NATIONAL COMPANY LAW APPELLATE TRIBUNAL
PRINCIPAL BENCH, NEW DELHI

COMPANY APPEAL (AT) NO. 68 of 2023
&
I.A. No.2007-2009 of 2023
(Arising out of the Order dated 13.04.2023 passed by the National Financial Reporting Authority in Nf-21/1/2022/03.)

IN THE MATTER OF:

Mr. Harish Kumar T.K

...Appellant

Versus

National Financial Reporting Authority
7th-8th floor, Hindustan Times House,
18-20 Kasturba Gandhi Marg.
New Delhi – 110001. **...Respondent**

Present

For Appellant: **Sr. Advocate P.H. Arvindh Pandian with Mr. Goutham Shivshankar, Sharamya Sinha, Adit Shah, Advocate.**

For Respondent: **Mr. Zoheb Hussain, Advocate.**

WITH

COMPANY APPEAL (AT) NO. 87 of 2023
&
I.A. No. 2401-2403 of 2023

(Arising out of the Order dated 31.03.2023 passed by the National Financial Reporting Authority in Nf-21/1/2022/02.)

IN THE MATTER OF:

CA Ayna Tamton

...Appellant

Versus

National Financial Reporting Authority
Office At:
7th-8th floor, Hindustan Times House,
18-20 Kasturba Gandhi Marg
New Delhi – 110001. **...Respondent**
Mail :review@nfra.gov.in

Present

For Appellants: **CA CV Sajan & Mr. Rishi Singhal, Adv**

For Respondents: **Mr. Zoheb Hussain, Ms. Farheen Penwale, Mr. Vivek Gurnani and Mr. Kvaish Garach, Advocates.**

WITH

COMPANY APPEAL (AT) NO. 90 of 2023
&
I.A. No. 2410-2412 of 2023

(Arising out of the Order dated 13.04.2023 passed by the National Financial Reporting Authority in Nf-21/1/2022/06.)

IN THE MATTER OF:

CA M Baskaran

...Appellant

Versus

National Financial Reporting Authority
Office At:
7th-8th floor, Hindustan Times House,
18-20 Kasturba Gandhi Marg
New Delhi – 110001.
Mail :review@nfra.gov.in **...Respondent**

Present

For Appellants: **CA CV Sajan and Mr. Rishi Singhal, Advocates.**

For Respondents: **Mr. Zoheb Hussain, Ms. Farheen Penwale, Mr. Vivek Gurnani and Mr. Kvaish Garach, Advocates.**

WITH

COMPANY APPEAL (AT) NO. 91 of 2023
&
I.A. No. 2413-2415 of 2023

(Arising out of the Order dated 12.04.2023 passed by the National Financial Reporting Authority in Nf-21/1/2022/05.)

IN THE MATTER OF:

CA SAM VARGHESE

...Appellant

Versus

National Financial Reporting Authority
Office At:
7th-8th floor, Hindustan Times House,
18-20 Kasturba Gandhi Marg
New Delhi – 110001.
Mail :review@nfra.gov.in **...Respondent**

Present

For Appellants: **CA CV Sajan & Rishi Singhal, Advocates.**
For Respondents: **Mr. Zoheb Hossain Adv.**

J U D G E M E N T

(01.12.2023)

[NARESH SALECHA, Member (TECHNICAL)]

1. These four Appeals are arising out of four different Impugned Orders passed by National Financial Reporting Authority (in short '**NFRA**').

2. It is the case of NFRA, the Respondent herein, that all four present Appeals before this Appellate Tribunal, belong to Branch Audit of 17 branches of Dewan Housing Finance Limited (in short '**DHFL**'), which were assigned to K. Varghese & Co. (in short '**the firm**') and the four Appellants in four Appeals were different Engagement Partners (in short '**EP**') for different branches, as such these four appeals may be clubbed and taken up together. The plea of clubbing was also agreed by the Counsel of the Appellant in all the four cases.

3. The summary of all these four cases can be seen from the under mentioned table for the sake of convenience.

DHFL Branch Auditors

Auditor	**Harish Kumar**	**AynaTamtam**	**Baskaran**	**Sam Varghese**
Appeal No.	**CA (AT) No. 68/2023**	**CA (AT) No. 87/2023**	**CA (AT) No. 90/2023**	**CA (AT) No. 91/2023**
SCN	07.12.2022	07.12.2022	07.12.2022	07.12.2022
Impugned Order	13.04.2023	31.03.2023	13.04.2023	12.04.2023
Penalty	Rs. 1,00,000 + Debarred for 1 year	Rs. 1,00,000 + Debarred for 1 year	Rs. 1,00,000 + Debarred for 1 year	Rs. 1,00,000 + Debarred for 1 year

Allegations	1. Acceptance of audit engagement without valid authorisation and without complying with ethical requirements; and issuing audit report in violation of the Act 2. Failure to comply with Standards on Auditing (SAs) SA 210"Agreeing the Terms of Audit Engagement" SA 230 "Audit Documentation" SA 700 "Forming an Opinion and Reporting on Financial Statements" Non-compliance with other SAs	1. Acceptance of audit engagement without valid authorisation and without complying with ethical requirements; and issuing audit report in violation of the Act 2. Failure to comply with Standards on Auditing (SAs) SA 210 "Agreeing the Terms of Audit Engagements" SA 230 "Audit Documentation" SA 700 "Forming an Opinion and Reporting on Financial Statements" Non-compliance with other SAs	1. Acceptance of audit engagement without valid authorisation and without complying with ethical requirements; and issuing audit report in violation of the Act 2. Failure to comply with Standards on Auditing (SAs) SA 210 "Agreeing the Terms of Audit Engagements" SA 230 "Audit Documentation" • SA 700 "Forming an Opinion and Reporting on Financial Statements" Non-compliance with other SAs	1. Acceptance of audit engagement without valid authorisation and without complying with ethical requirements; and issuing audit report in violation of the Act 2. Failure to comply with Standards on Auditing (SAs) SA 210 "Agreeing the Terms of Audit Engagements" SA 230 "Audit Documentation" • SA 700 "Forming an Opinion and Reporting on Financial Statements" Non-compliance with other SAs

4. At initial stage of hearing and based on above details, we find that the grounds, by and large, are common and facts are also similar, hence these shall be jointly examined and dealt with in subsequent discussions and one

common judgment will be pronounced. This was based on discussion and suggestion of the Counsel of all parties concerned.

5. At the outset, It is pertinent to mention that perhaps this is first case on professional misconduct by Auditors before this Appellate Tribunal (other settled on interpretation of Rule, 11 & 12 of NFRA Rule, 2018 vide our earlier order dated 02.06.2023 passed in Company Appeal (AT) No. 68, 87, 88, 90, 91, 92, 93 & 94 of 2023, hence our endeavour would be to collect all relevant material, law, citations, etc., as far as possible, to make it comprehensive for clarity and convenience.

6. Heard the Counsel for Parties and perused the records made available including cited judgments.

Company Appeal (AT) No. 68 of 2023 &
I.A. No. 2007-2009 of 2023
[Arising out of Order dated 13.04.2023 passed by the National Financial Reporting Authority, in Nf-21/1/2022/03.]

7. The present Appeal in CA AT No. 68/2023 has been filed by CA. Harish Kumar T.K., who was EP in Impugned Order dated 13.04.2023, passed by NFRA under Section 132(4) of the Companies Act, 2013 r/w Rule 11(6) of National Financial Reporting Rules, 2018 (in short '**NFRA Rules, 2018'**). The Appellant has been saddled with a penalty of Rs.1,00,000/- and is debarred for one year from being appointed as an Auditor or Internal Auditor or from undertaking any Audit in respect of Financial Statements or Internal Audit of the functions and activities of any Company or Body Corporate.

Company Appeal (AT) No. 87 of 2023 &
I.A. No. 2007-2009 of 2023
[Arising out of Order dated 13.04.2023 passed by the National Financial Reporting Authority, in Nf-21/1/2022/03.]

8. The present Appeal in CA AT No. 87/2023 has been filed by CA. Ayna Tamtam, who was EP in the Impugned Order dated 31.03.2023, passed by NFRA under Section 132(4) of the Companies Act, 2013 r/w Rule 11(6) of National Financial Reporting Rules, 2018 (in short NFRA Rules, 2018). The Appellant has been saddled with a penalty of Rs.1,00,000/- and is debarred for one year from being appointed as an Auditor or Internal Auditor or from undertaking any Audit in respect of Financial Statements or Internal Audit of the functions and activities of any Company or Body Corporate.

Company Appeal (AT) No. 90 of 2023 &
I.A. No. 2007-2009 of 2023
[Arising out of Order dated 13.04.2023 passed by the National Financial Reporting Authority, in Nf-21/1/2022/03.]

9. The present Appeal in CA AT No.90/2023 has been filed by CA. M. Baskaran, who was EP in the Impugned Order dated 13.04.2023, passed by NFRA under Section 132(4) of the Companies Act, 2013 r/w Rule 11(6) of National Financial Reporting Rules, 2018 (in short NFRA Rules, 2018). The Appellant has been saddled with a penalty of Rs.1,00,000/- and is debarred for one year from being appointed as an Auditor or Internal Auditor or from undertaking any Audit in respect of Financial Statements or Internal Audit of the functions and activities of any Company or Body Corporate.

Company Appeal (AT) No. 91 of 2023 &
I.A. No. 2007-2009 of 2023
[Arising out of Order dated 13.04.2023 passed by the National Financial Reporting Authority, in Nf-21/1/2022/03.]

10. The present Appeal in CA (AT) No. 91/2023 has been filed by CA. Sam Varghese, who was EP in the Impugned Order dated 12.04.2023, passed by NFRA under Section 132(4) of the Companies Act, 2013 r/w Rule 11(6) of National Financial Reporting Rules, 2018 (in short NFRA Rules, 2018). The Appellant has been saddled with a penalty of Rs.1,00,000/- and is debarred for one year from being appointed as an Auditor or Internal Auditor or from undertaking any Audit in respect of Financial Statements or Internal Audit of the functions and activities of any Company or Body Corporate.

11. The Learned Counsel for the Appellants gave overall background of all four Appeals and circumstances which led to the filing of the present Appeals under Section 132(5) of the Companies Act, 2013.

12. All four Appellants are practicing Chartered Accountants who joined the firm K. Varghese & Co. Chartered Accountants, which was assigned audit work of 17 Branches of DHFL, which in turn, assigned different set of branch audit work to different EP's.

a.) CA. Harish T.K was assigned branch audit work as EP of three branches of M/s DHFL at Thrissur, Kotayyam and Coimbatore.

b.) CA. Ayna Tamtam was assigned branch audit work as EP of two branches of M/s DHFL at Kannur and Calicut.

c.) CA. M. Baskaran was assigned branch audit work as EP of nine branches of M/s DHFL at Zone Tamil Nadu, RPU Chennai, Chennai,

Chennai Metro, Chennai OMR, Chennai Sales Vertical, Chennai Tambaram, Chennai Kodambakkam and Parrys.

d.) CA. Sam Varghese was assigned branch audit work as EP of two branches of M/s DHFL at Kochi, Kerala.

13. DHFL appointed the Firm on 27.08.2014 as Auditors to Audit 17 Branches of DHFL for the Financial Year 2014-2015 in consultation with the then joint Statutory Auditors of DHFL i.e., M/s. TR Chadha & Co. along with M/s. Rajinder Neeti & Associates.

14. It is the case of the Appellants that most of the decisions of DHFL were centralised in Head Office of DHFL who followed computerised accounting system through Enterprise Resource Planning System (in short '**ERP'**). As per the Appellants, the Books of Accounts of the Branches mainly concerned with financial effect of revenue and expenses identified to the respective Branches, as well as Fixed Assets and Liabilities being reflected in the Branch accounts. The Appellants emphasised that the Engagement Partners did not have any role in certifying the Financial Statements of DHFL and their role was confined only to Branch accounts of respective branches.

15. It has been stated that during FY 2014- 15, the Joint Statutory Auditors of DHFL i.e., M/s. TR Chadha & Co. along with M/s. Rajinder Neeti & Associates were reappointed in 30th AGM of DHFL and a Resolution was passed on the recommendation of the Audit Committee of DHFL to authorise Board of Directors of DHFL to appoint Auditors for branches and accordingly the Firm was appointed to conduct Audit at 17 Branches. The Appellants stated that they certified and confirmed that they did not have

any relationship with any Directors/Employee of DHFL and there was no conflict of interest in accepting the Audit and were not disqualified to be appointed as Auditors.

16. The Appellants stated that being an assignment from a new client in the FY 2014 - 15, the Firm carried out a comprehensive assessment about the client's business, features of the accounting and IT system, controls and procedure in the organization, activities and operations in the Branches and their financial effects, scope of the assignment as Branch Auditor, Branch Auditor's responsibility according to the terms of appointment and as per regulations in force, risk of material misstatement in the components of financial statements under Audit, risk from non-compliance, correctness in process of appointment; and checklist based verification for compliance of the Standards on Auditing (in short '**SAs**') issued by the Institute of Chartered Accountants of India (in short '**ICAI**'). The Appellants, further stated that based on such assessment, appropriate Audit programs were made, and were executed by the Firm through EPs the Appellants herein. As per the Appellants, the Firm's appointment was repeated in subsequent years, as such, the templates available on records were relied upon, subject to annual reassessment based on discussions and validation of records gathered.

17. It has been stated that the Firm was appointed Branch Auditors in subsequent Financial Year of 2015 - 16, 2016 -17, 2017 - 18 and 2018-19, after receiving similar appointment letters from DHFL. As per the Appellants, the Firm did not receive any Appointment Letter for 2019-2020

and did not carry out any Branch Audit thereafter, the Firm was involved in Branch Audit for 5 years from 2014-15 to 2018-19.

18. It has been reiterated that DHFL appointed the Joint Statutory Auditors M/s. TR Chadha & Co. and M/s. Rajinder Neeti & Associate in 30th AGM and then were reappointed as the Statutory Auditor for period of four years (upto 34th AGM), however the Statutory Auditors did not make themselves available to continue at 32nd AGM of DHFL and therefore at 32nd AGM, DHFL passed a Resolution on 20.07.2016 to appoint M/s. Chaturvedi and Shah (in short the '**CAS**) as Statutory Auditors to Audit all Company Offices including Zonal and Branch Offices for a period of five years (from conclusion of 32nd AGM to conclusion of 37th AGM). It has been highlighted that despite changes in Statutory Auditors, the Firm continued to receive Appointment Letter for 17 Branches from DHFL for Audit for the FY 2016-17, 2017 - 18 and 2018-19.

19. It has been brought out that on 10.08.2022, M/s K. Varghese & Company (the firm) received a letter from NFRA calling for Audit Files of Branch Audits conducted by the Firm for FY 2017 – 18 with regard to DHFL and the firm submitted the same to NFRA on 25.08.2022.

20. It is the case of the Respondent that NFRA initiated an Audit Quality Review to probe into role of Statutory Auditors for FY 2017-18, on suspected frauds by the Promoters & Directors of DHFL and alleged that prima facie the appointment of Branch Auditors were done without following due procedures as prescribed in the Companies Act, 2013, as well as violation of certain SAs and therefore the Appellants were charged for professional misconduct.

21. The Appellant- CA Harish Kumar T.K, in Company Appeal (AT) No. 68 of 2023, stated that, subsequent to furnishing audit files by the firm to NFRA, he received the Show Cause Notice (in short '**SCN**') dated 07.12.2022, whereby NFRA, alleged that prima facie the appointment of Branch Auditors was done without following due procedures as prescribed in the Companies Act, 2013, as well as violation of certain SAs and therefore Appellant was charged for professional misconduct. The Appellant- CA Harish Kumar T.K submitted his reply to the same on 03.02.2023 along with supplementary audit documentations running to about 600 pages. However, NFRA passed the Impugned Order on 13.04.2023 under Section 132 (4) (c) of the Companies Act, 2013, whereby the Appellant was debarred for one year from appointment as Auditor etc., and was asked to pay a monetary penalty of Rs. 1,00,000/-

22. The Appellant- CA Ayna Tamtam, in Company Appeal (AT) No. 87 of 2023, stated that, subsequent to furnishing audit files by the firm to NFRA, the Appellant received the SCN dated 07.12.2022, whereby NFRA, alleged that prima facie the appointment of Branch Audit was done without following due procedures as prescribed in the Companies Act, 2013, as well as violation of certain SAs and therefore Appellant was charged for professional misconduct. The Appellant- CA Ayna Tamtam submitted reply to the same on 04.02.2023 along with supplementary audit documentations. However, NFRA passed the Impugned Order on 31.03.2023 under Section 132 (4) (c) of the Companies Act, 2013, whereby the Appellant was debarred for one year from appointment as Auditor etc., and was asked to pay a monetary penalty of Rs. 1,00,000/- .

23. The Appellant- CA M. Baskaran, in Company Appeal (AT) No. 90 of 2023, stated that, subsequent to furnishing audit files by the firm to NFRA, he received the SCN dated 07.12.2022, whereby NFRA, alleged that prima facie the appointment of Branch Audit was done without following due procedures as prescribed in the Companies Act, 2013, as well as violation of certain SAs and therefore Appellant was charged for professional misconduct. The Appellant- CA M. Baskaran submitted reply to the same on 04.02.2023 along with supplementary audit documentations. However, NFRA passed the Impugned Order on 13.04.2023 under Section 132 (4) (c) of the Companies Act, 2013, whereby the Appellant was debarred for one year from appointment as Auditor etc., and was asked to pay a monetary penalty of Rs. 1,00,000/- .

24. The Appellant- CA Sam Varghese, in Company Appeal (AT) No. 91 of 2023, stated that, subsequent to furnishing audit files by the firm to NFRA, he received the SCN dated 07.12.2022, whereby NFRA, alleged that prima facie the appointment of Branch Audit was done without following due procedures as prescribed in the Companies Act, 2013, as well as violation of certain SAs and therefore Appellant was charged for professional misconduct. The Appellant- CA Sam Varghese submitted reply to the same on 04.02.2023 along with supplementary audit documentations. However, NFRA passed the Impugned Order on 12.04.2023 under Section 132 (4) (c) of the Companies Act, 2013, whereby the Appellant was debarred for one year from appointment as Auditor etc., and was asked to pay a monetary penalty of Rs. 1,00,000/- .

