rule our profession and whether they help auditors to remain independent in todays globalized , competitive world. It is said by 2020, India would be having the largest number of accountants in the world so the object of research becomes more relevant to accounting profession at large

### **STATEMENT OF THE PROBLEM**

Financial reports as stated In Igben (1999) are meant to be formal record of business

activities and these reports are meant to provide an overview of the financial position and profitability in both short and long term of companies to the users of these financial statements such as shareholders, managers, employees, tax officials, banks etc. But in recent times there has been lot of financial scams in corporate and the world of governmental agencies. We had Common wealth, 2G , coal mine scams which were unearthed by the auditors at the same time we had scams like Satyam, NSEL where auditors have failed to unearth the scams. The most important scam which set the ball rolling was the Satyam. Analysts in India have termed the Satyam scandal India's own Enron scandal. Some social commentators see it more as a part of a broader problem relating to India's caste-based, family-owned corporate environment. Indian business practices are unique – and may give rise to ethical behavior that may or may not be compatible with the prevailing Western viewpoint. Indian business culture, puts a premium on favors, friendship and clanship. Friendship is highly valued, whether based on multigenerational family friendships, school friendships or personal friendships. Indian management style differs from that in the West: Decisions are made by the person at the top, not in a participatory way. This has led to increased responsibility on the auditors' role. The study tries to focus on the role of ethics in independence of auditor.

## **METHOD**

### Population, Sample and Sampling Procedure Of Study

Mumbai was selected as the representative region as Mumbai is financial capital of India. Many of the corporate offices are located in Mumbai and maximum number of Chartered Accountants is in Mumbai who are Small and medium practicing accountants carrying out corporate and tax audits. The population size was Practicing Chartered Accountants (Small and Medium Practitioners) in Mumbai. The sampling method was random distribution of questionnaires among various chartered accountants in Mumbai via email and personal contacts. Table I shows the number of questionnaires distributed and the response collected

Particulars	Total Administered	Total Responded
No. of questionnaires sent on	100	Nil

---

Email		
No. of questionnaires sent through contacts	100	70
Total	200	70

It was found that the email was not attracting any responses. The reasons for the same can be that the respondents were not familiar with the researcher and therefore were hesitant to respond or they were not having sufficient time to reply.

### **RESEARCH INSTRUMENTS**

The study made use of primary and secondary data. Concerning the primary source the questionnaire was used to collect the data. The questionnaire was divided into seven parts

Part I consisted of Personal details and it had five questions

Part II consisted of Profile analyses. It had eight sub questions. The purpose was to know:

- A. Nature of Audits carried out i.e. Tax audit, Corporate audit, Vat audit, other assignment
- B. Bifurcation of total revenue into assurance and non-assurance service for last 3 years
- C. Percentage of client for assurance, consultancy services,

Part III consisted of two questions to test awareness of ethics

Part IV consisted of seven questions relating to appointment

Part V consisted of seven questions relating to competition and its effect on ethics

Part VI consisted of three questions on the effect of Peer review and its effects on ethics

Part VII consisted of five questions on the effect of other influences on ethics

Part VIII consisted of seven questions on the role of stakeholders in making ethics effective.



**FINDINGS:**

**Part I:** The Following was the status of organization which is shown in Table 2.1.

Status of Organisation	Number of Firms
Proprietary	34
Partnership(Refer Table 1.2)	36
Total	70

**Table 2.1**

The analysis is based therefore on the sample size of equal number of respondents of proprietary & partnerships concerns. In India, SMPs are not allowed to be corporate. The structure of partnership firms is highlighted in Table 2.2.

Firms Having Number of Partners	Number of Firms	%
Two	7	19
Three	19	53
Four	5	14
Five	2	5
Six	3	9
Total	36	100

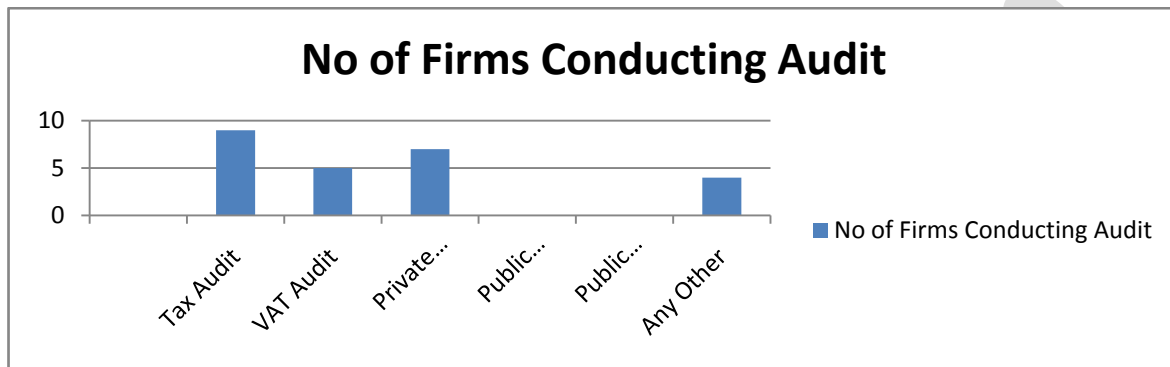
**Table 2.2**

74% of the firms were having 3 or less partners. The average size of SMP can therefore be of maximum 3 partners.

