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EDITORIAL ANALYSIS

Strengthening Oversight — Why Audit Firms Must Fix Their Governance

BUSINESS STANDARD

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SUBJECTS COVERED**ECONOMY****POLITY****GS PAPERS****GS2****GS3****CURATED & WRITTEN BY****Bharat Choudhary**

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Strengthening Oversight — Why Audit Firms Must Fix Their Governance

Business Standard

20 March 2026

GS2

GS3

BS

Business Standard

MAINS RELEVANCE:

GS Paper 2

GS Paper 3



INTERVIEW ANGLE

"The NFRA found serious governance failures in India's top audit firms. What is the role of independent audit in maintaining investor trust and financial stability? Should India consider separating audit from non-audit services entirely, as some countries have done?"

WHY IN NEWS

The **National Financial Reporting Authority (NFRA)** released inspection reports revealing critical structural weaknesses in India's top audit firms — including Price Waterhouse Chartered Accountants (PwC India), BSR & Co (KPMG India), and SRBC & Co (EY India) — flagging deficiencies in audit independence, fraud-risk assessment, and related-party transaction scrutiny.

THE NFRA FINDINGS — WHAT WAS FOUND

NFRA (National Financial Reporting Authority) — India's independent audit regulator — conducts periodic inspections of auditors of listed companies and large unlisted public companies. The 2026 inspection reports identified systemic weaknesses across India's Big Four-affiliated audit networks:

Key deficiencies flagged:

Deficiency	Implication
Audit independence failures	Partners maintaining financial/business relationships with audit clients
Poor documentation quality	Working papers insufficient to support audit conclusions
Inadequate fraud-risk assessment	Auditors not applying professional scepticism to management assertions
Weak related-party transaction scrutiny	Large intra-group transactions not adequately verified
Partner accountability gaps	Senior partners not supervising audit execution quality

Firms named: Price Waterhouse Chartered Accountants (PwCA), BSR & Co (KPMG affiliate), SRBC & Co (EY affiliate) — the Indian entities affiliated with three of the global Big Four accounting firms.

WHY AUDIT QUALITY MATTERS — THE SYSTEMIC ARGUMENT

Audit is the independent verification that a company's financial statements fairly represent its true financial position. It is the cornerstone of:

Investor trust: Public shareholders rely on audited accounts before investing

Creditor confidence: Banks and bondholders use audited financials for lending decisions

Tax compliance: Revenue authorities use audited accounts as the starting point for tax assessment

Regulatory oversight: SEBI, RBI, and sector regulators use financials to monitor systemic risk

When audit quality fails, the **information asymmetry** between company insiders and external stakeholders becomes severe — creating conditions for major corporate frauds.

India's audit failure history:

Satyam Computer Services fraud (2009): Auditors PricewaterhouseCoopers (Indian affiliate) failed to detect ₹7,800 crore accounting fraud — one of the largest corporate frauds in Indian history

IL&FS collapse (2018): Multiple rating agencies and auditors missed the growing liquidity crisis; SFIO (Serious Fraud Investigation Office) investigations found audit failures

Yes Bank (2020): Auditors failed to flag mounting NPAs and governance concerns before the near-collapse

Each case triggered regulatory tightening — but the NFRA findings suggest structural problems persist.

THE STRUCTURAL PROBLEM — COMMERCIAL PRESSURE VS. PROFESSIONAL INDEPENDENCE

The Business Standard editorial identifies a deep structural tension:

The business model problem: Audit firms earn revenue from:

Statutory audit fees (required by law for listed companies)

Non-audit services (consulting, tax advisory, risk management, due diligence)

When the same firm provides both audit and consulting to the same client, the incentive to maintain independence is weakened — the consulting revenue stream creates a dependency that compromises the auditor's willingness to issue qualified or adverse audit opinions.

India's regulatory framework:

Section 144 of the Companies Act, 2013: Prohibits auditors from providing certain non-audit services to audit clients

NFRA Rules, 2018: Independence requirements, rotation rules

Mandatory audit firm rotation: Listed companies must change audit firms every 10 years; auditors every 5 years (Companies Act 2013, Section 139)

The Big Four problem: Global audit networks operate through separate national entities (PwCA is legally distinct from PwC UK/US) — but share methodologies, branding, clients, and referral networks. National-level regulatory actions have limited reach over global network quality standards.

THE EDITORIAL'S CORE ARGUMENT

Business Standard argues that NFRA's findings reveal **audit quality as a systemic governance risk** for Indian capital markets, requiring three structural reforms:

1. STRENGTHEN NFRA'S ENFORCEMENT CAPACITY

NFRA was created by the Companies (Amendment) Act, 2017 and became operational in 2018 — but its enforcement powers remain limited:

It can debar auditors and impose monetary penalties

But it **cannot directly prosecute** — it must refer cases to SFIO (Serious Fraud Investigation Office) or MCA for prosecution

NFRA's budget and staffing remain inadequate relative to the scale of audit oversight needed

Reform needed: Give NFRA direct prosecution powers and a dedicated technical staff comparable to the UK's Financial Reporting Council or the US Public Company Accounting Oversight Board (PCAOB).

