

30 July 2021

The Secretary,  
National Financial Reporting Authority  
7th-8th Floor, Hindustan Times House, 18-20,  
Kasturba Gandhi Marg, New Delhi 110001.

Dear Sir/Madam:

We are highly appreciative of the tasks and initiatives undertaken by NFRA in a very short period of time since its creation. We particularly compliment NFRA for this initiative of seeking feedback/responses through a consultative mechanism.

On behalf of the Forum for Indian Accounting Research, a not-for-profit organization that brings together academicians and practitioners to foster high-quality Accounting research in India, we are pleased to submit our responses to the Consultation Paper on Enhancing Engagement with Stakeholders: Report of Technical Advisory Committee (March 2021).

We thank NFRA for this opportunity to present our comments.

Sincerely,  
P R Ramesh, ex-Chairman, Deloitte India  
Professor Sanjay Kallapur, Indian School of Business  
Professor Srinivasan Rangan, IIM Bangalore  
Professor Srinivasan Sankaraguruswamy, National University of Singapore

### **Response to questions**

*Question 1: Formation of Stakeholder Consultation groups*

*Question 1a. What would be a suitable list of subjects that should form the standing agenda of the SAG?*

The SAG is a vehicle for the NFRA to receive feedback on its ongoing projects. Hence, a suitable list of subjects for the SAG to deliberate on would include all the issues that the NFRA is examining, prioritized according to NFRA's needs. These subjects can cover the main charges that the NFRA has, namely formulating standards, adhering to standards, monitoring firms, and auditing the auditors. Any attempt to prescribe a list of subjects could impair flexibility and curtail the opportunity of seeking a wider consultation.

*Question 1b. What would be an appropriate method for filling up positions on the SAG?*

The NFRA can use a combination of nominations and selection to fill the positions on the SAG. For example, industry bodies like the CII or the FICCI or the Assocham can, subject to approval by NFRA, nominate a representative to the SAG. In the case of academics, the NFRA can directly select prominent academics to the SAG. The NFRA can invite retired partners of audit firms or ask individual audit firms to nominate members to the SAG.

Additionally, other regulators like SEBI, RBI and IRDA could also be invited to nominate representatives.

*Question 1c. Would a single comprehensive SAG lead to better quality of deliberations and advice, taken in an integrated perspective, rather than four separate groups that could perhaps lead to thinking in silos?*

One comprehensive SAG would lead to discussions among different stakeholders. The final report would incorporate the diverse views of the different stakeholders. Having four separate groups would forego the opportunity for discussions between them. As long as the final report contains the individual views of the members or the group of members in the integrated SAG, we feel that an integrated twelve-member SAG will serve the NFRA's purposes better than four individual SAG committees.

*Question 2: Fellowship Programs*

*Question 2a. Would a nominal fellowship amount as opposed to a full living allowance/compensation for loss of income attract high quality professionals/academics?*

Usually the fellowships last for a year in organizations similar to NFRA outside India. NFRA can come to an agreement with the organization that nominates the fellow to pay a certain level of income to the fellow. Instead of having organization-by-organization agreements, a single agreement with a class or group of organizations, say universities, would suffice. In some instances, the pay agreed to between NFRA and the sending organization will result in the professional taking a pay cut. The sending organization can top up the difference if required, as long as there is no conflict of interest.

*Question 2b. Would this fellowship be full time or part time?*

As long as there is enough work to be done, and NFRA has identified projects to be handled by the professionals, the fellowship should be full time. Part-time fellowship will become a secondary priority for the professional, who will be fully occupied with work at their home organization. The disadvantage of a full-time fellowship is that many professionals would be unwilling to move their families for one year.

*Question 2c. If this is to be part time then what is the kind of minimum involvement that should be insisted upon?*

NA.

*Question 2d. In the light of the above, is a one year tenure appropriate, or should it be for a longer period? Or should it be for a few months and tailored for the specific subject that is chosen for study?*

One year tenure with a chance to extend for another year is a good time frame. This time frame is especially needed if the professional has to relocate. A different contract and

designation can be used for hiring professionals on a study-by-study basis. This decision can be made based on the subject under review.

*Question 3: Public speeches etc.*

*Question 3a. Do you agree with NFRA's general approach to communication?*

Usually when ranking members of a public organization give a talk, they make a disclaimer up front. The disclaimer is that the speech represents the personal opinion of the ranking member and not the opinion of the public organization. Further, these speeches are vetted by the organization's lawyers and are also uploaded to the organization's website when the speech is delivered.

NFRA has a duty to develop high-quality reporting and auditing. Speeches can help NFRA set expectations and discuss policy issues, which will help in fulfilling this role, and being transparent.

*Question 4: Inspection, investigation and enforcement*

*Question 4a. What are your comments on the objectives and scope of the FRQR/AQR Inspection program?*

In terms of the scope of the FRQR/AQR program, all firms with large external impacts because of size, stock market listing, or borrowings from banks should be included. Further, the inspection program should ensure that all firms over which NFRA has jurisdiction should be covered over a period of time.