25. The Appellants have been charged for mis-conduct on following grounds:

(i) Failure to ascertain from the DHFL, whether the requirements of Sections 139 & 140 of the Companies Act, 2013 in respect of such appointment have been duly complied with.

(ii) Failure to disclose the material facts known to the Appellants which were not disclosed in the Financial Statements but disclosure of which was necessary in professional capacity.

(iii) Failure to exercise due diligence and acted being grossly negligent in the conduct of professional duties.

(iv) Failure to obtain sufficient information which was necessary for the expression of an opinion.

(v) Failure to invite attention to material departure from the generally accepted procedures of Audit.

It has been brought out that SCNs contained major lapses including:-

(i) Accepting auditor engagement issued without a valid authority.

(ii) Violations of the SAs :-

(a) Non-compliance with SA 210 "Agreeing the Terms of Audit Engagement:

(b) Non-compliance with SA 230 "Audit Documentation".

(c) Non-compliance with SA 700 “Forming an Opinion and Reporting on Financial Statements".

(d) Non- compliance with few provisions of SAS: 300, 315, 320,330, 450, 500, 520 & 530 and also of Code of Ethics issued by ICAI.

26. The Appellants submitted that they replied to SCNs denying allegations of professional misconduct and requested NFRA to drop SCNs in terms of Section 132(4) of Companies Act, 2013 and also submitted documents establishing that Appellants conducted Audit as per SAs and highlighted that their limited role confined to Audit of Branch Accounts. The Appellants stated that they were shocked to receive Impugned Orders containing penalty of Rs. 1,00,000/- and debarment for one year.

27. As a preliminary ground, it is the case of the Appellants that NFRA does not have any retrospective jurisdiction since NFRA itself was constituted on 01.10.2018 vide Ministry of Corporate Affairs (in short '**MCA'**) Notification dated 01.10.2018 and MCA also notified on 24.10.2018 as effective date for coming into force of Section 132(2), (4), (5), (10), (13), (14) & (15) of Companies Act, 2013. The Appellants submitted that NFRA Rules were notified on 13.11.2018, whereas the Financial Statements in question pertains to FY 2017-18 and Audit Reports for different Branch Audit were given on different dates for different branches which were prior to notification bringing NFRA into effect, therefore, the NFRA did not have any jurisdiction to look into the period prior to its own formation on 01.10.2018. It is further the case of the Appellants that there is no mention regarding retrospective applicability in Section 132 of the Companies Act, 2013 or in the MCA Notification issued for the same.

28. Few Judgements have been brought to the notice of this Appellate Tribunal which gives constitutional protection under Article 20 of the

Constitution of India regarding non-Application of retrospectivity of penal statute and in defence of other charges.

(a) Council of Institute of Chartered Accountants of India' Vs. C.H. Padiya', *(1979) 49 Com Cas 478.*

(b) `Maya Rani Punj' Vs. CIT, Income Tax, Delhi', *(1986) 1 SCC 445.*

(c) 'ICAI' Vs. `Shrui K. Venkatacharyulu', *MANU/AP/2140/2014***.**

(d) `S.K. Ganesan' Vs. A.K. Joscelyne', *1956 SCC Online Cal 43.*

(e) 'ICAI' Vs. `L.K. Ratna', *(1986) 4 SCC 537.*

29. Another preliminary ground of challenge by the Appellants, to the Impugned Orders of NFRA, in the Appeal Books as well as during several initial hearings, is that enquiry by NFRA was against the laid down procedures since NFRA did not constitute any division as required in Section 132(1A) of the Companies Act, 2013. It is the case of the Appellant that as per Rule 2(g) of NFRA Rules, 2018, NFRA is obligated to establish divisions for the purpose of organising its functions and duties. It has been emphasised that separate divisions are necessary for fair and independent investigations for alleged professional misconduct and other misconduct as can be inferred from Rule 10 & 11 of NFRA Rules, 2018, which prescribed separate divisions for investigations and for enforcement, similarly Rule 11(5) of NFRA Rules, 2018 talks about reasoned Order in adherence to principle of natural justice including an opportunity of being heard in person and submissions by concerned person to defend his case. It is case of the Appellants that in the present case, SCNs were signed by the "Executive Body, NFRA" comprising of Chairperson and two full time Members violating principle of natural justice. The Appellants submitted

that under Section - 132(1A) "NFRA shall perform its function through divisions as may be prescribed" and since divisions have not been prescribed for NFRA by the legislative, NFRA cannot function at all, until such divisions are set up.

30. It is the case of the Appellants that the term "professional or other misconduct" is defined in Chartered Accountant Act, 1949 therefore, they were under impression that they are covered under Chartered Accountant, 1949 Act only and did not have any indication that alleged professional misconduct can be instituted under Companies Act, 2013.

31. It is stated that the Appellants have received peer-review certification from ICAI for the FY 2017-18 which establishes that their job was satisfactory and the they conducted the Audit work in accordance with SAs and therefore allegations by NFRA are not sustainable.

32. It has been alleged by the Appellants that NFRA incorrectly applied the provisions of Chartered Accountant Act, 1949, which defines professional misconduct in Section 22 r/w first Schedule of the Chartered Accountant Act, 1949, according to which the Appellants were required to check that their appointments were in accordance with Section 225 of the Companies Act, 1956 and there was no reference in Companies Act, 1913, in fact the amendment for the same was brought out only in 2022.

33. The Appellant assailed the Impugned Orders where NFRA assumed that Chartered Accountant Act 1949 required compliance of Section 224 & 224(a) of Companies Act, 1956 and also required to check compliance with Section 139 of Companies Act, 2013. It is the case of the Appellant that since the Firm was appointed Branch Auditors for Financial Year 2014 - 15

at 30th AGM and in terms of Section 139 of the Companies Act, 2013 such appointments were for period of five years and therefore NFRA was incorrect in equating Section 225 of the Companies Act, 1956 to Sections 139 & 140 of the Companies Act, 2013, whereas these are not equivalent Sections.

34. It has been stated that it was wrong on the part of NFRA to rely on the provision of Section 139(1) of Companies Act, 2013 for annual ratification of Auditors and since they did not receive any Notice for removal under Section 140 of the Companies Act, 2013 the Appellants presumed that they continued as the Branch Auditors.

35. It is alleged that NFRA erred in relying on the Code of ethics issued by ICAI, which puts obligations on the incoming Auditor about compliance of requirement of Companies Act, 1956 whereas no such requirement exists for outgoing Auditors. It is case of the Appellants that they were appointed Auditors at 30th AGM and any change of Auditors in 32nd AGM would not have impacted them for violating Code of ethics, and for the same they relied upon three Judgements with reference to Code of ethics;

(i) D.G. Chandak Vs. S.D. Chauhan of M/s. S.D Chauhan & Co., Mumbai'.

(ii) Vinod Somani' Vs. M.L. Agarwal' .

(iii) Prafull R. Gandhi of M/s. P.R. Gandhi & Co.' Vs. Padam Chand Jain of M/s. Padam Chand Jain & Associates'.

36. The Appellants gave detailed submissions on denial of the charges of the Respondent/ NFRA of alleged violations of various SAs.

37. We have noted same and these averments of the Appellants will be analysed later while discussing and analysing the issue “True intent of

Standard of Audits and other related standards relevant for audit and issue regarding alleged violation by the Appellants herein".

38. At this moment, it is suffice to observe that it is the case of the Appellants that their role was limited to audit of branches and it was prime responsibility of CAS to do the needful. It is also case of the Appellant that they complied with all SAs.

39. It is the case of the Appellants that as per the proviso to Section 143(8) "branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

40. The Appellants also refuted NFRA's finding that there was absence of materiality levels documented in the audit files as Audit Reports submitted by the Appellants in relation to each of the branches audited by them had an Annexure IX titled "Branch Auditor Audit of Branch's Financial Information: Summary Memorandum - As a Whole" and which had statements on how materiality was determined in the audit procedure.

41. The Appellants also denied allegation with regard to assessment of risk of misstatement and test of controls and elaborated that as per the business model of the DHFL, the branch offices were for interface with the customers. The Trial Balances reflected in the books of accounts of the branches predominantly reflected expenses incurred in administration and maintenance, Fixed Assets in the branch concerned, loans granted and their interest earnings were not retained in the books of accounts of the branches and the accounting effect of operational activities such as loans and deposit, used to be reflected in the books of accounts of the Head Office of DHFL.

The Appellants emphasised that risk of misstatement in the accounts of DHFL for the Appellants were only with respect to expenses and income attributed to the branch and pointed out that for example - during F.Y. 2017-18, expenses incurred by Coimbatore Branch of DHFL were approximately Rs. 5.45 crores, whereas, the branch had income of Rs. 4.05 crores. Similarly, revenue of Kottayam branch was Rs. 50 lakhs and its expenses were about Rs. 1.01 crores and Thrissur Branch had revenue of Rs. 99 lakhs and expenses of Rs. 2.40 crores. The Appellants submitted that Risk of management override of controls was assessed as risk of material misstatement.

42. The Appellants refuted the non-compliance with Paras 6-10 of SA 300 as requirements of the said SA have been met by the Audit Plan documents and similarly allegations of non-compliance of with SA 315 and SA 330 for lack of documentation regarding the performance of risk assessment procedures for material misstatements at the financial statement level and assertion level and response to such risks. It is case of the Appellants that on the contrary, they had carried proper due diligence and examination of the records for assessment and identification of material misstatements and other risks that was tailored to meet the limited requirements of the Branch Audit including "Confirmation" given to Statutory Auditors' the extent of the branch auditor's responsibility to report on material departures in the accounting practices of the branches from significant accounting practices as described in the annual report of the company.

The Appellant emphatically submitted that since no misstatement of the any nature was noticed by them as branch auditors, they have not stated the presence of any misstatement in the overall evaluation and conclusion of misstatement.

43. The Appellants stated that the allegations made in relation to the Appellant's alleged failure to comply with SA 320 "Materiality in Planning and Performing Audit" and SA 450 "Evaluation of Identified Misstatements Identified During the Audit" and non-compliance of Paras 6 & 9 of SA 500 "Audit Evidence" (i.e., alleged failure to design and perform audit procedures to obtain sufficient appropriate audit evidences) are false as they had prepared the Audit Plan, Engagement Quality Assurance Review of Audit Engagement, Planning Meeting with Engagement Team, Independence Checklist with declaration by all the engagement partners and article assistants.

44. The Appellants emphasised that the Firm had undertaken branch audit of DHFL in previous three years also and therefore had a properly documented audit plans available in the audit files for previous years and therefore, documentation displaying an overall audit strategy and development of an audit plan for FY 2017-18 was felt not necessary.

45. It has been submitted that the total audit fees earned by the Firm was Rs 3,60,000, which indicated of the lower professional risk associated with the audit, low volume of transactions and lower risk of misstatement the Audit plan and strategy in such cases are not required to be complex that necessitate detailed documentation.

46. The EPs refuted that they have not complied with SA 520 and submitted that SA 520, deals with the auditor's use of analytical procedures as substantive procedures, and as procedures near the end of the audit that assist the auditors when forming an overall conclusion on the financial statements. It has been pointed out that as EPs their work was limited to auditing the Trial Balance of the branches, which did not reflect any operating assets or liabilities attributed to the Branches by virtue of ERP and therefore, no financial statements had been prepared for branches, nor was there any case to "form any overall conclusion" as provided in SA 520.

47. The Appellants refuted violation of SA 700 and highlighted that their role was confined only to conduct Branch Audits and as such SA 700 was not applicable to them. The Appellant submitted that expressing opinion on financial statements of DHFL as per SA 700 was responsibilities of CAS and the Appellants cannot be held responsible for the same.

48. The Appellant Mr. Harish Kumar TK filed an I.A. No. 2008 of 2023 in CA (AT) No. 68 of 2023, CA Ayna Tamton TK filed an I.A. No. 2402 of 2023 in CA (AT) No. 87 of 2023, CA M Baskaran filed an I.A. No. 2410 of 2023 in CA (AT) No. 90 of 2023 and CA Sam Varghese filed an I.A. No. 2413 of 2023 in CA (AT) No. 91 of 2023, whereby, they have requested for Interim Stay on the Impugned Orders.

49. It is the case of the Appellants that the Impugned Orders have serious ramification for their professional career and reputation. They have also raised issue regarding interpretation of Rule 11 and 12 of NFRA Rules, 2018. During averments the Appellants brought out that according to NFRA Rules, 2018 in case the Appellants deposit 10% of the amount of the

monetary penalty with the Appellate Tribunal and prefer the Appeal against the order of NFRA, then no communication regarding non-compliance should be made by NFRA to the concerned company or body corporate in which Auditors (the Appellants herein) are functioning as auditor, else such companies or body corporates are required to appoint new auditors in accordance with the provision of the Act.

50. The Appellants brought out that they have already deposited 10% of the penalty and have preferred the appeals before this Appellate Tribunal. The Appellants argued that therefore they have become entitled to get stay since they have deposited 10% of penalty and the Appeals have been made well in time.

51. Concluding arguments, the Appellants stated that the punishment of monetary penalty of Rs. 1,00,000/- on each of all four Appellants as well as debarment from auditing work for one year is far excessive and disproportionate to the Allegations and such findings of professional misconduct and penalties imposed will result in a grave consequence for the Appellants who are in process of building up their practices and good professional reputation over many years and maintenance of high ethical standards and requested this Appellate Tribunal to dismiss the Impugned Orders.

52. Per contra, the Respondent denied all averments of the Appellant to be false, misleading and mischievous. The Respondent gave background for establishing NFRA and cited judgment of ***'S. Sukumar' Vs. 'ICAI'*** *[(2018) 14 SCC 360].* The Respondent also gave the legislative object behind regulation

of auditors and cited judgment in the matter of ***'Union of India' Vs. Delloit Haskins'*** *[(2023) SCC OnLine SC 557].*

53. It is the case of the Respondent that after media report emerged in public regarding siphoning of public money of Rs. 31,000 Crores by promoters/ directors of DHFL and action by the Enforcement Directorate's reported action in April 2020 on an alleged banking fraud of about Rs.3700 crore by the promoter/ directors of DHFL, NFRA suo-motu initiated an Audit Quality Review (in short '**AQR**') to probe into the role of the Statutory Auditors of DHFL for the FY 2017-18, the year in which the alleged fraud was primarily stated to have occurred. While examining the Audit Files of the statutory audit carried out by Chaturvedi and Shah (in short '**CAS**'), certain prima-facie violations were observed relating to the appointment of Branch Auditors and the conduct of branch audits of DHFL which were relied upon by CAS

54. M/s K. Varghese & Co. ('**the Firm**') was the Auditors of 17 branches of DHFL. Accordingly, to examine the case, the Firm was requested on 10.08.2022, to submit the Audit Files along with some other information/documents. On 25.08.2022, the Audit Firm submitted the Audit Files along with other information in respect of 17 branches for FY 2017-18. After examination of the Audit Files and materials available on record, NFRA found prima-facie case of professional misconduct on the part of the EPs, four Appellants herein, who were found prima-facie guilty of professional mis-conduct and accordingly SCNs were issued to them under Rule 11 (1) of the NFRA Rules, 2018, giving them sufficient time to respond. The EPs were granted extension of time, based on their request for extension

of time for reply. The EPs submitted their replies along with Supplementary Audit Files containing certain additional documents purportedly from the Audit Files.

55. It is the case of the Respondent that keeping in view principles of natural justice and in accordance with Rule 11(5) of NFRA Rules 2018, the EPs were given opportunity for a personal hearing. However, the EPs did not avail of the offer of the personal hearing.

56. The Respondent stated that they examined all the materials on record including the written responses of the EPs, who were found guilty of charges of professional misconduct, and therefore four separate Impugned Orders were issued to the four Appellants herein, as detailed and well-reasoned speaking Impugned Orders showing the lapses, violations and professional misconduct of the Appellants.

57. The Respondent denied the averments of the Appellants that NFRA violated principles of natural justice on ground that no divisions were notified/ stipulated as required in the Companies Act, 2013 and NFRA Rules 2018. The Respondent submitted that as per Section 132(1A) of the Companies Act, 2013, "NFRA shall perform its functions through divisions, as may be prescribed", and the word "as may be prescribed" means if any prescribed. It is case of the Respondent that, NFRA has been functioning keeping in mind the principles of natural justice. In any case, by way of an amendment dated 13.11.2018 to Clause 2(g) of NFRA Rules, 2018, it has been stipulated that divisions means division including one headed by the chairperson or fulltime member for purpose of carrying out its functions and duties. Since, at the time of issue of SCNs as well as the Impugned Orders to

the Appellants, Clause 2(g) of NFRA Rules, 2018 clearly defined the division and as such as there was no illegality on the part of NFRA on this account. Moreover, the Appellants also were given opportunity for personal hearing which they denied and therefore, there have been no violation of natural justice.

58. It is case of the Respondent where power exists to prescribe the procedure and such power has not been exercised, the implementing authorities are at liberty to determine and adopt such procedure as they may deem fit subject to the same being fair and reasonable and relied upon the judgment of the Hon'ble Supreme Court in the matter of ***Ramjibhai Vs. State of Gujarat*** *[(1965) 2 SCC 5]* as well as om the matters of ***Chairman & MD, BP Ltd.' Vs. Gururaja & Ors***. *[(2003) 8 SCC 567].*

59. The Respondent argued that merely because the manner in which certain powers have to be exercised, has not yet been prescribed would not negate the existence of power itself. It is well settled that exercise of power conferred on an authority by a statute does not depend on the existence of rules or regulations and cited the judgment of the Hon'ble Supreme Court in the matter of ***Surinder Singh' Vs. Central Government & Ors.*** *[(1986) 4 SCC 667].*

60. The Respondent strongly refuted the issue raised by the Appellants regarding alleged retrospective jurisdiction exercised by NFRA against the settled law and the Appellants charged NFRA not having the authority to issue SCNs and consequently the Impugned Orders, since the audit of financial statements were done by the Appellants much prior period to the notification of MCA bringing NFRA into existence. In this connection, the

Respondent submitted that the notification of MCA bringing NFRA into existence, does not in any way alter the liability of the auditor to fully comply with the law. It is submitted that S. 132(4) of the Act is a non-obstante clause, hence, all cases fall within the jurisdiction of the NFRA. Additionally, Rule 10(3) of the NFRA Rules, 2018 clearly states that on the commencement of these rules, the action in respect of cases of professional or other misconduct against auditors of companies referred to in Rule 3 shall be initiated by the NFRA and no other institute or body shall initiate any such proceedings against such auditors. Thus, Respondent has exclusive jurisdiction in such matters.