2. EXPAND AUDIT COMMITTEE INDEPENDENCE

Under Schedule IV of the Companies Act (Listing Obligations and Disclosure Requirements), audit committees of listed companies must have independent directors. But:

“Independent” directors may have informal ties to promoters

Audit committees rarely exercise robust oversight of audit methodology

Related-party transaction approvals are often formulaic rather than substantive

3. MANDATORY SEPARATION OF AUDIT AND CONSULTING (STRUCTURAL SEPARATION)

The editorial recommends considering the EU model — **MiFID II-inspired audit reform** in Europe restricts non-audit services to listed company audit clients to a cap of 70% of audit fee revenue. The UK's Brydon Review (2019) and the Competition and Markets Authority (CMA) recommended full structural separation — requiring audit-only firms separate from consulting arms.

NFRA — QUICK PROFILE

Full form: National Financial Reporting Authority

Established: 2018 (under Companies (Amendment) Act, 2017; Section 132 of Companies Act 2013)

Headquarters: New Delhi

Under: Ministry of Corporate Affairs (MCA)

Chairperson (2026): Ajay Bhushan Pandey (former Revenue Secretary and UIDAI CEO)

Jurisdiction: Auditors of listed companies, public sector undertakings, large unlisted companies

Key power: Can debar auditors and impose fines up to ₹5 crore on individuals; ₹10 crore on firms

Distinct from ICAI: The Institute of Chartered Accountants of India (ICAI) is a self-regulatory body of the accounting profession. NFRA was created to provide **independent oversight** because self-regulation by ICAI was seen as inadequate — a structural conflict of interest.

UPSC RELEVANCE

NFRA (National Financial Reporting Authority), established 2018, under MCA, Section 132 of Companies Act 2013; Companies Act 2013 audit provisions (Section 139 rotation, Section 144 non-audit restrictions); SFIO (Serious Fraud Investigation Office); ICAI; Satyam fraud (2009); PCAOB (US equivalent); Big Four = Deloitte, PwC, EY, KPMG.

Mains GS2: Regulatory institutions — NFRA's role, audit independence, corporate governance reform, Companies Act provisions, comparison with global models (UK FRC, US PCAOB). **GS3:** Financial markets regulation, investor protection, capital market integrity, audit failure and systemic risk.

★ FACTS CORNER — KNOWLEDGE PEDIA

NFRA — CORE FACTS:

Full form: National Financial Reporting Authority

Established: 2018 (notified under Companies Act 2013, Section 132)

Ministry: Ministry of Corporate Affairs (MCA)

HQ: New Delhi

Powers: Debar auditors; fine up to ₹5 crore (individual), ₹10 crore (firm); refer for prosecution to SFIO

Chairperson (2026): Ajay Bhushan Pandey

COMPANIES ACT 2013 — KEY AUDIT PROVISIONS:

Section 132: Establishes NFRA

Section 139: Mandatory audit firm rotation — 10 years for listed companies

Section 144: Prohibits non-audit services to audit clients (specific list)

Schedule IV: Audit committee independence requirements for listed companies

INDIA'S MAJOR AUDIT FAILURES:

Satyam (2009): ₹7,800 crore fraud; auditor PwCA (Indian entity); led to Companies Act 2013

IL&FS (2018): Multi-layered subsidiary fraud; SFIO investigation; rating + audit failures

Yes Bank (2020): NPA concealment; RBI-led rescue; auditor scrutiny

FIRMS FLAGGED BY NFRA (2026):

Price Waterhouse Chartered Accountants (PwCA) — PwC India affiliate

BSR & Co — KPMG India affiliate

SRBC & Co — EY India affiliate

GLOBAL AUDIT REGULATORS:

USA: PCAOB (Public Company Accounting Oversight Board) — created by Sarbanes-Oxley Act 2002

UK: FRC (Financial Reporting Council); being reformed as ARG (Audit, Reporting and Governance Authority)

EU: MiFID II reform — non-audit fee cap at 70% of audit fee for listed entity auditors

OTHER RELEVANT FACTS:

ICAI: Institute of Chartered Accountants of India — self-regulatory body; NFRA created to provide external oversight

Big Four in India: Deloitte (BSR & Co), KPMG, EY (SRBC & Co), PwC — operate as Indian LLPs affiliated to global networks

SFIO: Serious Fraud Investigation Office — under MCA; investigates corporate fraud; can arrest

Mandatory CSR: Companies Act 2013 Section 135 — ≥2% net profit for eligible companies; audited separately

Sources: Business Standard, NFRA, MCA

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