**Part II: Profile Analysis**

On number of audits only 22% respondents replied to the questions i.e. only 15 respondents replied to number of audits. Majority of them i.e. all respondents were doing Tax Audit.

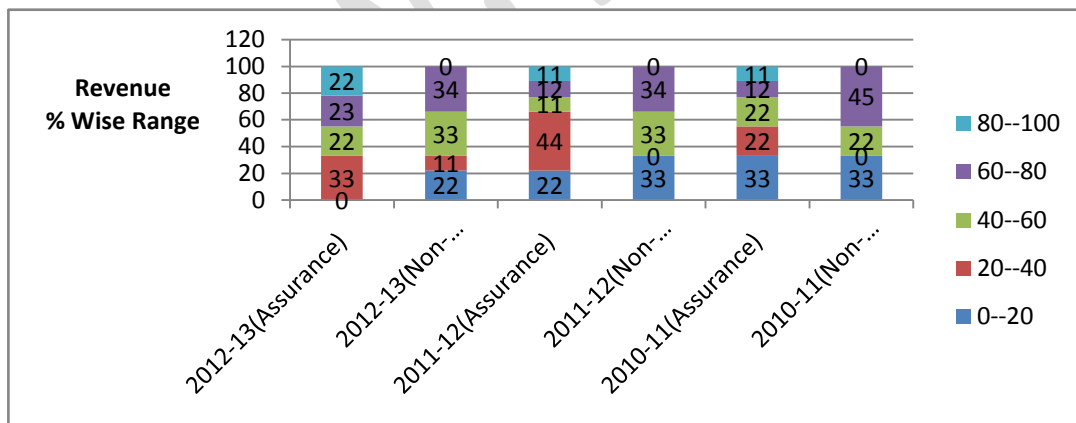
There were 2 firms who had reached the maximum limit of 45. 44% of the 15 respondents i.e. four firms who were not involved in VAT audit. 80% of the above responses i.e. Twelve firms were conducting audit of private limited companies. The audit of public limited companies was not conducted by any of the respondents. There were one third firms which were involved in any other audit i.e. audit of NGOs. The profile is illustrated in form of Bar Chart in Table 3.1.



**Bar Chart 3.1**

Only 22% respondents gave reply to total revenue % for last three years.

The same is illustrated in Table 3.2.



**Table 3.2: Year wise Revenue Breakup**

There are only few firms who are relying totally on assurance service as part of revenue. Majority of the firms were offering both assurance & Non-assurance services. It is also seen

---

that the percentage of revenue has increased of Non-assurance services as compared to Assurance services.

Only twelve percent of firms i.e. 8 firms responded to nature of services offered to the clientele. All firms who responded offered both the services to client i.e. assurance and non-assurance services. There were two firms which offered 50% of both the services to the clientele. In rest cases it was only 10% to 30%

Of assurance services, the remaining were focused on non-assurance services.

### **Part III: Awareness of ethics:**

Only Three percent of respondents were not aware of professional ethics. 83% of the respondents said their awareness of ethics was on average basis. This can be also supplemented where we asked the second question on the number of schedules where 30% of respondents answered incorrect.

### **Part IV: Ethics & Appointment**

The respondents were asked on the way in which they sought assurance engagement. 68% of respondents said they got audit through Acquaintance or Empanelment. Only 1% of respondents said they got audit only through Tender. In other words the engagement of audit was through acquaintance only.

After engagement it is necessary to communicate with previous auditor as per Code of Ethics. All the respondents agreed with this view.