61. The Respondent stated that the Retrospective applicability of Section 132 of Companies Act, 2013 could either be expressly provided for or can be inferred by necessary implication from the language employed. In this connection, the Respondent cited judgment of ***Zile Singh' Vs. State of Haryana',*** *[(2004) 8 SCC 1],* wherein the Hon'ble Supreme Court of India gave clear ratio that in such cases there would be no bar on the new authority like NFRA to look into such matters.

62. The Respondent emphasised that the Courts are obliged to look into the scheme and provisions of the law to ascertain whether the law, in effect, is retrospective or not and cited following judgments in his submission :-

(i) ***Commissioner of income Tax-1 Vs. Gold Coin Health Food Private Limited'****, [(2008) 9 SCC 622].*

(ii) ***Bijender Singh Vs. State of Haryana & Anr.*** *[(2005) 3 SCC 685].*

63. It is the case of the Respondent that in Article 20(1) of the Constitution, the expression "penalty" has been used in a narrow sense,

meaning a payment which has to be made for a deprivation of liberty which has to be suffered as a consequence of a finding that a person accused of a crime is guilty of the charge and cited case of the Hon'ble Supreme Court in the matter of ***Shiv Dutt Rai Fateh Chand' Vs. Union of India'*** *[(1983) 3 SCC 529].*

64. The Respondent further argued strongly that the protection against ex-post facto laws under the Constitution, does not extend to modes of procedure and would be limited to increasing of punishment or change in ingredients of offence and cited judgment in his support :-

(i) ***Gibson' Vs. State of Mississippi,*** *[162 US 565 (1896)].*

(ii) ***Rao Shiv Bahadur Singh' Vs. State of Vindhya Pradesh,*** *[(1953) 2 SCC 111].*

(iii) ***Sajjan Singh' Vs. State of Punjab,*** *[(1964) 4 SCR 630].*

(iv) ***Queens Vs. St. Mary Whitecaple****, [116 ER 811].*

(v) ***Om Prakash Shrivastava' Vs. State of NCT of Delhi'****, [2009 SCC OnLine Del 3264].*

(vi) ***Hitendra Vishnu Thakur' Vs. State of Maharashtra,*** *[(1994) 4 SCC 602].*

(vii) ***'Union of India' Vs, Sukumar Pune',*** *[(1966) 2 SCR 34].*

It is the case of the Respondent that the mischief sought to be remedied by the legislature, has to be kept in mind and cited case of ***Heydon's Case*** *[76 ER 637].*

65. It is the case of the Respondent that NFRA carefully examined all documents including detailed replies along with audit files and

documentations of the four Appellants herein, vis-à-vis SCNs issued to them and came to the conclusion that the replies of the Appellants were evasive and misleading, resulting establishing the facts that they the Appellants violated the several SAs.

66. The Respondent alleged that the Appellants did not comply with most of the Standards on Auditing (SAs) as applicable and further the Appellant had wrong and flawed understanding of SAS, inter alia, SA 210, SA 230, SA 315, SA 320, SA 330, SA 700 and section 143(8) of the Companies Act, 2013.

67. The Respondent gave detailed submissions alleged violations by the Appellants of various SAs. We have noted and shall further into all these averments during our discussion on Issue "True intent of Standard of Audits and other related standards relevant for audit and issue regarding alleged violation by the Appellants herein".

At this stage, we will record that the Respondent emphatically argued that the Appellants failed to adhere to SAs having statutory force. The Respondent reiterated that the Company i.e., DHFL, whose half of branches, were audited by the Appellants and DHFL was involved in fraud of Rs. 31,000 Crores and the Appellants are fully responsible for their areas.

68. The Respondent further denied the averments that the NFRA wrongly equated few provisions of Companies Act, 1956 to Companies Act, 2013 and further also allegation that the Chartered Accountants Act, 1949 referred to only Companies Act, 1956 and not Companies Act, 2013. In this connection, the Respondent elaborated that even prior to the 2022

amendment in Chartered Accountants Act, 1949, Section 22 of the Chartered Accountants Act, 1949 read with Clause (9) of Part I of the First Schedule to the said Act (the meaning of which is conceived in Section 132(4) as professional misconduct) and ICAI Code of Ethics 2009, a chartered accountant in practice shall be deemed to be guilty of professional misconduct if an appointment as auditor of a company is accepted without first ascertaining from it whether the requirements of Section 224, 224A and 225 of the Companies Act, 1956 have been complied with. The Respondent submitted that as per Ministry of Corporate Affairs Circular No. 7/2014, dated 01.04.2014, the equivalent sections of the Companies Act 2013 for the above sections of the Companies Act 1956 are sections 139 and 140. The Companies Act 2013 is only a continuation of the 1956 Act with necessary modifications as deemed fit by the Parliament. All matters covered in the old act are mutatis mutandis, continue to be effective and there is no specific need to amend the Chartered Accountants Act, 1949 in this regard.

69. It is the case of the Respondent that the Council in addition to "professional misconduct" as defined in Section 22 of the Chartered Accountants Act, 1949 has been given power to inquire into the conduct of any member of the institution under circumstances other than those specified in the Schedules to the Act. The Respondent relied on judgments of Hon'ble Supreme Court which are as follows :-

(i) ***Council of Institute of Chartered Accountants of India Vs. Y.K. Gupta*** *[(2010) SCC OnLine Del 4192].*

(ii) ***Council of Institute of Chartered Accountants of India' Vs. Mr. Rakesh Aggarwal****, [(2010) SCC OnLine Del 4012].*

(iii) ***ICAI' Vs. Vivek Kapoor*** *[(2016) SCC OnLine P7H 7501].*

70. The Respondent castigated the conduct of the Appellants for taking the stand that the appointment of the Branch Auditors was not required to be made under Section 139 of the Companies Act, 1956. As per Respondent, it seems that the Appellants did not even check the requirement of the Companies Act, 1956 since they believed that their appointments were not required to be made under Section 139 of the Companies Act, 1956. The Respondent stated that a change or removal of the branch auditor should be in compliance with Section 139 of the Companies Act, 1956 and in this connection, the MCA had issued a clarification, under the Companies Act, 1956, thus, unless a clarification to the contrary is issued, it would be logical to follow this approach which is:

> *"a. Department's Clarification. Where a Company proposes to entrust the auditing of branch from the Company's auditor to an outside auditor; wishes to change its branch auditor and where an branch accounts have not been previously audited and it is proposed to get them audited from to a person other than the Company's auditor the answer given to these proposals in the extract from minutes of Department's meeting, dated 2-6-1961 is that the term auditor as mentioned in section 225 means statutory auditor and it would be preferable if in all cases of appointments of auditors the procedure prescribed by section 225 is followed Minutes of Department's meeting, dated 2-6-1961]"*

71. The Respondent submitted that the Appellants themselves accepted that "the first appointment of the Appellant's Firm as branch auditor was

clearly in consonance with Section 139 of the Act" which appointed the appellant's firm as branch auditor for 5 years. First proviso to the then Section 139(1) stated that "the company shall place the matter relating to such appointment for ratification by members at every annual general meeting".

72. The Respondent refuted the contentions made by EPs regarding Peer Review Certification of the audit firm and stated that this plea is irrelevant since the proceedings by NFRA under section 132 (4) and the Peer Review conducted as per ICAI requirements are totally different in all aspects including the statutory mandate, scope and coverage. The contentions cannot be accepted for the reasons as the Appellants nowhere submitted any evidence to show that the peer reviewer has verified the matters contained in the SCN issued by NFRA. Moreover, there are inherent Limitations of Peer Review as the review would not necessarily disclose all weaknesses in compliance of technical standards and maintenance of quality of attestation services since it would be based on selective tests. As there are inherent limitations in the effectiveness of any system of quality control which happens to be subject-matter of review, departure from the system may occur and may not be detected.

73. It is the argument of the Respondent that mere sending copies of appointment letters to CAS or non- receipt of any special notice for their removal as branch auditors of DHFL as contemplated under Section 140(4)(i) and (ii) of the 2013 Act, did not absolve the Appellants of the mandatory requirements of Chartered Accountants Act, 1949 as detailed in the Impugned Orders.

74. The Respondent stated that in their Independent Branch Auditor's Report which Appellants had issued for the branches for as the EPs and certified under "**Auditor's Responsibility**" **that "we have taken into account provisions of the Companies Act, 2013, the accounting and auditing standards and matters which are required to be included in the audit report under the provisions of the Act and the Rules made there under. We conducted our audit in accordance with the Standards on auditing specified under Section 143(10) of the Act. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance".** It is the case of the Respondent that SAs are applicable for the branch statutory audit also and therefore, the Appellant's claim that there was no case to "form any overall conclusion" is required to be rejected since in their "Independent Branch Auditors' Report" the Appellants noted a positive overall conclusion on "true and fair view of the branch".

75. The Respondent pleaded that mere change of forum does not attract article 20 (1) of the constitution and relied upto the judgement of Hon'ble Supreme Court in the matter of ***New India Insurance Co. Ltd. Vs. Shanti Mishra*** *[(1975) 2 SCC 840]* and in the matter of ***Securities and Exchange Board of India' Vs. Classic Credit Ltd.',*** *Criminal Appeal No. 67 of 2011.*

76. The Respondent also pointed out that the public interest is a vital factor for passing orders of interim injunctions as laid down by the Hon'ble Supreme Court in ***Colgate Palmolive (India) Ltd. v. Hindustan Lever Ltd.,*** [*(1999) 7 SCC 1]*, where the Hon'ble Supreme Court held:

"24. We, however, think it fit to note herein below certain specific considerations in the matter of grant of interlocutory injunction, the basic being non-expression of opinion as to the merits of the matter by the court, since the issue of grant of injunction, usually, is at the earliest possible stage so far as the time- frame is concerned. The other considerations which ought to weigh with the court hearing the application or petition for the grant of injunctions are as below:

i) extent of damages being an adequate remedy;
(ii) protect the plaintiff's interest for violation of his rights though, however, having regard to the injury that may be suffered by the defendants by reason therefor,
(iii) the court while dealing with the matter ought not to ignore the factum of strength of one party's case being stronger than the other's;
(iv) no fixed rules or notions ought to be had in the matter of grant of injunction but on the facts and circumstances of each case- the relief being kept flexible;
(v) the issue is to be looked at from the point of view as to whether on refusal of the injunction the plaintiff would suffer irreparable loss and injury keeping in view the strength of the parties' case;
(vi) balance of convenience or inconvenience ought to be considered as an important requirement even if there is a serious question or prima facie case in support of the grant;"

(Emphasis Supplied)

77. The Respondent stated that since No prejudice caused to the petitioner hence the objection being purely technical deserves to be rejected

based on the ratio of ***State of Karnataka' Vs. Kuppuswamy Gownder*** *(1987) 2 SCC 74* and ***Fertico Marketing & Investment Pvt. Ltd. & Ors. Vs. Central Bureau of Investigation & Anr.*** *[(2021) 2 SCC 525].*

It is further argument of the Respondent that the doctrine of necessity is not allowed full play in certain unavoidable situations, it would impede the course of justice itself and the defaulting party would benefit therefrom and can be found in the judgments in the matters of ***Election Commission of India' Vs. 'Subramaniam*** *(1996) 4 SCC 104,* ***Om Pal Singh' Vs. 'Union of India', ILR*** *(2006) II Delhi I* and ***Clariant International Ltd. & Anr. Vs. Securities and Exchange Board of India [****(2004) 8 SCC 524].*

78. The Respondent refused the allegations of the Appellants that the Appellants were not given suitable opportunity to defend their cases and thereby, the Respondent violated the principles of natural justice. In this regard, the Respondent clarified that under Rule 11(5) of NFRA Rules, 2018, the Appellants were given clear opportunity for personal hearings which were not availed by the Appellants. The Respondent stated that at every stage, they complied all the required provisions of the law and rules and further principles of natural justice. The Respondent gave all opportunities from time to time in order to facilitate the Appellants to furnish their clarifications including by way of extension of time to submit their replies whenever requested.

79. The Respondent opposed vehemently the I.A. Nos. 2008 of 2023, 2402 of 2023, 2410 of 2023 and 2413 of 2023 filed by the Appellants in their respective appeals for seeking Interim Stay on the Impugned Orders passed

by NFRA. It is the case of the Respondent that the Appellants have created havoc in not doing their job as Auditors which resulted in non-detection of siphoning of Rs. 31,000 Crores by DHFL. It is also the case of the Respondent that this is wrong assumption on the part of the Appellants that by paying 10% of the penalty they become automatically entitled to get Interim Stay. The Respondent submitted that the 10% deduction of penalty provision in NFRA Rules, 2018 is applicable only when the monetary penalty is imposed and debarment penalty is not imposed. The Respondent clarified that debarment is done for serious offences and no stay is triggered automatically except on the merit of the case to be decided by the Appellate Tribunal. The Respondent, therefore, requested to dismiss al four I.A's seeking for Stay on the Impugned Orders under challenges in four appeals before this Appellate Tribunal.

80. Concluding the arguments, the Respondent emphasised that NFRA dealt with all four Appals with all sincerity, seriousness and keeping in view legal provisions and principles of natural justice and therefore urged this Appellate Tribunal to dismiss the Appeals.

Finding and Analysis

81. It is observed that DHFL is a company listed on the Bombay Stock Exchange and National Stock Exchange and therefore, as per Rules of the Companies (Indian Accounting Standards) Rules, 2015, it is required to comply with the Indian Accounting Standards (Ind AS) prescribed under these rules for the preparation and presentation of its annual financial statements.

82. From the detailed averments of the Appellants and the Respondent in all the four Appeals, which are based on common facts, background and charges regarding professional misconduct by the Appellants, this Appellate Tribunal observe that in order to finalize these Appeals, following issues are required to be deliberated and decided by us and we shall do accordingly.

Issues framed by us

83. Issue No. (I) Role of NFRA V/s ICAI on disciplinary matters of Chartered Accountants.

Issue No. (II) Retrospective V/s prospective applicability of provisions as contained in Section 132 of Companies Act, 2013 as well as NFRA Rules, 2018.

Issue No. (III) Violation of Principle of natural justice w.r.t. separate division of NFRA.

Issue No. (IV) Role of Statutory Auditors of the Company V/s Statutory Auditors of the Branches of the company.

Issue No. (V) Are Standards of Auditing (SA) mandatory or Advisory or to be treated as guidance notes to Auditors.

Issue No. (VI) What is professional misconduct for member of ICAI and legal provisions.

Issue No. (VII) True intent of Standard of Audits and other related standards relevant for audit and issue regarding alleged violation by the Appellants herein.

Issue No. (VIII) Alleged violation of the Code of Ethics issued by ICAI and impact on Appeals before this Appellate Tribunal.

Issue No. (IX) Excessive V/s adequate imposition of penalties on Appellants, herein.

Issue No. (X) Can automatic stay is triggered on deposit of 10% of penalty and appeal is made before NCLAT.

Provisions of Law

84. Before we take issues framed by us as above, it will be necessary and desirable to note all relevant sections and rules or portion thereof as applicable and relevant, inter-alia, of Companies Act, 2013, Companies Act, 1956, Chartered Accountants Act, 1949, notification by Ministry of Corporate Affairs, etc. These sections and rules have been quoted by both the Appellant and Respondent in their submissions and averments. These read as under :-

Section 224, 225 of Companies Act, 1956

> ***"224. APPOINTMENT AND REMUNERATION OF AUDITORS***
>
> *(1) Every company shall, at each annual general meeting, appoint an auditor or auditors to hold office from the conclusion of that meeting until the conclusion of the next annual general meeting and shall, within seven days of the appointment, give intimation thereof to every auditor so appointed:*****

(2) Subject to the provisions of sub-section (1B) and section 224A, at any annual general meeting, a retiring auditor, by whatsoever authority appointed, shall be re-appointed, unless –

(a) he is not qualified for re-appointment;
(b) he has given the company notice in writing of his unwillingness to be re-appointed;

225. PROVISIONS AS TO RESOLUTIONS FOR APPOINTING OR REMOVING AUDITORS.

(1) Special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor, or providing expressly that a retiring auditor shall not be re-appointed."

(Emphasis Supplied)

Companies Act, 2013

"132: Constitution of National Financial Reporting Authority.—

(1) The Central Government may, by notification, constitute a National Financial Reporting Authority to provide for matters relating to accounting and auditing standards under this Act.

[(1A) The National Financial Reporting Authority shall perform its functions through such divisions as may be prescribed.]

(2) Notwithstanding anything contained in any other law for the time being in force, the National Financial Reporting Authority shall—

(a) make recommendations to the Central Government on the formulation and laying down of accounting and auditing policies and standards for adoption by companies or class of companies or their auditors, as the case may be;

(b) monitor and enforce the compliance with accounting standards and auditing standards in such manner as may be prescribed;

(c) oversee the quality of service of the professions associated with ensuring compliance with such standards, and suggest measures required for improvement in quality of service and such other related matters as may be prescribed; and

(d) perform such other functions relating to clauses (a), (b) and (c) as may be prescribed.

***

[(3A) Each division of the National Financial Reporting Authority shall be presided over by the Chairperson or a full-time Member authorized by the Chairperson.

