

Policy Addendum with regard to standing on Cost Auditor Remuneration

SES Proxy Advisory Guidelines Update: #1/2022-23

SES is of the view that in order to get independent and quality reports from professionals, their remuneration must be fair and commensurate with the scope of their work.

Background:

During the course of past Proxy Advisory seasons, SES had observed that remunerations proposed to Cost Auditors across various sectors continued to be significantly lower than the minimum suggested as per the Institute of Cost Accountants of India ('ICAI - CMA') guidelines. Further, the Companies were not disclosing the quantum of turnover that was subject to Cost Audit. In absence of the scope of cost audit, stakeholders had no basis to determine whether the proposed remuneration was fair or not, while analyzing proposals relating to annual ratification of remuneration for cost audits.

In November 2012, MCA had raised concern relating to quality of the Cost Audit Report and indicated low audit fee to be a potential cause for the same. In 2018, the Institute of Cost Accountants of India ('ICAI - CMA') issued a recommendatory guideline suggesting minimum fees that ought to be paid for the professional assignments done by the Cost Accountants.

Initial SES Stance:

Considering above issues and the recommendation made by the ICAI - CMA, SES commenced to highlight concerns in its reports from 2018 with regard to resolutions proposing approval for cost audit remuneration which were significantly lesser than ICAI - CMA benchmarks and where scope of turnover subject to cost audit was not disclosed. SES consistently raised concerns addressing the above issues, however, it did not recommend against such resolutions until the year 2022. SES had also stated that, in future, SES might give adverse recommendations in such cases.

Subsequent Change in SES Stance:

In 2022, after continuously highlighting concerns over the low remuneration of cost audits and lack of transparency over scope of such audits for past four years, since no proper justifications were forthcoming from Companies in their notices, SES commenced with negative recommendations against proposals for ratification of Cost Audit fees that were significantly lower than minimum fee suggested by ICAI-CMA.

SES experience in Proxy Season 2022:

In response to negative recommendations made by SES, many Companies responded that the Cost Auditors were shortlisted after inviting quotations from eligible professionals and the final remunerations were actually determined basis the quotations that were received, which happened to be significantly lower than the minimum fee suggested by ICAI-CMA.

The Companies further indicated that the quotes received by them represented a more proper reflection of the scope involved than what was suggested by the ICAI-CMA.

Companies also indicated that due to advancement in technology, Cost Audit was now conducted through ERP and other automation tools, with Cost Audit teams comprising of fewer members.

Thus, a lot of companies were of the opinion that their proposals for cost audit fees were very much commensurate with the work involved and the size of teams in the present business environment.

Stakeholders Empowerment Services

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SES Dilemma:

Based on the feedback received from Companies in previous proxy season (21-22), SES acknowledges the ground realities and understands issues faced by the companies in the sense that the cost audit fees are driven low as a result of reduction in scope of work due to advancement in software and auditing systems and further, due to cost auditors themselves putting forward lower quotations, in order to undercut potential rivals.

Conclusion:

Although SES observed concerns with regard to lower cost audit remunerations and lack of transparency over scope of such audits, SES is constrained to change its stance basis the feedback received from companies across multiple sectors. Henceforth, SES would only continue to highlight concerns on lack of transparency over the scope of cost audits, but will refrain from making adverse recommendations based on low cost audit fees proposed.

Thus, SES will no longer be recommending AGAINST proposals for ratification of cost audit fees which are significantly lower than the minimum suggested fee by ICAI-CMA.

SES is of the view that the ICAI-CMA should have a thorough relook on the need / applicability of cost audits w.r.t. most products across all sectors and release an updated recommendation guideline for minimum suggested fees considering present business environment and scope of work involved while conducting Cost Audit. SES feels that even the need for cost audit must be examined afresh as India is no longer a controlled economy and, except a few products, there are no cost controls or pricing controls operative.

Effective Date:

With immediate effect (i.e. 29th March, 2023)

Circulation:

All Listed Companies in SES coverage and all SES clients