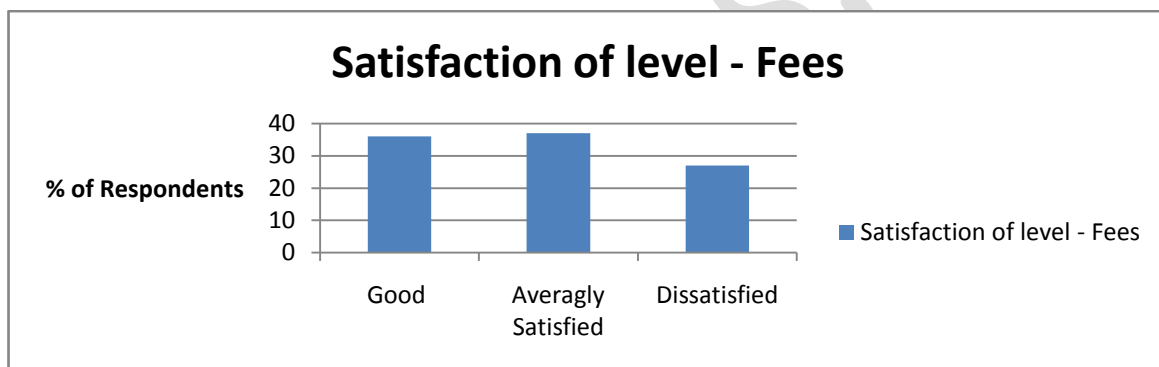
In Code of Ethics it is stated the audit of books of account should not be done where relative of auditor is partner or director. 17% of respondents agreed with this view. Thus, practically majority of respondents felt that the acquaintance does not affect the assurance services. 87% of respondents communicate always with previous auditor before accepting the assignment.

17% of respondents carried out audit of their relatives. 90% of respondents rendered many services to a single client. 60% of respondents gave letter of engagement to the client.

35% of respondents felt that the independence is compromised in case where more services are rendered to a single client.

**Part V: Ethics & Competition:**

37% of the respondents said that independence is lost due to competition. 87% of respondents that independence is compromised in case of low paid fees. 80% of respondents felt that there is lot of importance of fees for maintaining independence in assurance service engagement. The level of satisfaction of assurance services and the level of fees received is shown in the chart given in Table 4:



**Table 4**

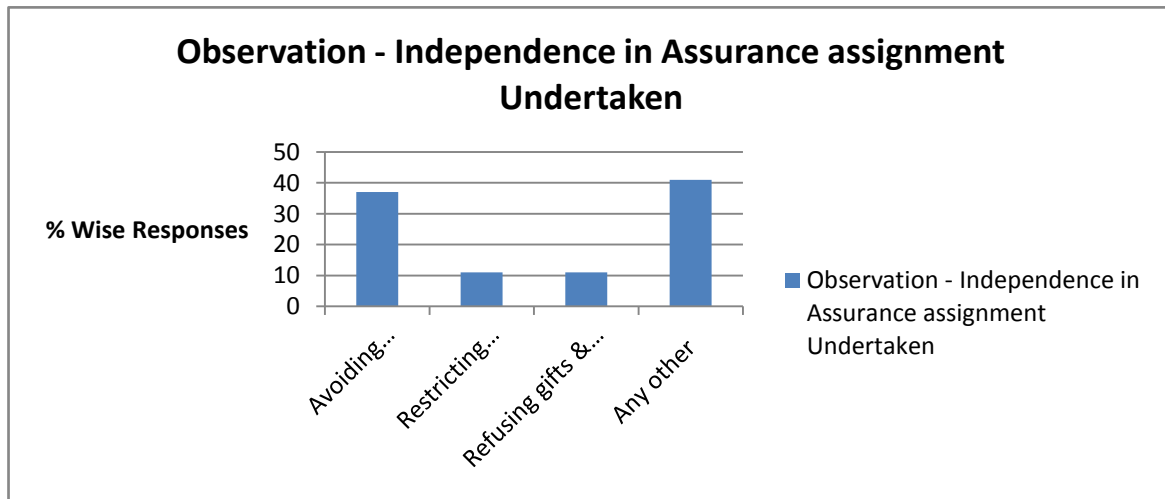
31% of Respondents felt that independence is sacrificed on account of prospects of Reappointment. 78% of the respondents felt that independence is compromised due to heavy competition among professional accountants rendering assurance services. 37% of respondents observed minimum scale of fees as recommended by Institute of Chartered Accountants of India (ICAI).

**Part VI: Ethics and Peer Review**

31% of respondents were peer reviewed. 14% of respondents carried out peer review of other firms. Only 14% of respondents agreed that peer review will improve ethics.

**Part VII: Ethics and Other**

37% of respondents felt that receiving Gift from clients is unethical. In spite of that 57% respondents received Gifts from their clients. In order to maintain Independence respondents undertook assurance assignment in way as shown the Table 5:



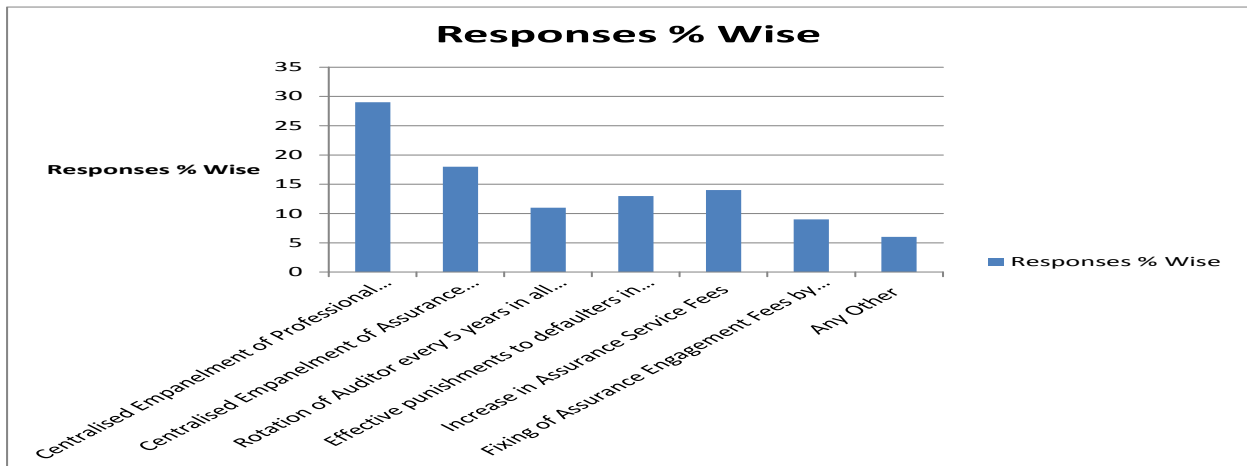
**Table 5**

Table 5 shows that ethics are more self-governed by the SMPs. 70% of respondents felt that Code of Ethics governed by ICAI kept Independence in the assignments undertaken. Only 19% of respondents felt that Independence is lost due to regulatory Framework.

**Part VIII: Ethics & Stakeholders**

13% of respondents mentioned that their clients use audit committee. 41% of respondents think that auditing profession in India has been losing its respect and creditworthiness in the eyes of business stakeholders. 94% of respondents felt that Independence will restore faith of business world in Auditing Profession in India. 71% of respondents felt that Independence is compromised in the case of Assurance Engagements in Public Bodies, PSU, Banks, Financial Institutions and Govt. Organizations. 90% of respondents felt that proper compliance with Code of Ethics by professional Accountants will restore level of financial dependence on Auditee Entity. 61% of respondents felt that Independence is compromised in the process of Tendering & auctioning. Respondents felt that following measures can be taken as shown in

Table 6 to restore faith and credibility and ensure fair distribution of assurance engagements in professional accountants in India:



The other measures suggested by the respondents were increased education on ethics and awareness. Rotation of auditors was agreed to a less number of years i.e. 3 years, etc.

### CONCLUSION:

Ethics is self regulatory measure and it is necessary that with the responsibility of stakeholders being varied the financial statements should show a true and fair view in today's globalized environment. The independence of auditors has to be ensured as a self regulatory measure. More so when the audit engagement is mostly acquired by acquaintance, it is necessary that auditor should remain independent. There are a lot of pressures to compromise independence because of dependence of SMP on Non-assurance services as revenue generation. Further more the increased competition has put pressure on the fees. Since most of the ethics are self regulatory very few SMPs charge fees as prescribed by the Institute. Further it was felt that every respondent felt the need to educate himself more about ethics but when it came to practicality he sometimes crossed the line of independence.

Therefore following specific recommendations are made.

1. Ethics should be regulated.
2. There should be rotation of auditors.

- 
3. The auditor should not be allowed to audit client with non-assurance services.
  4. There should be centralized empanelment of auditors.
  5. There should be more awareness on ethics and its role in independence of auditors.
  6. The charging of fees should be a regulatory measure.
  7. There should be implementation on peer review and audit committee.
  8. The competition should be healthy and give proper scope for ensuring independence i.e. undercutting of fees should not be allowed.

These recommendations will ensure that auditor remains a independent person to exercise his opinion on the financial statements which will increase the credibility in the eyes of stakeholders.

**REFERENCES:**

- i. Guidance Note on Independence of Auditors, Institute of Chartered Accountants of India.
- ii. Companies Act 1956, RAMIYA.
- iii. Research Journal of Finance and Accounting. Volume-2, No.3, 2011.
- iv. International Journal of Economics and Finance, Volume-1, No.1.
- v. Yale Law School Legal Scholarship Repository.
- vi. Spicer and Pegler's Practical Auditing.
- vii. We, The Nation by Palkhivala.
- viii. Cotemporary auditing by Kamal Gupta.
- ix. Auditor's Practice Manual by Kamal Garg.

- x. Companies Act by M.C. Bhandari.
- xi. Chartered Accountant's Audits Manual by Avadhesh Ojha.
- xii. Auditing and assurance Standard(AAS) 28, The auditor's Report on Financial Statements by Institute of Chartered Accountants of India.
- xiii. The Maharashtra Public Trust Act, 1950
- xiv. The Societies Registration Act, 1860
- xv. Multi State Co-operative Societies Act, 2002
- xvi. Wikipedia.