(3B) There shall be an executive body of the National Financial Reporting Authority consisting of the Chairperson and full-time Members of such Authority for efficient discharge of its functions under sub-section (2) [other than clause (a) and sub-section (4).]

(4) Notwithstanding anything contained in any other law for the time being in force, the National Financial Reporting Authority shall—

(a) have the power to investigate, either suo motu or on a reference made to it by the Central Government, for such class of bodies corporate or persons, in such manner as

may be prescribed into the matters of professional or other misconduct committed by any member or firm of chartered accountants, registered under the Chartered Accountants Act, 1949 (38 of 1949):

Provided that no other institute or body shall initiate or continue any proceedings in such matters of misconduct where the National Financial Reporting Authority has initiated an investigation under this section;

(b) have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit, in respect of the following matters, namely:—
(i) discovery and production of books of account and other documents, at such place and at such time as may be specified by the National Financial Reporting Authority;
(ii) summoning and enforcing the attendance of persons and examining them on oath;
(iii) inspection of any books, registers and other documents of any person referred to in clause (b) at any place;
(iv) issuing commissions for examination of witnesses or documents;

(c) where professional or other misconduct is proved, have the power to make order for—

(A) imposing penalty of—
(II) not less than one lakh rupees, but which may extend to five times of the fees received, in case of individuals; and
(III) not less than [five lakh rupees], but which may extend to ten times of the fees received, in case of firms;

[(B) debarring the member or the firm from—

I. being appointed as an auditor or internal auditor or undertaking any audit in respect of financial statements or internal audit of the functions and activities of any company or body corporate; or

II. performing any valuation as provided under section 247, for a minimum period of six months or such higher period not exceeding ten years as may be determined by the National Financial Reporting Authority.]

Explanation.— For the purposes of this sub-section, the expression "professional or other misconduct" shall have the same meaning assigned to it under section 22 of the Chartered Accountants Act, 1949 (38 of 1949).

(5) Any person aggrieved by any order of the National Financial Reporting Authority issued under clause (c) of sub-section (4), may prefer an appeal before [the Appellate Tribunal in such manner and on payment of such fee as may be prescribed].

(10) The National Financial Reporting Authority shall meet at such times and places and shall observe such rules of procedure in regard to the transaction of business at its meetings in such manner as may be prescribed.

***139. Appointment of auditors.—** (1) Subject to the provisions of this Chapter, every company shall, at the first annual general meeting, appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting and the manner and procedure of selection of auditors by the members of the company at such meeting shall be such as may be prescribed:*

Provided further that before such appointment is made, the written consent of the auditor to such appointment, and a certificate from him or it that the appointment, if made, shall be in accordance with the conditions as may be prescribed, shall be obtained from the auditor:

Provided also that the certificate shall also indicate whether the auditor satisfies the criteria provided in section 141:

Provided also that the company shall inform the auditor concerned of his or its appointment, and also file a notice of such appointment with the Registrar within fifteen days of the meeting in which the auditor is appointed.

Explanation.—For the purposes of this Chapter, "appointment" includes reappointment.

(3) Subject to the provisions of this Act, members of a company may resolve to provide that—

(a) in the audit firm appointed by it, the auditing partner and his team shall be rotated at such intervals as may be resolved by members; or

(b) the audit shall be conducted by more than one auditor.

***

(i) in the case of a company other than a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Board of Directors within thirty days, but if such casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting;

(ii) in the case of a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Comptroller and Auditor-General of India within thirty days:

Provided that in case the Comptroller and Auditor-General of India does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next thirty days.

(9) Subject to the provisions of sub-section (1) and the rules made thereunder, a retiring auditor may be re-appointed at an annual general meeting, if—

(a) he is not disqualified for re-appointment;
(b) he has not given the company a notice in writing of his unwillingness to be re-appointed; and
(c) a special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed.

(10) Where at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

(11) Where a company is required to constitute an Audit Committee under section 177, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee.

140. Removal, resignation of auditor and giving of special notice.— *(1) The auditor appointed under section 139 may be removed from his office before the expiry of his term only by a special resolution of the company, after*

obtaining the previous approval of the Central Government in that behalf in the prescribed manner:

Provided that before taking any action under this sub-section, the auditor concerned shall be given a reasonable opportunity of being heard.

***

(4) (i) Special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor, or providing expressly that a retiring auditor shall not be reappointed, except where the retiring auditor has completed a consecutive tenure of five years or, as the case may be, ten years, as provided under sub-section (2) of section 139.

***

(5) Without prejudice to any action under the provisions of this Act or any other law for the time being in force, the Tribunal either suo motu or on an application made to it by the Central Government or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors:

Provided that if the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall within fifteen days of receipt of such application, make an order that he shall not function as an auditor and the Central Government may appoint another auditor in his place:

Provided further that an auditor, whether individual or firm, against whom final order has been passed by the Tribunal under this section shall not be eligible to be appointed as an auditor of any company for a period of five years from the date of passing of the order and the auditor shall also be liable for action under section 447.

Explanation I.—It is hereby clarified that the case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

Explanation II.—For the purposes of this Chapter the word "auditor" includes a firm of auditors.

141. Eligibility, qualifications and disqualifications of auditors.— *(1) A person shall be eligible for appointment as an auditor of a company only if he is a chartered accountant:*

Provided that a firm whereof majority of partners practising in India are qualified for appointment as aforesaid may be appointed by its firm name to be auditor of a company.

(2) Where a firm including a limited liability partnership is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm.

142. Remuneration of auditors.— *(1) The remuneration of the auditor of a company shall be fixed in its general meeting or in such manner as may be determined therein:*

Provided that the Board may fix remuneration of the first auditor appointed by it.

143. Powers and duties of auditors and auditing standards.— *(1) Every auditor of a company shall have a right of access at all times to the books of account and vouchers of the company, whether kept at the registered office of the company or at any other place and shall be entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor and amongst other matters inquire into the following matters, namely:—*

(a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;

(b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;

(c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities have been sold at a price less than that at which they were purchased by the company;

(d) whether loans and advances made by the company have been shown as deposits;

(e) whether personal expenses have been charged to revenue account;

(f) where it is stated in the books and documents of the company that any shares have been allotted for cash,

whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading:

Provided that the auditor of a company which is a holding company shall also have the right of access to the records of all its subsidiaries and associate companies in so far as it relates to the consolidation of its financial statements with that of its subsidiaries and associate companies.

(2) The auditor shall make a report to the members of the company on the accounts examined by him and on every financial statements which are required by or under this Act to be laid before the company in general meeting and the report shall after taking into account the provisions of this Act, the accounting and auditing standards and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under sub-section (11) and to the best of his information and knowledge, the said accounts, financial statements give a true and fair view of the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year and such other matters as may be prescribed:

Provided that until the National Financial Reporting Authority is constituted under section 132, the Central Government may hold consultation required under this sub-section with the Committee chaired by an officer of the rank of Joint Secretary or equivalent in the Ministry of Corporate Affairs and the Committee shall have the representatives from the Institute of Chartered

Accountants of India and Industry Chambers and also special invitees from the National Advisory Committee on Accounting Standards and the office of the Comptroller and Auditor General.

(3) The auditor's report shall also state—

(a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;

(b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;

(c) whether the report on the accounts of any branch office of the company audited under subsection (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

(d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;

(g) whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate internal financial controls with reference to financial statements in place and the operating effectiveness of such controls;

(j) such other matters as may be prescribed.

(4) Where any of the matters required to be included in the audit report under this section is answered in the negative or with a qualification, the report shall state the reasons therefor.

***

(8) ***Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company (herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section 139, or where the branch office is situated in a country outside India, the accounts*** *of the branch office shall be* ***audited either by the company's auditor*** *or* ***by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country*** *and the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as may be prescribed:*

Provided that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to

the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

(9) ***Every auditor shall comply with the auditing standards****.*

(10) The Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949 (38 of 1949), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority:

Provided that until any auditing standards are notified, any standard or standards of auditing specified by the Institute of Chartered Accountants of India shall be deemed to be the auditing standards.

(11) The Central Government may, in consultation with the National Financial Reporting Authority, by general or special order, direct, in respect of such class or description of companies, as may be specified in the order, that the auditor's report shall also include a statement on such matters as may be specified therein.

(12) ***Notwithstanding anything contained in this section, if an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amounts as may be prescribed is being or has been committed against the company*** *by officers or employees of the company,* ***he shall immediately report the matter to the Central Government*** *within such time and in such manner as may be prescribed:*

Provided that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed.

145. Auditor to sign audit reports, etc.— *The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of sub-section (2) of section 141, and the qualifications, observations or comments on financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.*

146. Auditors to attend general meeting.— *All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company, and the auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorised representative, who shall also be qualified to be an auditor, any general meeting and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.*

147. Punishment for contravention.— *(1) If any of the provisions of sections 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.*

(2) If an auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees or four times the renumeration of the auditor, whichever is less:

Provided that if an auditor has contravened such provisions knowingly or wilfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year and with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees or eight times the renumeration of the auditor, whichever is less.

(3) Where an auditor has been convicted under sub-section (2), he shall be liable to—

(i) refund the remuneration received by him to the company; and

(ii) pay for damages to the company, statutory bodies or authorities or to members or creditors of the company for loss arising out of incorrect or misleading statements of particulars made in his audit report.

(4) The Central Government shall, by notification, specify any statutory body or authority or an officer for ensuring prompt payment of damages to the company or the persons under clause (ii) of subsection (3) and such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.

(5) Where, in case of audit of a company being conducted by an audit firm, it is proved that the partner or partners of the audit firm has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability, whether civil or criminal as provided in this Act or in any other law for the time being in force, for such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally:

Provided that in case of criminal liability of an audit firm, in respect of liability other than fine, the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud shall only be liable."

(Emphasis Supplied)

NFRA Rules, 2018

*"**2.(g)** "Division" means a division [including the one headed by the chairperson or a full-time member] established by the Authority for the purpose of organizing and carrying out its functions and duties.*

***Rule 3: Classes of companies and bodies corporate governed by the Authority. –** (1) The Authority shall*

have power to monitor and enforce compliance with accounting standards and auditing standards, oversee the quality of service under sub-section (2) of section 132 or undertake investigation under sub-section (4) of such section of the auditors of the following class of companies and bodies, namely: -

(a) Companies whose securities are listed on any stock exchange in India or outside India;

(b) Unlisted public companies having paid-up capital of not less than rupees five hundred crores or having annual turnover of not less than rupees one thousand crores or having, in aggregate, outstanding loans, debentures and deposits of not less than rupees five hundred crores as on the 31st March of immediately preceding financial year;

(c) insurance companies, banking companies, companies engaged in the generation or supply of electricity, companies governed by any special Act for the time being in force or bodies corporate incorporated by an Act in accordance with clauses (b), (c), (d), (e) and (f) of sub-section (4) of section 1 of the Act.

Explanation. For the purpose of this clause, "banking company includes "corresponding new bank" as defined in clause (d) of section 2 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970) and clause (b) of section 2 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (40 of 1980) and "subsidiary bank" as defined in clause (k) of section 2 of the State Bank of India (Subsidiary Bank) Act, 1959 (38 of 1959).

(d) Any body corporate or company or person, or any class of bodies corporate or companies or persons, on a reference made to the Authority by the Central Government in public interest; and

(e) a body corporate incorporated or registered outside India, which is a subsidiary or associate company of any company or body corporate incorporated or registered in India as referred to in clauses (a) to (d), if the income or networth of such subsidiary or associate company exceeds twenty per cent of the consolidated income or consolidated networth of such company or the body corporate, as the case may be, referred to in clauses (a) to (d).

(2) Every existing body corporate other than a company governed by these rules, shall inform the Authority within thirty days of the commencement of these rules, in Form NFRA-1, the particulars of the auditor as on the date of commencement of these rules.

(3) Every body corporate, other than a company as defined in clause (20) of section 2, formed in India and governed under this rule shall, within fifteen days of appointment of an auditor under sub-section (1) of section 139, inform the Authority in Form NFRA-1, the particulars of the auditor appointed by such body corporate:

Provided that a body corporate governed under clause (e) of sub-rule (1) shall provide details of appointment of its auditor in Form NFRA-1.

(4) A company or a body corporate other than a company governed under this rule shall continue to be governed by the Authority for a period of three years after it ceases to be listed or its paid-up capital or turnover or aggregate of loans, debentures deposits falls below the limit stated therein."

(Emphasis Supplied)

Chartered Accountants Act, 1949

"21. Disciplinary Directorate:

(1) The Council shall, by notification2, establish a Disciplinary Directorate headed by an officer of the Institute designated as Director (Discipline) and such other employees for making investigations in respect of any information or complaint received by it.

(2) On receipt of any information or complaint along with the prescribed fee, the Director (Discipline) shall arrive at a prima facie opinion on the occurrence of the alleged misconduct.

(3) Where the Director (Discipline) is of the opinion that a member is guilty of any professional or other misconduct mentioned in the First Schedule, he shall place the matter before the Board of Discipline and where the Director (Discipline) is of the opinion that a member is guilty of any professional or other misconduct mentioned in the Second Schedule or in both the Schedules, he shall place the matter before the Disciplinary Committee.

(4) In order to make investigations under the provisions of this Act, the Disciplinary Directorate shall follow such procedure as may be specified .

(5) Where a complainant withdraws the complaint, the Director (Discipline) shall place such withdrawal before the Board of Discipline or, as the case may be, the Disciplinary Committee, and the said Board or Committee may, if it is of the view that the circumstances so warrant, permit the withdrawal at any stage.]

22. Professional or other misconduct defined

For the purposes of this Act, the expression "professional or other misconduct" shall be deemed to include any act or omission provided in any of the Schedules, but nothing in this Section shall be construed to limit or abridge in any way the power conferred or duty cast on the Director (Discipline) under sub-section (1) of Section 21 to inquire into the conduct of any member of the Institute under any other circumstances.

THE FIRST SCHEDULE

PART I : Professional misconduct in relation to chartered accountants in practice

A chartered accountant in practice shall be deemed to be guilty of professional misconduct, if he –

(1) allows any person to practice in his name as a chartered accountant unless such person is also a chartered accountant in practice and is in partnership with or employed by him;

(2) pays or allows or agrees to pay or allow, directly or indirectly, any share, commission or brokerage in the fees or profits of his professional business, to any person other than a member of the Institute or a partner or a retired partner or the legal representative of

a deceased partner, or a member of any other professional body or with such other persons having such qualifications as may be prescribed, for the purpose of rendering such professional services from time to time in or outside India.

Explanation – In this item, "partner" includes a person residing outside India with whom a chartered accountant in practice has entered into partnership which is not in contravention of item (4) of this Part;

(3) accepts or agrees to accept any part of the profits of the professional work of a person who is not a member of the Institute: Provided that nothing herein contained shall be construed as prohibiting a member from entering into profit sharing or other similar arrangements, including receiving any share commission or brokerage in the fees, with a member of such professional body or other person having qualifications, as is referred to in item (2) of this Part;

(4) enters into partnership, in or outside India, with any person other than a chartered accountant in practice or such other person who is a member of any other professional body having such qualifications as may be prescribed, including a resident who but for his residence abroad would be entitled to be registered as a member under clause (v) of sub-section (1) of Section 4 or whose qualifications are recognised by the Central Government or the Council for the purpose of permitting such partnerships;

(5) secures, either through the services of a person who is not an employee of such chartered accountant or who is not his partner or by means which are not open to a chartered accountant, any professional business:

Provided that nothing herein contained shall be construed as prohibiting any arrangement permitted in terms of items (2), (3) and (4) of this Part;

(6) solicits clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means:

Provided that nothing herein contained shall be construed as preventing or prohibiting– any chartered accountant from applying or requesting for or inviting or securing professional work from another chartered accountant in practice; or (ii) a member from responding to tenders or enquiries issued by various users of professional services or organisations from time to time and securing professional work as a consequence;

(7) advertises his professional attainments or services, or uses any designation or expressions other than chartered accountant on professional documents, visiting cards, letter heads or sign boards, unless it be a degree of a University established by law in India or recognised by the Central Government or a title indicating membership of the Institute of Chartered Accountants of India or of any other institution that has been recognised by the Central Government or may be recognised by the Council: Provided that a member in practice may advertise through a write up setting out the services provided by him or his firm and particulars of his firm subject to such guidelines2 as may be issued by the Council;

(8) accepts a position as auditor previously held by another chartered accountant or a certified auditor who has been issued certificate under the Restricted Certificate Rules, 1932 without first communicating with him in writing;

(9) accepts an appointment as auditor of a company without first ascertaining from it whether the requirements of Section 225 of the Companies Act, 1956 in respect of such appointment have been duly complied with;*

(10) charges or offers to charge, accepts or offers to accept in respect of any professional employment, fees which are based on a percentage of profits or which are contingent

upon the findings, or results of such employment, except as permitted under any regulation made under this Act;

(11) engages in any business or occupation other than the profession of chartered accountant unless permitted by the Council so to engage: Provided that nothing contained herein shall disentitle a chartered accountant from being a director of a company (not being a managing director or a whole time director) unless he or any of his partners is interested in such company as an auditor;

(12) allows a person not being a member of the Institute in practice, or a member not being his partner to sign on his behalf or on behalf of his firm, any balance-sheet, profit and loss account, report or financial statements.

PART II : Professional misconduct in relation to members of the Institute in service

A member of the Institute (other than a member in practice) shall be deemed to be guilty of professional misconduct, if he being an employee of any company, firm or person–(1) pays or allows or agrees to pay directly or indirectly to any person any share in the emoluments of the employment undertaken by him;

(2) accepts or agrees to accept any part of fees, profits or gains from a lawyer, a chartered accountant or broker engaged by such company, firm or person or agent or customer of such company, firm or person by way of commission or gratification.

PART III : Professional misconduct in relation to members of the Institute generally

A member of the Institute, whether in practice or not, shall be deemed to be guilty of professional misconduct, if he–

(1) not being a fellow of the Institute, acts as a fellow of the Institute;

(2) does not supply the information called for, or does not comply with the requirements asked for, by the Institute, Council or any of its Committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the Appellate Authority; (3) while inviting professional work from another chartered accountant or while responding to tenders or enquiries or while advertising through a write up, or anything as provided for in items (6) and (7) of Part I of this Schedule, gives information knowing it to be false.