Review of financial statements by the NFRA staff is important for ensuring that companies' disclosure quality is high and complies with accounting standards. We feel that all firms meeting the criteria should be reviewed every N years (in the US N tends to be 3 or 4 years), where NFRA can determine N. Whether a firm is selected for review should also partly depend on the outcome of the previous review.

*Question 4b. What are your suggestions regarding the Risk-Based Methodology for choice of companies as described above?*

We feel that external impact is very important and instead of an independent sort between external impact and high risk, we suggest that a dependent sort be done. That is, within the high-external-impact group, high-, medium-, and low-risk PIEs should be inspected. Time and effort allocation can be calibrated across the different risk categories, with maximum allocation to the high-risk category. Similarly, medium- and low-impact groups can be sub-classified based on risks. A dependent sort is preferable to an independent sort because it ensures that even if there is noise in the risk classification, PIEs that significantly affect the economy will be inspected thoroughly and regularly.

In structuring the teams for inspection, it will help if the teams are broken down by industry. This structure will allow the teams to develop expertise in that industry and help in

comparisons across firms within the same industry. The accounting practices are usually similar among the firms in the same industry.

Automatic feedback: The MDAR (management discussion and analysis report) is mandated for listed companies under Clause 49. This section discloses in narrative form what is happening in the company. Experience from the US MD&A reports shows that usually the disclosure is boilerplate and the correlation of word pairs in the MD&A is very high across years. However, businesses are not static, and so the MD&A should vary by year. NFRA could create a program that will automatically capture the MDAR from Indian companies and compare the current year's description with the prior year's description to generate a similarity score. NFRA could then send a note to the company indicating that their description of the business is 98% similar to last year's description, and asking them to please provide additional data to either support the current narrative or make changes reflecting the current state of the business. This will put the PIEs on notice that the monitoring is high and timely.

Additional comment: The US SEC maintains a spreadsheet with every tip that it gets and whether it was acted upon, what progress was made and how it was concluded. It will help if NFRA also has a similar spreadsheet in relation to the whistleblower programme.

#### *Question 5: Settlement of Disciplinary matters and remediation*

Settlement helps ease the litigation process and unclogs the system; therefore, it is desirable. Some cases need to go to court for developing principles of wide applicability, but the rest can be settled. The Companies Act, however, does not have plea bargaining. Therefore, there is a need for legislative enablement.

#### *Question 6: Communication and Advocacy: Website structure and layout*

No comment.

#### *Question 7: What in your opinion, would be the subjects/areas that Newsletters from NFRA should focus on?*

Newsletters should be factual and report on current trends in accounting and auditing and activities of NFRA. A structured process with inputs from the various divisions of the NFRA can help set the agenda for newsletters. However, authoritative guidance on accounting standards and auditing standards should be a separate publication. Usually guidance is necessary after a new standard is issued, or when implementing changes in existing standards.

#### *Question 8: Webinars*

NFRA can organize a panel or round table discussions on important topics, which can be broadcast live. A regular webinar series, except for research papers presented at NFRA, would lead to information overload and discussion of nitty-gritty details rather than big-

picture issues. On the whole, interaction and outreach by NFRA should be done transparently.

*Question 8a: Do you agree with NFRA's preliminary views on communication with the Press and Media on reports by the authority?*

Having regular briefings with the press for large settlement and investigative issues will be helpful.

*Question 9: Do you have any suggestions on viable modalities for collaborations with universities and educational institutes?*

Universities can be engaged by providing researchers with a forum to present their research. So having a regular seminar series will help.

If NFRA requires a study to be performed, then identifying an expert in that area and commissioning them to do a study can be another way of engaging researchers.

NFRA research staff presenting papers at universities will also help researchers understand the processes at NFRA.

Having case competitions each year on disclosure standards or application of accounting standards, where college students take part, will engage the youth in NFRA activities.

To facilitate research, the MCA Corporate Filings website should be patterned after the US sec.gov website so that users can quickly access the data that they need. For example, Drake, Roulstone, and Thornock, "The Determinants and Consequences of Information Acquisition via EDGAR," *Contemporary Accounting Research*, 2014, show that investors use the SEC's EDGAR database when making their investment decisions. Availability of data will go a long way towards engaging researchers and industry players and will provide scientific inputs for policy-making by the NFRA.

*Question # 10 Roadmap: Strategic Plan and Operating Plan*

*(a) Do you have any suggestions on NFRA's Strategic Goals and Priorities for the medium term?*

Since NFRA is a new organization, having a series of short-term goals will help achieve its objectives. The world is changing rapidly and so medium term and long-term plans are likely to become obsolete quickly.

*Question # 11 Building Regulatory Capacity*

*a) Do you agree with NFRA's overall approach to building regulatory capacity, as explained above? Or do you feel that this approach needs to be different, and, if so, how?*

Whilst we agree with the NFRA's overall approach, we believe a combination of in-sourcing, co-sourcing and outsourcing should be considered depending on the situation. It is important for NFRA to build up capacity quickly; its credibility will be enhanced by an early demonstration of its relevance to the financial reporting and auditing eco-system. To achieve its objectives in a short period of time, NFRA should be willing to consider co-sourcing or outsourcing in the short term.