

National Foundation for Corporate Governance

National Conclave on Corporate Governance in India : *Disclosure Practices – Accounting and Audit*

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If you go on any trip to, say four countries this is the problem that you will face, whatever you carry your cell phone or lap top or whatever you will have to carry multiple adapters. Why could not the world standardize on one format the plug point and one electricity voltage beat me just imagine how simple his life would have been. The same thing applies to disclosure and accounting policies as well. On the lighter vain I was told that when one of India's commodity major acquired a U.S. company in the same industry it created a sudden spurt in demand for Indian CAs in the US because now they the US company has to recast its accounts under the Indian GAP so the parent in India could consolidate. While in a way it is heart warming to note that sometimes the East India Company is playing out in a reverse phenomenon but just imagine if accounting standards were simplified and standardized it wouldn't cause all those complications even if we can't change the electric wall outlets all over the world even in the accounting standards that would help.

Many people have spoken about the trend towards IFRS etc. Especially the point being if IFRS is more principles based, in my view it is better because as all of us know that we can follow all the rules and still come to a wrong

conclusion were if you follow the principle based approach not trivializing the challenge of adopting such a thing, Richard and others have spoken about getting the requisite amount of training both for companies and for auditors and for everything else but still I think principles based approach would lead to a better conclusion in the end. Thankfully many of the Indian accounting standards were aligned to IFRS. any way. Probably the transition would be simpler for India.

Second thing I am seeing increasingly over time and some of these things I clearly believe India is in a much more advanced position than for example in the U.S. If you look within the technology industry say, Infosys annual report the kind of disclosures you see are far superior than American company like Accenture. I think many of us have moved to a stage where you don't report only historic financial information whether my sales went up or when down etc. you look at your investor base and you try and understand what information is relevant for the investor and you don't therefore say this is the minimum disclosure, can I get away with it kind of an approach. You say if I explain better to my investors and they understand it better therefore my valuation goes up on the basis.

In a way the world is moving towards more on investor centric view of preparation and disclosures of financial statements beyond just the statutory minimum format. The trends that you are seeing now among the well governed leading companies directors' report etc is to try and communicate investors what is the long term value potential of the business because one way or the other you can't get away from the fact that the format of your financial reporting is historic, is short term oriented. You can't get away from it. You are reporting last quarter numbers and you are reporting those numbers after having happened. Maybe that is important, maybe that is useful, maybe that his statutory so you have to comply with it but management's have to go beyond that, you have to explain to the people the long term value potential of the business. Otherwise you can't blame that the markets are being shortsighted and you need to ask yourself what did you do to explain that to the markets as well.

I come from the IT industry and you look at many of us in the IT industry, when Mind Tree publishes its quarterly information beyond the statutory balance sheet, P&L, cash flow, MDNA etc. Several of us include what we call a fact sheet which explains our business. Things that are relevant to context for our industry but not financial. For example, we explain our movement in receivables, what was their utilization last quarter to this quarter, how much the volume growth happen, how much the prize growth happened, they view breakdown by geography or verticals etc. - all of which are contextual, non-financial information that are relevant for our industry, so our analysts are our market participants would track us can understand our results better, compare us better with the other people in our industry and therefore they can find out which has greater long term value from investment point of view.

Clearly there is a lot more focus and a lot more emphasis on does management have adequate internal control over financial reporting, while clearly there have been a lot of discomfort, problems in terms of implementation of Sox and the cost etc. it is surprising to see that nobody has studied the reverse of the phenomenon, nobody has studied what is the benefit that the companies have got out of better disclosure, better reporting practice etc. in a way sometimes regulations follow environmental changes and this is therefore followed that change there. The people who have found it most painful are the people who had bad practices in the past. Ultimately the issue is whether you comply with Sorbanes Oxley or not the issue is when you report results to your investors, to markets, to external stakeholders are you comfortable with that reporting adequate internal controls exercised over the preparation and disclosures which I think is a commonsensical requirement. The problem is when markets go go-go people forget fundamentals. Therefore it is important also to realize that some of these issues are also problems of people who were unprepared etc. The fact is that somebody's neck is on the chopping block that if you find an error in the financial statement CEO and the CFO in the US would go to jail.

In India the modified version of clause 49 etc. has adopted the company could get delisted now people realize that I can't say that I don't know. Now there is a clear accountability which I think is an improvement definitely.

Something I would like to leave with the audience to think about, some things are at individual company level. I think companies when they prepare their annual report or their quarterly disclosures etc. should spend a couple of minutes introspecting what are you putting out into the market. Is that sufficient for investors to understand you? How do you explain your organization, your culture, your strategies, whatever is there that makes you unique or different or gives your business a long term value potential and you explain that correctly. Sometimes when I compare for example, the financial statements in India right now the management disclosure, discussion and analysis typically tends to be like a cricket commentary kind of a thing.

Nowhere were you able to understand why it happened. I think it should go beyond saying what happened you should also say why it happened. I think we can also at a small level relook at the presentation format. If I compare the disclosure formats in India and the US the Indian accounting formats have most recent period on the left older period on the right. Your eye doesn't read that way. If you draw a graph and show sales of 2005, 2006, 2007 etc. 2005 would be left to most and the 2007 would be right. For example, that would make easier for the presenter to compare and for the reader to understand. We can revisit those presentation formats. With all the changes in the environment, with the requirement for specialization both from the presenter and the reader point of view we should probably look at industry specific accounting standards. The presentation format or the use of estimates or any of those kind of stuff would be very different for a manufacturing company for a bank or for an insurance company or a knowledge based enterprise like software or KPOs etc.

Lastly, I think one of the lacunae in India right now is that nobody governs the accountants from a structural point of view. The accountants are answerable only to the ICAI unlike in the U.S. where the accountants are regulated both by the SEC and PCAOB who guards the guardians in a way. For example, you find that there is a misstatement, you find an auditor management collusion it becomes loose way kind of the format right now maybe we should look at some structural oversight, maybe it should be SEBI in India or somebody else,

some structural kind of a change where accountants are answerable beyond just their own brethren it should be answerable to a public entity, maybe something we can consider.

Thank you