PART IV : Other misconduct in relation to members of the Institute generally

A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he– (1) is held guilty by any civil or criminal court for an offence which is punishable with imprisonment for a term not exceeding six months;

(2) in the opinion of the Council, brings disrepute to the profession or the Institute as a result of his action whether or not related to his professional work"

THE SECOND SCHEDULE

PART I : Professional misconduct in relation to chartered accountants in practice

A chartered accountant in practice shall be deemed to be guilty of professional misconduct, if he–

(1) discloses information acquired in the course of his professional engagement to any person other than his client so engaging him, without the consent of his client or otherwise than as required by any law for the time being in force;

(2) certifies or submits in his name, or in the name of his firm, a report of an examination of financial statements unless the examination of such statements and the related records has been made by him or by a partner or an employee in his firm or by another chartered accountant in practice;

(3) permits his name or the name of his firm to be used in connection with an estimate of earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast;

(4) expresses his opinion on financial statements of any business or enterprise in which he, his firm, or a partner in his firm has a substantial interest;

(5) ***fails to disclose a material fact known to him which is not disclosed in a financial statement, but disclosure of which is necessary in making such financial statement where he is concerned with that financial statement in a professional capacity;***

(6) fails to report a material misstatement known to him to appear in a financial statement with which he is concerned in a professional capacity;

(7) does not exercise due diligence, or is grossly negligent in the conduct of his professional duties;

(8) fails to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion;

(9) fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances;

(10) fails to keep moneys of his client other than fees or remuneration or money meant to be expended in a separate banking account or to use such moneys for purposes for which they are intended within a reasonable time.

PART II : Professional misconduct in relation to members of the Institute generally

A member of the Institute, whether in practice or not, shall be deemed to be guilty of professional misconduct, if he–

(1) contravenes any of the provisions of this Act or the regulations made thereunder or any guidelines issued by the Council;

(2) being an employee of any company, firm or person, discloses confidential information acquired in the course of his employment except as and when required by any law for the time being in force or except as permitted by the employer;

(3) includes in any information, statement, return or form to be submitted to the Institute, Council or any of its Committees, Director (Discipline), Board of Discipline, Disciplinary Committee, Quality Review Board or the

Appellate Authority any particulars knowing them to be false;

(4) defalcates or embezzles moneys received in his professional capacity.

PART III : Other misconduct in relation to members of the Institute generally

A member of the Institute, whether in practice or not, shall be deemed to be guilty of professional other misconduct, if he is held guilty by any civil or criminal court for an offence which is punishable with imprisonment for a term exceeding six months."

(Emphasis supplied)

Rule 12 (1) of Company (Audit and Auditors) Rules 2014

"(1) For the purposes of sub-Section (8) of Section 143, the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in sub-Sections (1) to (4) of Section 143 which makes it clear that even for the audit of the branches of a company, the responsibility of auditors as provided in Section 143(1) 143(4) are on the company's auditor and not on the Branch Auditor."

(Emphasis Supplied)

85. <u>Issue No. (I)</u> <u>Role of NFRA V/s ICAI on disciplinary matters of Chartered Accountant.</u>

- At the outset this Appellate Tribunal consider discipline among professionals to be of utmost importance. The profession of Chartered Accountants, who are involved in accounting and auditing work, are governed by the Chartered Accountant Act, 1949, being members of ICAI. Section 22 of the Chartered Accountant Act, 1949, along with Schedule I & II describes the professional misconduct of the members of the ICAI.
- The Institute of Chartered Accountants of India is the statutory body which regulates the profession of Chartered Accountants in India. ICAI was set-up by the act of parliament. It was formed under Chartered Accountants Act, 1949 to regulate the professionalism of its members including auditors in India. Every member of ICAI is duty bound to follow the professional standards and code of ethics ICAI. It needs to be appreciated that any violation of professional standards and code of ethics, results in disciplinary issue and ICAI is required to take action against the member of ICAI. The disciplinary board of ICAI is entrusted to take action against its members who are found guilty of professional misconduct, under the Chartered Accountants Act, 1949. It is the duty of the Disciplinary Directorate of the ICAI to keep watch on alleged irregularities committed by its members. There are prescribed procedures to investigate the misconduct and it is notified by the Central Government under provisions of Section 21

of Chartered Accountants Act of 1949, which we have already noted earlier.

- We note that prior to 2006, decisions of ICAI disciplinary committees had to be approved by the High Court having jurisdiction. However, after the 2006 amendment to the Chartered Accountants Act, 1949, disciplinary committees were empowered to decide cases brought before them and impose a penalty on an auditor without the approval of the High Court.
- Under the Chartered Accountants Act, the monetary penalty that may be imposed on individual auditors is capped at Rs 5,00,000 and there is no provision for imposing a penalty on audit firms.
- After the ill famous Satyam Scandal which took place in 2009, the concept of an independent regulator was considered and recommended the by "Parliamentary Standing Committee on Finance" (in short **'SCOF')**. The SCOF proposed in its 21st Report the concept of NFRA which was finally approved by Government of India on 01.03.2018 and subsequently necessary amendments were made in Section 132 of the Companies Act, 2013 to create NFRA. The objective of NFRA is to act as an independent regulatory body for improving transparency and reliability of financial statements and information of companies in India after Statutory Audit by the Chartered Accountants.
- Prior to formation of NFRA, the responsibility of regulating the accounting and auditing professionals was within sole dominance of ICAI who used to regulate Auditors under Chartered

Accountants Act, 1949. However, over the period; somewhat impression was created that the required level of discipline and accountability from Chartered Accountants was becoming the challenge due to self-regulation and therefore, the SCOF recommended for NFRA.

- It is worthwhile to note that ICAI continues to be responsible and authority for conducting examination, registering members, investigate conduct of its members who are auditors of all private companies and those public companies which are not covered under Section 132 of the Companies Act, 2013.
- As per data available on the website of MCA (8th Annual Report) the total no of registered companies in India are 14,28,372 having Rs. 89,06,751.76 Crores as authorised capital. Out of these total companies as on 31.03.2022, the total Public Limited Companies registered in India are 67,451 out of which 60,708 are unlisted companies and only public 6,743 companies are listed. Remaining 13,60,921 are Private Limited Companies. Thus, 95.95% of total registered companies in India as on 31.03.2022 (as per 8th Annual Report of MCA- tables 3.16 & 3.17) are Private Limited Companies. Auditors of such large no. of Companies are still regulated by ICAI exclusively.

Source :- 8th Annual Report of Ministry of Corporate Affairs (MCA)

Active Companies as on 31st March, 2022

(₹ in crore)

Sl. No.	Type of Company	Number	Authorized capital
(1)	(2)	(3)	(4)
I	**Companies Limited by Shares**	**14,28,372**	**89,06,751.76**
	(a) Government Companies	2,171	23,91,066.00
	i) Public	1,527	23,06,388.70
	ii) Private	644	84,677.30
	iii) OPC	0	0.00
	(b) Non- Government Companies	14,26,201	65,15,685.75
	i) Public	65,924	35,35,953.82
	ii) Private	13,17,253	29,78,227.04
	iii) OPC	43,024	1,504.88
II	**Companies with Unlimited Liability**	**297**	**8,526.49**
	(a) Government Companies	4	1,065.00
	(b) Non- Government Companies	293	7,461.49
III	**Liability limited by Guarantee**	**9,376**	**2,742.23**
	(a) Government Companies	29	732.06
	(b) Non- Government Companies	9,347	2,010.17
Total		**14,38,045**	**89,18,020.47**

Active Companies Limited by Shares as on 31st March, 2022

Sl. No.	Companies Limited by Shares	Government	Non-Government	Total
(1)	(2)	(3)	(4)	(5)
1.	**Public Limited**	**1,527**	**65,924**	**67,451**
	Of which -			
I	Listed	79	6,664	6,743
II	Unlisted	1,448	59,260	60,708

Sl. No.	Companies Limited by Shares	Government	Non-Government	Total
(1)	(2)	(3)	(4)	(5)
2.	**Private Limited**	**644**	**13,60,277**	**13,60,921**
	Of which -			
	One Person Company	0	43,024	43,024
Total		**2,171**	**14,26,201**	**14,28,372**

- The role of ICAI, therefore, can't be underestimated. The role of NFRA is all together different, of-course, having overriding powers over ICAI for the companies covered under Section 132 of the Companies Act, 2013.
- We note that the Hon'ble Supreme Court of India in its landmark judgment in the matter of ***S. Kumar Vs. Secretary ICAI & Ors***. *[(2018) 14 SCC 2018]* dated 26.02.2018 issued direction to Government for considering suitable mechanism and law for oversight of auditors on the lines of Sarbanes Oxley Act, 2002 [which came after Enron episode and resulted into establishment of Public Company Accounting Oversight Board ("**PCAOB**")] in U.S.A.
- The relevant para in matter of ***S. Sukumar and Ors. (Supra)*** reads as under:-

> *"49. It can hardly be disputed that profession of auditing is of great importance for the economy. Financial statements audited by qualified auditors are acted upon and failures of the auditors have resulted into scandals in the past. The auditing profession requires proper oversight. Such oversight mechanism needs to be revisited from time to time. It has been pointed out that post Enron Anderson Scandal, in the year 2000, Sarbanse Oxley Act was enacted in U.S. requiring corporate leaders to personally certify the accuracy of their company's financials. The Act also lays down Rules for functioning of audit companies with a view to prevent the corporate analysts from benefitting at the cost of*

public interest. The audit companies were also prohibited from providing non audit services to companies whose audits were conducted by such auditors. Needless to say that absence of adequate oversight mechanism has the potential of infringing public interest and Rule of law which are part of fundamental rights Under Articles 14 and 21. It appears necessary to realise that auditing business is required to be separated from the consultancy business to ensure independence of auditors. The accounting firms could not be left to self regulate themselves."

(Emphasis Supplied)

- We therefore, note important aspects arising from above judgment:-
  a) Audit is very critical for economy.
  b) Audited financial statement are relied and acted upon by the Stakeholders including investors.
  c) Failure of Auditors may lead to scams and frauds.
  d) Auditing profession needs to be properly regulated.
  e) Audit professional should not be left self regulated.
  f) Absence of proper audit oversight mechanism leads to infringing public interest and violate Art 14 and 21 of the constitution.
- NFRA assist and suggest the Government, regarding the Accounting and Auditing policies and standards that the companies need to adopt and follow. NFRA also monitor enforcement of accounting and auditing standards. It oversees professionalism is maintained by the

auditors and suggests improvements that are needed in uplifting the quality of service in the audit profession.

- NFRA has also been given the responsibility of Audit Quality Review (AQR). The main objective of the AQR is to access the quality control system of the audit firm and the extent to which the quality control system has been complied with the auditing standards. NFRA has the authority to ask auditors to report on its governance practices and internal processes established to promote Audit Quality.
- NFRA has the power to investigate the professional misconduct of the auditors and the law states that, if NFRA starts investigating on any case, no other institution has the power to continue or initiate any proceeding against the same case. This reduces the power of ICAI to act against the professional wrongdoing of its members as stipulated in Section 132 of the Companies Act, 2013. Before the formation of NFRA, ICAI had the exclusive right to take any action against the professional misconduct of its auditors.
- There are many regulatory bodies which govern the audit governance of the listed and unlisted companies in India including NFRA, ICAI, MCA and SEBI. Out of these, NFRA and ICAI are established for the similar objective to protect the interest of creditors, investors, and other parties who are directly or indirectly associated with companies.
- The jurisdiction of SEBI over the conduct of auditors and audit firms is related to their involvement in defrauding investors and thus narrower than that of the ICAI. The NFRA has more flexibility when it

comes to imposing penalty on auditors and audit firms and it has a broader mandate than SEBI.

- The notification of NFRA does not in any way alter the liability of the statutory auditors to fully comply with the law. NFRA's authority to monitor and enforce compliance with the accounting and auditing standards is with reference to such standards as were established by law even earlier and are binding on statutory auditors. SAs are part of the law of the land and are required to be mandatorily complied with from the date of their respective applicability, while conducting statutory audits. Hence, no new obligation is created on the Appellants and these standards were to be mandatorily followed even prior to NFRA's establishment. Section 132(4) merely designates NFRA as the forum for determination of professional misconduct. No. litigant has or can have vested rights in a particular forum.
- NFRA has jurisdiction to enforce compliance with auditing and accounting standards with respect to the entities listed in the NFRA Rules, 2018 and Companies Act, 2013 which we have already taken note our earlier discussion.
- We also note that the Hon'ble Supreme Court in another matter of ***Union of India and Another V/s Deloitte Haskins and Sells LLP & Anr.,*** Criminal Appeal Nos.2305- 2307 of 2022 reiterated the role and importance of auditors and, inter-alia, observed as under:

> *"13. It is required to be noted that the role of auditors cannot be equated with directors and/or management. Auditors play very important role in the affairs of the*

company and therefore they have to act in the larger public interest and all other stakeholders including investors etc."

(Emphasis Supplied)

- After going through provision of Chartered Accountant Act, 1949 and Companies Act, 2013 it becomes clear that disciplinary jurisdiction over the Chartered Accountants remain with both the ICAI and NFRA on concurrent basis. However, on carefully reading it reveals that NFRA has superior and overriding powers in matters relating to professional misconduct of the Chartered Accountants in terms of Section 132 of Companies Act, 2013 as discussed in details earlier.
- On a pointed query to the Appellants to confirm our understanding, the Learned Counsel for the Appellant confirmed that both the ICAI and NFRA have jurisdiction over Chartered Accountant Act, 1949. We observe that for all matters, by default, ICAI has disciplinary jurisdiction over Chartered Accountant. However, it is required to be clearly understood that in term of Companies Act, 2013 and NFRA Rules, 2018 over important and serious matters especially involving large alleged accounting or financial frauds, or matters of public interest, etc., NFRA suo-moto can initiate investigation or take for investigating and ICAI will cease to exercise such disciplinary jurisdiction.
- Hence, we may conclude NFRA has been consciously and deliberately given superior authority over ICAI on oversight of auditors

and in disciplinary matters as stipulated in Section 132 of Companies Act, 2013.

- We clarify the Issue No. 1 accordingly.

Issue No. (II) Retrospective or prospective applicability of provisions as contained in Section 132 of Companies Act, 2013 as well as NFRA Rules, 2018.

- As a preliminary ground, it is the case of the Appellants that NFRA does not have any retrospective jurisdiction since NFRA itself was constituted on 01.10.2018 vide Ministry of Corporate Affairs (in short MCA) Notification dated 01.10.2018 and MCA also notified on 24.10.2018 as effective date for coming into force of Section 132(2), (4), (5), (10), (13), (14) & (15) of Companies Act, 2013. The Appellants submitted that NFRA Rules were notified on 13.11.2018, whereas the Financial Statements in question pertains to FY 2017-18 and Audit Reports for different branches were given on different dates which were prior to notification bringing NFRA into force, therefore, the NFRA did not have any jurisdiction to look into the period prior to its own formation on 01.10.2018. It is further the case of the Appellants that there is no mention regarding retrospective applicability in Section 132 of the Companies Act, 2013 or in the MCA Notification issued for the same.
- Two judgements have been brought to the notice of this Appellate Tribunal by the Appellant which gives constitutional protection under

Article 20 of the Constitution of India regarding non-Application of retrospectivity of penal statute:

(a) Maya Rani Punj' Vs. CIT, Income Tax, Delhi, *(1986) 1 SCC 445.*

(b) S.K. Ganesan' Vs. A.K. Joscelyne', *1956 SCC Online Cal 43.*

- It has been alleged by the Appellants that the issue regarding retrospective or prospective applicability of provisions as contained in Section 132 of Companies Act, 2013 as well as NFRA Rules, 2018, have not been appreciated by the Respondent in right perspective and exercised jurisdiction wrongly in all four cases by NFRA.' The Appellants claims that it is the settled law that no law which has got penal element or any law prescribing new offense can be done retrospectively.
- It is the case of the Appellants that if legislature had intentions of retrospectively, it would have made an express provision for same in Section 132 of the Companies Act, 2013 on this aspect.
- We will now look into judgments referred by the Appellants in their defence.
- ***Maya Rani Punj' Vs. CIT, Income Tax, Delhi',*** *(1986) 1 SCC 445.*

> *"9. Under Section 28 of the 1922 Act the upper limit of penalty only was provided and there was no prescription of any particular rate as found in Section 271(1)(a) of 1961 Act. That penalty contemplated under the respective sections of the two Acts quasi criminal in character is not disputed. Mr Dholakia for the appellant canvassed before us that in Jain Brothers case the challenge raised by the assessee was not examined with reference to the provisions of*

*Article 20(1) of the Constitution. Under sub-article (1) of Article 20 no person is to be subjected to a penalty greater than that which might have been inflicted under, the law in force at the time of the commission of the offence. According to counsel, when there was default in furnishing the return within September 28, 1961, the breach had occurred and the assessee had exposed himself to be visited with penalty. That was a time when the Act of 1922 was in force. Therefore, for levying penalty on the assessee resort should have been made to the provisions of Section 28 of the 1922 Act and not to Section 271(1)(a) of 1961 Act. If the 1922 Act applied, in the absence of a prescription of any particular rate or the minimum, it was open to the Tribunal to reduce the penalty***"*

(Emphasis Supplied)

- ***S.K. Ganesan' Vs. A.K. Joscelyne',*** *1956 SCC Online Cal 43.*

"18. In my opinion, the contention of Dr. Pal is not well-founded. It is true that in the case of statutes of a penal character which create certain offences and make certain acts punishable as such offences for the first time, no proceedings under them are generally maintainable in respect of acts done before the commencement of the statute, unless the statutes include such acts by express provision or necessary intendment. The reason is plain. The act which was not an offence at the time it was done under the law then prevailing, cannot become so by reason of the operation of some statute which itself came into existence at a subsequent date, speaking as from

then and making acts of the kind concerned, if thereafter done, offences. Looking at the matter from another point of view, it will be seen that, in such a case, the element of mens rea which is always a constituent of offences, unless specifically excluded, will also be lacking, because one cannot have a criminal intention in doing an act which is not a crime at the time at all. It may be said that cases of professional misconduct do not differ essentially from cases of offences. Two tests, however, must be looked for. Is the offence or misconduct created for the first time by the Act concerned and, secondly, does the Act contain any indication that activities of the kind mentioned are intended to be covered by its provisions, whenever they may have been done? In the present case whether acts of the types charged against the respondent would amount to misconduct under the prior law cannot be said for certain, because the Auditor's Certificate Rules, which constituted the prior law, left it to the Central Government to determine in each case whether a particular conduct on the part of an Auditor was or was not professional misconduct. As to indications in the Act itself regarding its retrospective operation, I shall presently examine its provisions. I may state, however, that in spite of the ordinary and I might almost say cardinal rule of construction that statutes, particularly statutes creating liabilities, ought not to be so construed as to give them a retrospective operation unless there is a clear provision to that effect or a necessary intendment implied in the provisions, there is another principle on which Courts have sometimes acted. It has been held that where

the object of an Act is not to inflict punishment on anyone but to protect the public from undesirable persons, bearing the stigma of a conviction or misconduct on their character, the ordinary rule of construction need not be strictly applied. ***

34. Judging by that test, I am unable to hold that the respondent acted in this case with reasonable care. The difficulty, however, is that he has been charged only under items (o) and (p) of the Schedule, but has not been charged under item (q) which is concerned with 'gross negligence' in the conduct of professional duties. Even apart from negligence, there might have been a ground for proceeding against the respondent if it could be established against him that he had been a willing party to or at least had connived at the concealment of the payment of the selling commission by the Directors. On that point again, there is the difficulty that the complainant withdrew the allegation that the respondent had acted with a desire to accommodate the Managing Agency and the Directors in regard to their concealing the payment of the commission. Speaking for myself, I am inclined to think that in a case of professional misconduct charged against an Accountant or a lawyer, the fact that the complainant withdraws a particular allegation cannot always be decisive or a reason for not pursuing an enquiry, for the object of such proceedings is to test the fitness of the person concerned, in the public interest, to exercise his profession. The fact, however, remains in the present case that not only was the allegation withdrawn but there has also been no further enquiry and, therefore, we have no right to assume that what was alleged

against the respondent actually happened. It is in view of the nature of the charges framed that we find it difficult to take any action in the matter. Mr. Meyer himself frankly conceded that since the allegation of deliberate accommodation of the Directors and the Managing Agents in the matter of concealing the payment of the selling commission had been withdrawn. It was difficult to establish that. nevertheless, the respondent had failed to disclose a material fact known to him or to report on a misstatement similarly known. For what purpose and for what reason he would fail to disclose the fact in one case and report it in the other is not intelligible, if he appreciated the fact to be material and appreciated the statement to be a misstatement, inasmuch as there is no longer any allegation or wilful participation in the concealment or connivance at it. All that can be said on the facts proved is that he failed to take normal and reasonable care in informing himself of the true position under S. 132(3) and Regulation 107 in relation to the Agreement and the Profit and Loss Account, as drawn up. The position, therefore, seems to be that in view of the absence of any charge of negligence and the withdrawal of the particular allegation, it is not possible to hold that the charges actually framed had been established, although, as I have found, the respondent does not appear to me to have acted with reasonable care.

(Emphasis Supplied)

- We find above quoted judgments although in context of Article 20 of the constitution, but are with different facts and circumstances in comparison to appeals before us and hence not considered as directly applicable here.
- A different perspective has been presented by the Respondent before us that express provision of applicability of coming into force of particular section of any Act with retrospective effect is not necessary and it can be inferred by implications by reading language of the statute, intent of the parliament, rational and objective behind bringing the law or changes in the law, precedents as available, judgments of Courts and so on.
- It has further been argued before us by the Respondent that on the same logic, any law which only empower a new authority in place of old authority or prescribes same or lesser penal provisions cannot be treated as retrospective application of jurisdiction.
- In this regard, we will refer to another judgment in the matter of ***Hitendra Vishnu Thakur and Ors. vs. State of Maharashtra and Ors.*** *[(1994) 4 SCC 602],* where it was held in Hon'ble Supreme Court that :-

> *"26. The Designated Court has held that the amendment would operate retrospectively and would apply to the pending cases in which investigation was not complete on the date on which the Amendment Act came into force and the challan had not till then been filed in the court. From the law settled by this Court in various cases, the illustrative though not*

exhaustive, principles which emerge with regard to the ambit and scope of an Amending Act and its retrospective operation may be culled out as follows:

(i) A statute which affects substantive rights is presumed to be prospective in operation, unless made retrospective, either expressly or by necessary intendment, whereas a Statute which merely affects procedure, unless such a construction is texturally impossible, is presumed to be retrospective in its application, should not be given an extended meaning, and should be strictly confined to its clearly defined limits.

(ii) Law relating to forum and limitation is procedural in nature, whereas law relating to right of action and right of appeal, even though remedial, is substantive in nature.

(iii) Every litigant has a vested right in substantive law, but no such right exists in procedural law.

(iv) A procedural Statute should not generally speaking be applied retrospectively, where the result would be to create new disabilities or obligations, or to impose new duties in respect of transactions already accomplished.

(v) A Statute which not only changes the procedure but also creates a new rights and liabilities, shall be construed to be prospective in operation, unless otherwise provided, either expressly or by necessary implication.

25. In fairness to the learned Additional Solicitor General Mr. Tulsi, it may be stated that he did not controvert the legal position (both in his oral submissions and written arguments) that Amendment

Act 43 of 1993 regulating the period of compulsory detention and the procedure for grant of bail, being procedural in nature, would operate retrospectively. We need not, therefore, detain ourselves to further examine the question of retrospective operation of the Amendment Act. On the basis of the submissions made by learned Counsel for the parties, we uphold the finding of the Designated Court, for the reasons recorded by it and those noticed by us above that the Amendment of 1993 would apply to the cases which were pending investigation on 22nd May 1993 and in which the challan had not till then been filed in court."

(Emphasis Supplied)

- In this connection, we would like to into details of the refer to judgment referred by both by the Appellants and the Respondent which has been pronounced by the Hon'ble Supreme Court of India in case of ***Zile Singh Vs. State of Haryana Reported in (2004) 8 SCC 1.***

"15. Though retrospectivity is not to be presumed and rather there is presumption against retrospectivity, according to Craies (Statute Law, 7th Edn.), it is open for the legislature to enact laws having retrospective operation. This can be achieved by express enactment or by necessary implication from the language employed. If it is a necessary implication from the language employed that the legislature intended a particular section to have a retrospective operation, the courts will give it such an operation. In the absence of a retrospective operation having been

expressly given, the courts may be called upon to construe the provisions and answer the question whether the legislature had sufficiently expressed that intention giving the statute retrospectivity. Four factors are suggested as relevant: (i) general scope and purview of the statute; (ii) the remedy sought to be applied; (iii) the former state of the law; and (iv) what it was the legislature contemplated. (p. 388) The rule against retrospectivity does not extend to protect from the effect of a repeal, a privilege which did not amount to accrued right. (p. 392)"

(Emphasis Supplied)

- From above judgments, it seems that if new law is made to take care of known wrongs for the benefits of society as a whole, then the express provision of retrospective application in new law may not be required and necessary implication need to be made out from the language employed. The said judgement list of factors to construe the provisions of the statute retrospectively i.e.,

  (a) General scope and purview of the statute;

  (b) The remedy sought to be applied.

  (c) The former state of the law,

  (d) What it was the legislature contemplated.

- In this connection we may safely rely on ratio laid down by Hon'ble Supreme Court of India in ***Securities and Exchange Board of India Vs. Classic Credit Ltd.*** *[Civil Appeal No. 67 of 2011],* where it was held as under :-

"34. We will now deal with the legality of the propositions canvassed, at the hands of learned counsel for the rival parties. In our considered view, the legal position expounded by this Court in a large number of judgments including New India Insurance Co. Ltd. v. Shanti Misra, (1975) 2 SCC 840; Securities and Exchange Board of India v. Ajay Agarwal, (2010) 3 SCC 765; and Ramesh Kumar Soni v. State of Madhya Pradesh, (2013) 4 SCC 696, is clear and unambiguous, namely, that procedural amendments are presumed to be retrospective in nature, unless the amending statute expressly or impliedly provides otherwise. And also, that generally change of 'forum' of trial is procedural, and normally following the above proposition, it is presumed to be retrospective in nature, unless the amending statute provides otherwise. This determination emerges from the decision of this Court in Hitendra Vishnu Thakur v. State of Maharashtra (1994) 4 SCC 602; Ranbir Yadav v. State of Bihar (1995) 4 SCC 392, and Kamlesh Kumar v. State of 72 Jharkhand, (2013) 15 SCC 460, as well as, a number of further judgments noted above."

(Emphasis Supplied)

86. We will also refer to yet another judgment of Hon'ble Supreme Court in the matter of ***New India Insurance Co. Ltd. Vs. Shanti Misra*** *[(1975) 2 SCC 840]*, where it was held that :-

"5. *On the plain language of Sections 110A and 11 of there should be no difficulty in taking the view that the change in law was merely a change of forum i. e.*

a change of adjectival or procedural law and not of substantive law. It is a well-established proposition that such a change of law operates retrospectively and the person has to go to the new forum even if his cause of action or right of action accrued prior to the change of forum. He will have a vested right of action but not a vested right of forum. If by express words the new forum is made available only to causes of action arising after the creation of the forum, then the retrospective operation of the law is taken away; Otherwise the general rule is to make it retrospective. The expressions "arising out of an accident" occurring in Sub-section (1) and "over the area in which the accident occurred", mentioned in Sub-section (2) clearly show that the change of forum was meant to be operative retrospectively irrespective of the fact as to when the accident occurred. To that extent there was no difficulty in giving the answer in a simple way. But the provision of limitation of 60 days contained in Sub-section (3) created an obstacle in the straight application of the well-established principle of law. If the accident had occurred within 60 days prior to the Constitution of the Tribunal then the bar of limitation provided in Sub-section (3) was not an impediment. An application to the Tribunal could be said to be the only remedy. If such an application, due to one reason or the other, could not be made within 60 days then the Tribunal had the power to condone the delay under the proviso. But if the accident occurred more than 60 days before the Constitution of the Tribunal then the bar of limitation provided in Sub-section (3) of Section 110A on its face was attracted. This difficulty of limitation led most of

the High Courts to fall back upon the proviso and say that such a case will be a fit one where the Tribunal would be able to condone the delay under the proviso to Sub- section (3), and led others to say that the Tribunal will have no jurisdiction to entertain such an application and the remedy of going to the Civil Court in such a situation was not barred under Section 110F of the Act. While taking the latter view the High Court failed to notice that primarily the law engrafted in Sections 110A and 110F was a law relating to the change of forum."

(Emphasis Supplied)

- It is therefore, clear that for matters of misconduct committed prior to coming into force of Section 132 (4), NFRA can initiate an investigation. It also stated that the expression "such matters of misconduct" can be inferred to mean misconduct' which has been committed prior to 24.10.2018 i.e., the date of coming into force of Section 132 (4) and qua which proceedings already underway by the ICAI and w.e.f. 24.10.2018 the said proceeding would be in the exclusive domain of the NFRA.
- In the matter of ***Election Commission of India and Ors. vs. Subramanian Swamy and Ors.*** *[(1996) 4 SCC 104],* it was held in Hon'ble Supreme Court that :-

"16. We must have a clear conception of the doctrine. It is well settled that the law permits certain things to be done as a matter of necessity which it would otherwise not countenance on the touchstone of

judicial propriety. Stated differently, the doctrine of necessity makes it imperative for the authority to decide and considerations of judicial propriety must yield. It is often invoked in cases of bias where there is no other authority or Judge to decide the issue. If the doctrine of necessity is not allowed full play in certain unavoidable situations, it would impede the course of justice itself and the defaulting party would benefit therefrom. Take the case of a certain taxing statute which taxes certain perquisites allowed to Judges. If the validity of such a provision is challenged who but the members of the judiciary must decide it. If all the Judges are disqualified on the plea that striking down of such a legislation would benefit them, a stalemate situation may develop. In such cases the doctrine of necessity comes into play. If the choice is between allowing a biased person to act or to stifle the action altogether, the choice must fall in favour of the former as it is the only way to promote decision-making. In the present case also if the two Election Commissioners are able to reach a unanimous decision, there is no need for the Chief Election Commissioner to participate, if not the doctrine of necessity may have to be invoked."

(Emphasis Supplied)

- We will like into consideration ratio laid down by the Hon'ble Supreme Court in the matter of ***Bijender Singh vs. State of Haryana and Ors.*** *[(2005) 3 SCC 685],* wherein it was held that

> *"14. The embargo of giving a retrospective effect to a statute arises only when it takes away vested right of*

a person. By reasons of Section 20 of 2000 Act no vested right in a person has been taken away, but thereby only an additional protection had been provided to a juvenile".

(Emphasis Supplied)

- At this stage, we will attempt to deep dive into penalty aspects as contained in Chartered Accountants Act, 1949 and also as stipulated in Companies Act, 2013. This read as under **:-**

a) Chartered Accountant Act, 1949

***"[21B. Disciplinary Committee**.-(1) The Council shall constitute a Disciplinary Committee consisting of the President or the Vice-President of the Council as the Presiding Officer and two members to be elected from amongst the members of the Council and two members to be nominated by the Central Government from amongst the persons of eminence having experience in the field of law, economics, business, finance or accountancy:*

Provided that the Council may constitute more Disciplinary Committees as and when it considers necessary.

(2) The Disciplinary Committee, while considering the cases placed before it shall follow such procedure as may be specified.

(3) Where the Disciplinary Committee is of the opinion that a member is guilty of a professional or other misconduct mentioned in the Second Schedule or both the First Schedule and the Second Schedule, it shall afford to the member an opportunity of being heard

before making any order against him and may thereafter take any one or more of the following actions, namely:-

(a) reprimand the member;

(b) remove the name of the member from the Register permanently or for such period, as it thinks fit;

(c) impose such fine as it may think fit, which may extend to rupees five lakhs."

(Emphasis Supplied)

b) Companies Act, 2013

*"**132. Constitution of National Financial Reporting Authority**-*

(4) Notwithstanding anything contained in any other law for the time being in force, the National Financial Reporting Authority shall—

*(c) where professional or other misconduct is proved, have the power to make order for— (A) imposing penalty of— (I) **not less than one lakh rupees, but which may extend to five times of the fees received, in case of individuals**; and (II) not less than ten lakh rupees, but which may extend to ten times of the fees received, in case of firms;*

*(B) **debarring the member or the firm from engaging** himself or itself from practice as member of the Institute of Chartered Accountant of India referred to in clause (e) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 for **a minimum period of six months or for such higher period***

not exceeding ten years as may be decided by the National Financial Reporting Authority.

Explanation.—For the purposes of his sub-section, the expression "professional or other misconduct" shall have the same meaning assigned to it under section 22 of the Chartered Accountants Act, 1949."

(Emphasis Supplied)

- Thus, it becomes clear that under Chartered Accountants Act, 1949, the members of ICAI could be debarred for any period including for life, thereby causing lifelong punishment to erring Chartered Accountants. On the contrary, NFRA has limited scope of debarring the guilty Chartered Accountants or the firm for maximum 10 years of debarment. This clearly is lesser penal provision than as available to ICAI under Chartered Accountants Act, 1949.
- From above judgements, following clear ratios are noted for deciding on the issue of retrospectivity. These are as follows :-

(i) Change in forum due to change in law has no bar on being implemented with retrospective effect.

(ii) The litigant has vested right in action but does not have any vested right on forum.

(iii) Retrospective application in such procedural law and change in forum is barred only if express provision is made in new law.

From this, we are of prima-facie view that Section 132 (4) of the Companies Act, 2013 can be applied retrospectively.

- We also take into consideration the fact that neither any new misconduct has been created in law, which NFRA can investigate and levy penalty, if required nor NFRA can levy penalty greater than the quantum of penalty envisaged under the Chartered Accountants Act, 1949.
- Thus, plea of the Appellants about protection under Article 20 of the Constitution and cited judgments will not give any reprieve to the Appellants in present cases in view of our detailed discussing earlier.
- Thus, after taking into consideration the background for forming NFRA, the judgment of the Apex Court, proven scams, need to restore shaken confidence of public and investors at large and prevent any adverse impact on Indian economy, we hold that NFRA has clear and required retrospective jurisdiction over the alleged offences by delinquent Chartered Accountants for period prior to formation of NFRA or prior to coming into effect relevant portion of Section 132 of Companies Act, 2013.

Issue No. (III) Violation of Principle of natural justice V/s separate division of NFRA.

- Another preliminary ground of challenge by the Appellants, to the Impugned Orders of NFRA, in the Appeal Books as well as during several initial hearings, is that enquiry by NFRA was against the laid down procedures since NFRA did not constitute any division as required in Section 132(A) of the Companies Act, 2013. It is the case of the Appellant that as per Rule 2(g) of NFRA Rules, 2018, NFRA is obligated to establish divisions for the purpose of organising its

functions and duties. It has been emphasised that separate divisions are necessary for fair and independent investigations for alleged professional misconduct and other misconduct as can be inferred from Rule 10 & 11 of NFRA Rules, 2018, which prescribed separate divisions for investigations and for enforcement, similarly Rule 11(5) of NFRA Rules, 2018 talks about reasoned Order in adherence to principle of natural justice including an opportunity of being heard in person and submissions by concerned person to defend his case. It is case of the Appellants that in the present case, SCNs were signed by the "Executive Body, NFRA" comprising of Chairperson and two full time Members violating principle of natural justice. The Appellants submitted that under Section - 132(1A) "NFRA shall perform its function through divisions as may be prescribed" and since divisions have not been prescribed for NFRA by the legislative, NFRA cannot function at all, until such divisions are set up.

- However, during final hearings, on a pointed query by this Appellate Tribunal to the Appellants regarding specific amendments in the NFRA Rules, 2018 regarding constitution of division, the Learned Counsel for the Appellants conceded that this point was missed by them earlier and accepted that the Division of the NFRA has duly been constituted in Rule 2(g) of the NFRA Rules, 2018. However, the Appellants stated that the process followed by the NFRA, although legally complied but still could not be considered as in compliance with principal of natural justice in so far as there has not been a

proper separation of powers in investigation, prosecution and adjudication by the NFRA.

- On the other hand, the Respondent denied the averments of the Appellants that NFRA violated principles of natural justice on ground that no divisions were notified/ stipulated as required in the Companies Act, 2013 and NFRA Rules 2018. The Respondent submitted that as per Section 132(1A) of the Companies Act, 2013, "NFRA shall perform its functions through divisions, as may be prescribed", and the word "as may be prescribed" means if any prescribed, and since the legislature has not prescribed any divisions, at initial stages NFRA has been functioning keeping in mind the principles of natural justice. In any case, by way of an amendment dated 13.11.2018 to Clause 2(g) of NFRA Rules, 2018, it has been stipulated that divisions means division including one headed by the chairperson or fulltime member for purpose of carrying out its functions and duties. Since, at the time of issue of SCNs as well as the Impugned Orders to the Appellants, Clause 2(g) of NFRA Rules, 2018 clearly defined the division and as such as there was no illegality on the part of NFRA on this account. Moreover, the Appellants also were given opportunity for personal hearing which they denied and therefore, there have been no violation of natural justice.
- It is brought to the notice by NFRA that there has been no violation of principles of natural justice with regard to formation of separate divisions by NFRA. It is submitted that as per Section 132 (1A) pf Companies Act, 2013 NFRA is to function through such divisions as

may be prescribed and Section 2(66) of the Companies Act, 2013 defines prescribed by law as rules under such act, which are to be framed by the Central Government and not NFRA as per Section 469 of the Companies Act, 2013. It has further been argued that there is distinct difference between "existence of powers" and "manner of exercise of powers", and merely if not prescribed would not amount to denying the existence of powers of NFRA itself. It has been submitted that in absence of any specific rules, it is for NFRA to determine and adopt the procedure as deemed fit and being fair and reasonable. This is supported by the ***Ramjibhai Vs. State of Gujarat (1965) 2 SCC 5 and Chairman & MD, BPL Ltd. Vs. Gururaja & Ors.*** *[(2003) 8 SCC 567***.**

- On this issue of segregation or formation of division which allegedly violated principles of natural justice, we may take help of ratio arising out of the judgment in the matter of ***State of Karnataka Vs. Kuppuswamy Gownder & Ors.*** *[(1987) 2 SCC 74],* which held as under :-

> *"15. It is not disputed that the plea of prejudice or failure of justice is neither pleaded nor proved. Not only that even the judgment of the High Court does not indicate any possibility of prejudice or failure of justice. learned Counsel appearing for the respondent also did not suggest any possibility of prejudice or failure of justice. Under these circumstances therefore the view taken by the High Court does not appear to be correct in view of the language of Section 462 read with Section 465. The judgment of the High Court is*

therefore set aside. The direction of remand made by the High Court is also quashed. It is unfortunate that these matters pertaining to incidents of 1980 should not have been disposed of till today and that the matter should have remained pending on such technical grounds for all these years. We therefore direct that the appeals be remitted back to the High Court so that they are heard and disposed of on merits as expeditiously as possible."

(Emphasis Supplied)

- From above, it becomes clear that matters cannot be allowed to be avoided only on pure technicalities and there may not be any prejudice or failure of justice on this account alone.
- We may note the observation made by the Hon'ble Apex Court in the mater of ***Clariant International Ltd. and Ors. vs. Securities and Exchange Board of India*** *[(2004) 8 SCC 524],* which held as under :-

"69. Reasons for creating special tribunals, according to the learned author, are:
(i) Expert knowledge
(ii) Cheapness
(iii) Speed
(iv) Flexibility
(v) Informality
80. The Board exercises its legislative power by making regulations, executive power by administering the regulations framed by it and taking action against any entity violating these regulations and judicial power by adjudicating disputes in the implementation thereof. The only check upon exercise of such wide ranging power

is that it must comply with the Constitution and the Act. In that view of the matter, where an expert Tribunal has been constituted, the scrutiny at its end must be held to be of wide import. The Tribunal, another expert body, must, thus, be allowed to exercise its own jurisdiction conferred on it by the statute without any limitation."

(Emphasis Supplied)

- The Rule for division are prescribed in Section 132 of the Companies Act, 2013 and NFRA Rules 2018 (Rune No. 2(g) which have already noted earlier.
- Therefore, it is clear that prior to amendment in Rule 2(g) of NFRA Rules 2018, the "division" was not defined but Ministry of Corporate Affairs vide amendment dated 13.11.2018 on NFRA Rule, 2018 specified as to what constitute "division" under Rule 2(g). We note that the Respondent used the division as stipulated in the Companies Act, 2013 and NFRA Rules, 2018, hence there has been no violation of principles of natural justice. This fact was also fairly conceded by the Appellant also during final stage of hearing.
- Issue No. III stand settled accordingly.

Issue No. (IV) Role of Statutory Auditors of the Company V/s Statutory Auditors of the Branches of the company.

- Since the Appellants in all four Appeals, herein have worked as EPs involved in Branch Audit of 17 branches of DHFL, they emphatically

pleaded that they do not have any liability or at least they should have minimum responsibility confined only to branch.

- In view of this, it becomes necessary to examine the issue of role of Statutory Auditors V/s Auditors of Branch. This issue, itself, may have several related issues deserving consideration for clarity and for helping us to reach final logical and informed outcome. Thus, we may prefer also to deal with following related points while considering this issue, which inter-alia, includes :-

    a) Whether the Branch Auditors are independent or subservient to statutory auditors.

    b) Can Statutory Auditors conduct the audits of branch themselves.

    c) Whether different criteria and qualification are stipulated for appointment of Branch Auditors vis-a-vis that of Statutory Auditors.

    d) Aspects of application of SAs to Branch Audit.

    e) Does audit of branch audit impact quality and output of overall financial audit of the Corporate Debtor.

- Since all these are interconnected and also dependent on each other, we will deliberate in conjoint way in subsequent discussions.

Definition and scope of Statutory Audit :

- Statutory Audit is a legally required review of the accuracy of financial statement of the entity as per relevant statutes applicable to such entities. Such entities as Auditee may include public limited

Company, Private Limited Company, Limited Liability Partnerships, Banks, Insurance Company, Electricity Company, Co-operative Banks, Government Companies listed or unlisted companies, NBFC and so on. Occasionally such Auditee entities may be governed by different laws, as applicable. For instance, the companies are governed by the Companies Act, 2013, their Statutory Audit has been prescribed in Section 139 to 147, which we have already noted earlier.

- Generally speaking, Statutory Audit is conducted by independent auditors who are duly qualified and permitted by the examination and regulatory body i.e., ICAI. Statutory Audit involve detailed examination of financial and other relevant connected records of the entity to establish that financial statements of the entity depicts true and fair picture of the company.

Definition and scope of Branch Audit.

- Section 2(14) of the Companies Act, 2013 describes "Branch office" in relation to company means any establishment described as such by the Company.
- As per Section 143 (8) of Companies Act, 2013, where a company has a branch or more than one branch, the accounts of such branch shall be audited by :-

  a) the Statutory Auditor, so appointed by the shareholder of the Company, itself.

  b) Any other person, qualified to be and appointed as an Auditor as prescribed under Section 139 of Companies Act, 2013.

- However, if branch of such company is situated outside India, the accounts of such branch shall be audited, either by Auditor appointed by the company or by an auditor duly qualified to act as an Auditor of accounts of branch office in accordance with law of that country.
- As per the proviso to Section 143(8) "branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.
- At this stage, this Appellate Tribunal takes into Rule 12 (1) of Company (Audit and Auditors) Rules 2014 which is as follows:

> *"(1) For the purposes of sub-Section (8) of Section 143, the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be as contained in sub-Sections (1) to (4) of Section 143 which makes it clear that even for the audit of the branches of a company, the responsibility of auditors as provided in Section 143(1) 143(4) are on the company's auditor and not on the Branch Auditor."*
>
> *(Emphasis Supplied)*

- **Analysis :-**

  - After careful reading Section 143(8) along with Section 149 of Companies Act, 2013, (noted in earlier discussion) it appears that the process of appointment of Statutory Audit and Auditor for the branch audit remains the same. In other words,

whatever process is followed for appointment of Statutory Auditors shall also be applicable regarding appointment of Branch Auditors.

- On the other hand, Statutory Auditor is required to deal with the Branch Audit Reports received from the Branch Auditor, if appointed other than the Statutory Auditor himself, in preparing an overall Auditor Report of the company. No prescribed manners or procedure for the same has apparently been laid down and it is left to Statutory Auditors to take care of such Branch Audit Reports suitably.
- Therefore, complete freedom has been given to Statutory Auditor to decide the reliance and the impact of Branch Audit Report on the overall audit of company accounts. While doing so, he may incorporate the observations regarding outcome of Branch Audit as deemed fit to give true and fair picture about financial statements of the company, keeping in view, the concept of materiality along with accounting and auditing principles and standards as applicable, in given context.
- However, in case Branch Audit Report contains qualifications on matters which are required to be disclosed in company account, the Statutory Auditor is duty bound to incorporate such observations in its comprehensive Audit Report of the company.
- As regard the relationship between the Statutory Auditor and the Branch Auditor we may infer that both are responsible for

their respective area, however, the Branch Auditor will squarely remain responsible in respect of branch audit conducted by him.

- We observe that SA 230 describes Auditor's responsibility where the audit to be conducted is of "Financial Statements" of the company and Financial Statements, as per Section 2(40) of the Companies Act, 2013 are the Balance Sheet, Profit and Loss Account, Cash Flow Statement and Statement of Changes in Equity along with Notes on Accounts, whereas the scope of Branch Audit is limited to audit of the Company's branches.
- The Appellants pointed out that Scope of auditing of the Financial Statements of the Company as a whole was upon the DHFL Statutory Auditor i.e., CAS only. Per contra, the Respondent empathetically denied and refuted the arguments of the Appellants that the branch audit was limited to expressing opinion on the accounting of the branches in question, as reflected through Trial Balance should not be accepted since in the "Independent Branch Auditors' Report". The Respondent stated for instance, the Appellant opined on the "true and fair view of the branch". In the annexure titled "Branch Auditor Audit of Branch's Financial Information Summary Memorandum As A Whole", the appellant certified that "We have audited, for purposes of your audit of the financial statements of Dewan Housing Finance Corporation Limited, the financial information as of 31st March, 2018 and for the year then ended. In our opinion, based on our audit, the financial information for Coimbatore as of 31st March, 2018 and for

the year ended gives a true and fair view in conformity with the applicable financial reporting framework in India and the group accounting policies". Thus, the Appellants certified that the financial information of the branches of DHFL as on 31st March, 2018 were true and fair for different branches in similar manner.

- In terms of para 2 of SA 200, the principles and procedures laid down in the SAs including professional skepticism, audit documentation, sufficiency and appropriateness of audit evidence, audit planning, materiality, engagement risk, nature, timing and extent of evidence-gathering procedures and reporting are all applicable in the branch audit as well, being an audit of historical financial information. Branch auditors appointed under section 143(8) read with Section 139 of the Companies Act, 2013 are statutorily required to comply with the SAs since section 143(9) requires "every auditor" to comply with the SAs. We have already noted from the averments of the Respondent that the Appellants themselves admitted that "Overall audit strategy and development of an audit plan depends on the nature and scope of every audit assignment and risk of material misstatement, perceived by the auditor". This is not in sync with appellant's contention that he "had a properly documented audit plan available in the audit file for previous years. Therefore, documentation displaying an overall audit strategy and development of an audit plan for FY 2017-18 was felt not necessary, in view of the fact that it was not an audit of financial statements". The Appellant as EPs failed to assess the need to update the existing Overall audit strategy and audit

plan in light of changed risk environment as SA 300 requires the auditor to include in the audit plan, the timing of the audit and to update and change the overall audit strategy and the audit plan as necessary during the course of the audit.

- We note the content of SA 300 as under :-

> ***"SA 300 PARA 7 and 9***
>
> *7. In establishing the overall audit strategy, the auditor shall: (a) Identify the characteristics of the engagement that define its scope; (b) Ascertain the reporting objectives of the engagement to plan the timing of the audit and the nature of the communications required; (c) Consider the factors that, in the auditor's professional judgment, are significant in directing the engagement team's efforts; (d) Consider the results of preliminary engagement activities and, where applicable, whether knowledge gained on other engagements performed by the engagement partner for the entity is relevant; and (e) Ascertain the nature, timing and extent of resources necessary to perform the engagement. (Ref: Para. A9-A12)*
>
> *9. The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit."*
>
> *(Emphasis Supplied)*

- As per Section 143(8) of the Companies Act, 2013 "Where a company has a branch office, the accounts of that office shall be audited by either by the auditors appointed by the company or by any other person qualified for appointment as an auditor of the company under

this Act and appointed as such under section 139.....", which makes it obvious that the appointment of a Auditors of the branch is required to be made under Section 139 of the Act i.e., by the members at an annual general meeting. The general meeting may authorise the Board of Directors to make the appointment in consultation with company's auditor.

- The acceptance letter dated 12.09.2017 issued by the Audit Firm and the "Independent Branch Auditor's Report" issued by the Appellants for the 17 branches of DHFL, including the report required under CARO 2006 described the engagement as Branch Statutory Audit.
- Section 22 read with Clause 9 of Schedule I of the Chartered Accountants Act, 1949, required appellant to ensure that provisions of Section 143(8) read with Section 139 of the Companies Act, 2013 are complied with, which was not done by the Appellant, hence the Appellants were rightly held guilty of professional misconduct on this account.
- To sum up on various sub issues as discussed in preceding paragraphs we observe the following:-
    - Branch Auditor has specific role to perform with reference to Audit of the Branch and to that extent he may be treated as sub-servient to Statutory Auditor since he submits the Branch Auditors Report to the Statutory Auditor who incorporates suitably in its comprehensive audit report of the company.
    - As regards issue framed regarding as to who has to audit branches, if the Statutory Auditor can perform duties of Branch

Auditor himself, the answer is clear and positive that the Statutory Auditor can conduct the auditor of all branches or some of the branches himself else other qualified to be auditors and so appointed can conduct Branch Audit.

- As regards qualification required for appointment of Statutory Auditor and/ or Branch Auditors, we observe that the qualification remains exactly the same for appointment of Statutory Auditor as well as Branch Auditors. In continuation, it may also be observing that the Statutory Auditor is appointed by the members of the company i.e., the shareholders who in turn may appoint branch auditors also if required or the Branch Audit can be entrusted to the Statutory Auditors.
- As regard, application of SAs to Branch Audit, we are of clear opinion that all SAs stand applicable to the branch audit, as required for the work of the branch audit.
- As regard, the impact of the quality of branch audit on the overall audit of the company, it is quite obvious and natural that the quality of Branch Audit will definitely impact the overall audit. In few situation, it may happen depending upon the nature of business that main activities of work except for the centralised functions, may lies only in the branches and the importance of such branches becomes very significant.
- Incidentally, in the present four appeals where M/s K. Varghese and company (firm) was appointed to conduct the audit 17

branches for of total 33 branches of DHFL, which can be considered very significant looking to the nature of the work of DFHL.

- We note from the Impugned Order dated 13.04.2023 of NFRA in case of CA Harish Kumar T.K. where it has been recorded that appointment of none of 33 branch auditors was approved at the AGM of DHFL as stipulated in the Companies Act, 2013.
- To sum up the role of branch auditor, though limited primarily to the branch, however, is critical for overall audit of the company and the Auditors of the Branch cannot absolve his responsibilities. We cannot overlook the fact that the allegations of fraud involving Rs. 31,000 Crores by the DHFL including banking fraud of about 3,700 Crores by Directors of DHFL happened and the Auditors clearly failed in their duties.

Issue No. (V) Are Standards of Auditing (SA) mandatory or Advisory or to be treated as guidance notes to Auditors.

- According to Section 143 (9) of the Companies Act, 2013 every auditor "**shall"** comply with auditing standard. Section 143 (10) of Companies Act, 2013 further empowers Central Government to prescribe the Standards of Auditing (SAs) as recommended by ICAI in consultation and after examination of the recommendation made by NFRA. As per the proviso to Section 143 (10) until any auditing standard are notified, any standard or standards of auditing specified by ICAI shall be deemed to be auditing standard.

- It is further noted that the Accounting Standards and Auditing Standards have been defined in the Companies Act, 2013 and both sets of standards are to be mandatorily followed by all stakeholders including the companies and the Chartered Accountants. Thus, we are of the clear opinion that the Appellants as Auditors were duty bound to follow these standards which they alleged to have been breached in respect of SA 210, SA 230, SA 315, SA 320, SA 330, SA 700 along with few other paragraphs of other SAs and Section 143(8) of the Companies Act, 2013.
- In view of the legal position the SAs are mandatory and not as advisory or a guidance note to auditors.

Issue No. (VI) **What is professional misconduct for member of ICAI and legal provisions.**

- NFRA has been empowered to investigate either suo-moto or on a reference made to it by Central Government to investigate into the matters of professional or other misconduct committee by any member or firm of CA's registered under the Chartered Accountants Act, 1949.
- Proviso to this sub Section 132(4) provide that no other institute or body shall initiate or continue any proceeding in such matters of misconduct where NFRA has initiated an investigation under this Section.
- The explanation under Section 132(4) of Companies Act, 2013 have already been gone into earlier.

- From this it is clear that professional or other misconduct will have to derive the meaning and further details from Section 22 of Chartered Accountants Act, 1949.
- Section 22 of Chartered Accountants Act, 1949 reads as under:-

> *"**22. Professional or other misconduct defined***
> *For the purposes of this Act, the expression "professional or other mis conduct" shall be deemed to include any act or omission provided in any of the Schedules, but nothing in this Section shall be construed to limit or abridge in any way the power conferred or duty cast on the Director (Discipline) under sub-section (1) of Section 21 to inquire into the conduct of any member of the Institute under any other circumstances."*
>
> *(Emphasis Supplied)*

- As per Section 22 of the Chartered Accountants Act, 1949 "professional or other misconduct" shall include any act or profession omission as in any of the schedule but nothing in this Section shall be construed to limit in any way powers conferred to enquire into conduct of any Member of ICAI under any circumstances.
- Since the schedules of Chartered Accountants Act, 1949 mentioned in Section 22 which becomes basis for particular professional or any other misconduct. We will refer to I Schedule- Part 1, Part 2, Part 3 & Part 4 **:-**

(A) Schedule-I consist of Part 1, Part 2, Part 3 & Part 4 –

Part I of Schedule I describes "Professional misconduct" in relation to Chartered Accountants in practice and list out of twelve items, violation of which shall deemed to be professional misconduct.

Part 2 of Schedule I pertain to "Professional misconduct in relation to Members of the institute in service and mention two items.

Part 3 of Schedule I talks about Professional misconduct in relation to Members of the institute generally and describe three professional misconducts.

Part 4 of Schedule I relate to other misconduct in relation to members of the institute generally and describes two professional misconduct.

Thus, there are total 19 deemed misconduct under Schedule I.

(B) Schedule II Part 1 relates to Professional misconduct in relation to Chartered Accountants in practice, where Chartered Accountants is deemed to be guilty of professional misconduct in 10 types of deemed professional misconduct.

Part 2 of Schedule II relates to Professional misconduct in relation to Members of institute generally and describe four types of misconduct, whereas Part 3 of Schedule II describes other misconduct in relation to Members of institute generally.

- Chapter V of Chartered Accountants Act, 1949 on misconduct consist of two sections, namely, Section 21 and Section 22. Section 21 describes disciplinary directorate and empowers the Council of ICAI and to establish disciplinary directorate headed by Director (Discipline). According Section 21(3), where the Director Discipline is

of opinion that Member is guilty of any professional or other misconduct mentioned in Schedule I , he is duty bound to place the matter before the "Board of Discipline" and where Director Discipline is of opinion that member is guilty of professional or other misconduct mentioned in II Schedule or both Schedules, Director Disciplinary is required to place matter before the "Disciplinary Committee".

- Board of Discipline in terms of Section 21 A of the Chartered Accountants Act, 1949 have been given the following three powers:-
  a) Reprimand the member;
  b) Remove the name of the member from the Register up to a period of three months,
  c) Impose such fine as it may think fit, which may extend to rupees one lakh.
- The Disciplinary Committee of ICAI which is headed by President or Vice President of Council as presiding officer, generally deals in serious offence as stipulated in Schedule II or both schedules. The Disciplinary Committee has been empowered to take following action after following due process :-
  a) Reprimand the member;
  b) Remove the name of the member from the Register permanently or for such period, as it thinks fit;
  c) Impose such fine as it may think fit, which may extend to rupees five lakhs.
- It will be worthwhile to note that the Chartered Accountants Act, 1949 was amended in 2006 to change the procedure for determining

whether an auditor is guilty of misconduct. Prior to 2006 amendment, disciplinary proceedings were governed by the Council of ICAI who had power to refer the matter to Disciplinary Committee and if the Council was of opinion that a prima-facie case of misconduct has been made out against Chartered Accountants, however if council felt that but if the case was not made out it had power to dismiss the complaint. However, if the Report of the Disciplinary Committee proved the professional misconduct of the Member it could remove the name of the Chartered Accountants from its register of Members for a period of not exceeding five years in terms of the then Section 21(4) of Chartered Accountants Act, 1949. For serious offence following in Schedule II based on the Report of Disciplinary Committee, it was obligatory on the part of the Council to refer such cases to the High Court in terms of the then Section 21(5) of Chartered Accountants Act, 1949.

- After 2006 amendment to Chartered Accountants Act, 1949, High Court is no longer in picture regarding disciplinary proceeding relating to Chartered Accountants. The practice continued till NFRA came into existence in 2018 as already discussed in details earlier and now NFRA derives the power to investigate the matters in terms of Section 132 of the Companies Act, 2013.
- It will be worthwhile to note that unlike differentiation based on Schedule I and Schedule II with reference to Section 21 and 22 of the Chartered Accountants Act, 1949, for NFRA there is no such distinction and can look into matters which are covered under Section

22 which automatically refer to all Schedules of Chartered Accountants Act, 1949, meaning Schedule I and Schedule II on comprehensive basis. Thus, the powers of NFRA are more and wider than available to ICAI, as discussed in preceding paragraphs.

- On a gross and broader basis, it can be inferred that the misconduct as referred in Schedule I are of lesser gravity and more related in pattern of practice or remunerations or soliciting work or engaging in the provision or occupation prescribed by the Counsel etc.
- On the other hand, the Schedule II of Chartered Accountants Act, 1949 are of more serious nature relating to disclosing confidential information, misconduct regarding examination of financial statement failure to disclose material facts which have could impact on true and fair picture of financial statement, failure to report material mis-statements, non-exercised due diligence or grossly negligence in conduct of professional duties or failure to obtain information or material departure from generally expected audit procedure as applicable in the circumstances and forum.
- Thus, it is observed that the professional misconduct continues to be defined under Section 22 of the Chartered Accountants Act, 1949 r/w Schedule I and Schedule II of Chartered Accountants Act, 1949.
- We will like to refer to the judgment of the Hon'ble Supreme Court in the matter of ***Council of Institute of Chartered Accountants of India Vs. Y.K. Gupta, F.C.A,*** *[2010) SCC OnLine Del 4192].* The relevant portion clarifying the powers of ICAI, now in turn of NFRA reads as under :-

"16. The Code of Conduct issued by the Institute of Chartered Accountants of India records that it is necessary for the Institute "to guide and compel the members to live up to these high standards. The prestige and confidence enjoyed by a profession, to a great extent, is dependent on strictness and scrupulosity with which such a Code is interpreted and not necessarily by legislation or regulations as much by self-discipline". It is also stated that the Council in addition to "professional misconduct" as defined in Section 22 of the Act has been given power to inquire into the conduct of any member of the institution under circumstances other than those specified in the Schedules to the Act. The Council is not debarred from inquiring into the conduct of any member of the institute under any other circumstances, as asserted in the Code. This aspect is fully borne out by the expression "professional or other misconduct" occurring in Section 21. The power of the Council to inquire into "other misconduct" which is not mentioned in the Schedules is placed beyond any pale of controversy by the decision of the Supreme Court in Institute of Chartered Accountants v. B. Mukharajea (supra) in which the Supreme Court has, in terms, held that, if a member of the Institute is found, prima facie, guilty of conduct which, in the opinion of the Council, renders him unfit to be a member of the Institute, even though such conduct may not attract any of the provisions of the schedule, it would still be open to the Council to hold an inquiry against the member in respect of such conduct and a finding against him in such an inquiry

would justify appropriate action being taken by the High Court. It was held that though the definition of the material expression used in Section 21(1) refers to the acts and omissions specified in the schedule, the list of the said acts and omissions is not exhaustive; and in any event, the said list does not purport to limit the powers of the Council under Section 21(1), which may otherwise flow from the words used in the said sub-section itself. It was held that it would not be right to hold that such disciplinary jurisdiction can be invoked only in respect of conduct falling specifically and expressly within the inclusive definition given by Section 15. Members of the Institute are bound to act in a manner consistent with the good reputation of the profession. They should refrain from any conduct which might bring discredit to the institute. Members should be guided not merely by the terms, but also by the spirit of the Code of Conduct and the fact that particular conduct does not receive mention does not prevent it from being unacceptable or discreditable conduct, thus making a member liable to disciplinary action. After all, Code of Ethics draws community ethics and moral principles into the professional institutions. There is a need to arrive at a balance between the interests of the member as a citizen in expressing views in the matters of public concern and the interest of the institution in preserving the status and dignity of the professionals rendering service as Chartered Accountants."

(Emphasis Supplied)

- It is therefore clear that there is no bar on ICAI or NFRA to restrict investigation of professional misconduct covered only under Section 22 of the Chartered Accountants Act, 1949. The powers are far more and wider and any conduct which makes auditor of unbecoming of such profession will make him liable for suitable investigation and if found guilty may face punishment as per law.
- NFRA derives the power regarding disciplinary action on professional or other misconduct of the members of ICAI under Section 132 (4) (c) of the Companies Act, 2013.
- NFRA has far more powers and authority for professional misconduct of members of ICAI in comparison to powers and authority of ICAI itself.

Issue No. (VII) True intent of Standard of Audits and other related standards relevant for audit and issue regarding alleged violation by the Appellants herein.

(A) Legal status and details of Standards of Auditing and other related Standards in India :

- Before 2014, Standards of Auditing (SA) were relevant to the extent as these prescribed the methodology of conducting an audit and were issued by the Central Government pursuant to Section 133 of the Companies Act. However, a deviation from these standards did not automatically amount to gross negligence or professional misconduct. This position did change after 2014, when auditing standards were given a statutory status. The Section 143 (g) of the Companies Act,

2013 requires auditors to comply with auditing standards. SAs now have the force of law which tantamount that the existence or lack of intention is immaterial when it comes to making a finding of professional misconduct and gross negligence.

- A lapse in following the SAs, may result in professional misconduct, violation of a statutory duty, and gross negligence. Section 143(9)-(10) of the Companies Act 2013 gives a clear mandate to NFRA to ensure adherence of auditing standards by all stakeholders. The expectation is that auditors will exercise the professional scepticism and thoroughly verify statements made by the management of a company as explanations for their balance sheet. Auditors are thus required to strictly comply with SAs, violation of which may result into punishment and penalty.
- The significance of the SAs becomes critical for maintenance of investor confidence, as audited financial statements are necessary inputs for any decision, investors make. Auditors are thus entrusted with duty to calibrate their approach based on what they judge to be the significance of the audit operation.
- SAs are issued based on International Standards on Auditing (ISAs) issued by International Federations of Accountants (IFAC).
- These Standards in India are issued under the authority of the council of the ICAI. Section 143 (2) of the Companies Act 2013 requires the auditor to ensure compliance with these SAs.
- We note that the standards on auditing have been divided into 6 groups having 38 standards as detailed below.

- 100-199: Introductory Matters (Nil Standard)
- 200-299: General Principles & Responsibilities (9 Standards)
- 300-499: Risk Assessment and Response to Assessed Risks (6 Standards)
- 500-599: Audit Evidence (11 Standards)
- 600-699: Using Work of Others (3 Standards)
- 700-799: Audit Conclusions & Reporting (6 Standards)
- 800-899: Specialised Areas (3 Standards)

➢ There are two Standards on Review Engagements (SRES) are applied in the review of historical financial information.

➢ There are three Standards on Assurance Engagements (SAES) which are applied in assurance engagements, other than audits and reviews of historical financial information.

➢ There are two Standards on Related Services (SRSS) which are applied to engagements involving application of agreed-upon procedures to information, compilation engagements, and other related services engagements, as may be specified by the ICAI.

➢ Standards on Quality Control (SQC) are for ensuring quality by firms that performs audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements. SQC requires that the firm should establish a system of quality control designed to provide it with reasonable assurance that the firm and its personnel comply with professional standards, regulatory, legal requirements, and that reports issued by the firm or engagement

partner(s) are appropriate in the circumstances. SQC is for enhancing the quality of audit.

B. <u>Key aspects of the Standard on Auditing</u> :

- We have noted from resources of ICAI about some of the important principles of the SAs which are elaborated below. The understanding of these principles is significant as they are directly and indirectly redated to alleged violating of SAs by the Appellants in present four appeals before us. These principles as noted are :-

(i) <u>Risk Based Auditing</u>

The standards of auditing issued by the ICAI require the auditor to perform a 'Risk Based Audit, where the auditor seeks to obtain reasonable assurance that no material misstatements whether caused by fraud or errors exist in the financial statements.

(ii) <u>Skepticism :</u>

SA 200 "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing" defines Professional Skepticism as "An attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence".

In addition to SA 200, at least 10 other standards such as SA 240, SA 300, etc. emphasize on the need for maintaining professional skepticism while conducting the audit.

(iii) <u>Professional Judgement :</u>

An audit requires the auditor to perform procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. The auditor applies professional judgement in deciding which procedures are to be performed. This requires the auditor to rely on their knowledge, training and experience and professional skepticism.

(iv) Materiality :

The standards on auditing refer to the concept of materiality. Information is considered material if its omission or misstatement has the potential to influence the decisions of users taken on the basis of the financial statements. Materiality is relative to the size and prevailing circumstances of companies. Determining materiality involves the exercise of professional judgment by the auditor.

(v) Audit Evidence :

Standards on auditing in the series 500-599 provide for obtaining sufficient and appropriate audit evidence. This includes external confirmations, sampling, specific areas such observation of physical verification of inventories, accounting estimates, related parties among others.

(vi) Documentation :

Audit Documentation is the record of audit procedures performed (including audit planning), relevant audit evidence obtained, and conclusions the auditor reached. Terms such as 'working papers' or 'workpapers' are sometimes used for audit documentation.

While SA 230 "Audit Documentation" provides detailed and general guidance on the audit documentation, most standards on auditing require specific documentation to be done by the auditor. Given the increased scrutiny by various regulators, it is important for the auditor to have robust documentation of the work done. The cardinal principle is "Work not Documented is Work not Done"!

C. <u>Analysis of Issue of Violation of various SAs by the Appellants :-</u>

- Having noted the legal basis of SA and other details, time has come to look into specific allegations of such violations by the Appellants.
- From the Impugned Orders passed by the Respondent, we note that NFRA held Appellants primarily responsible for Violations of SA 210, SA 230 and SA 700. For instance, in Company Appeal (AT) No. 68 of 2023 in the matter of ***Mr. Harish Kumar T.K Vs. National Financial Reporting Authority*** in Impugned Order dated 13.04.2023 Part II of Impugned Order discussed under caption "Failure to comply with Standard of Auditing (SAs)". Para 19 to 23 of the said Impugned Order discuss violating of SA 210, Para 24 to 31 discuss Violation of SA 230 and Para 32 to Para 37 discuss Violating of SA 700.
- Violation of other SAs have been discussed in the said Impugned Order under caption "Non-Compliance of Other SA's" in Para 38. The Appellants also replied in similar manner.
- As such, we will examine and discuss alleged violation of SAs in details in coming discussions.
- NFRA has charged the Auditors for violation of following SAs:

i. SA 200 (Absence of Professional Skepticism)

ii. SA 210 (Non issuance of Engagement Letter)

iii. SA 230 (Absence of Audit Documentation giving nature, timing and extent of audit procedures performed and the conclusions reached)

iv. SA 300 (Absence of an Audit Plan and Audit Strategy)

v. SA 320 (Non determination of Planning and Performance Materiality)

vi. SA 315 and SA 330 (Non performance of Risk Assessment Procedures)

vii. SA 450 (Absence of documentation of misstatements)

viii. SA 500 (Non evaluation of reliability of info produced by the company)

ix. SA 520 (Absence of Analytical audit procedures)

x. SA 530 (Non determination of sample size and sample design)

xi. SA 700 (For forming a baseless audit opinion by not complying with the SAs)

Violation of SA- 200 & 210 :-

- **SA 200** is about Professional Skepticism and **SA 210** relates to agreeing to terms of arguments.
- The Appellants submitted that as regards alleged violation of SA 210, it is wrong to state that the Appellants failed to comply with the requirements of SA 210 "Agreeing the Terms of Audit Engagements". It is the case of the Appellants that there was no negligence in

complying with the provisions. The Appellants emphasised that SA 210 deals with recurring audits and in such audits, the auditor is required to assess whether there are circumstances that require the terms of the audit engagement to be revised and whether there is need to remind the entity of the existing terms of the audit engagement based on following factors:

i. Any indication that the entity misunderstands the objective and scope of the audit.

ii. Any revised or special terms of the audit engagement.

iii. A recent change of senior management.

iv. A significant change in ownership.

v. A significant change in nature or size of the entity's business.

vi. A change in legal or regulatory requirements.

vii. A change in the financial reporting framework adopted in the preparation of the financial statements.

viii. A change in other reporting requirements.

- It the case of the Appellants that the such engagement letters are to be sent by newly appointed auditor, which convey acceptance of the audit assignment and to spell out the auditor's understanding about the scope and limitations of the audit. The Appellants submitted that their letters consisted of the acceptance letter issued by the audit firm as also the copies of appointment letter duly signed, and acknowledged to the Annexures attached to the appointment letters contained the scope of the Branch Audit. And therefore, Firm's Letter

dated 12.09.2017 had fulfilled the auditor responsibility in agreeing the terms of the audit engagement with management as laid down.

- The Appellants emphasized that the Firm was appointed in F.Y. 2014-15 as Branch Auditors of the DHFL at the 30th AGM Notice and the minutes of the said 30th AGM show that the resolution authorizing the Board of Directors to appoint branch auditors as recommended by the Audit Committee and therefore, their appointments were in accordance with Section 139 of the Companies Act, 2013 for a period of 5 years, unless it was properly cut short by the procedure followed under Section 140. The Appellants stated that since they did not receive any notice for removal, the Firm proceeded on the basis that its appointment as Branch Auditors as validly continuing. The Appellants submitted that the new Statutory Auditors were kept copied on all communication which makes it clear that understanding of all parties at that stage was that the Branch Auditors would continue as done for the previous years.
- The Appellants submitted that all required documents were furnished to NFRA indicating that they complied SA 210 including Audit Plan, Engagement Quality Assurance Review in respect of Audit engagement, Acceptance Letter dated 12.09.2017 with acknowledgment of appointment letter, etc., and thus, there was no violation by the Appellants of SA 200 & SA 210. The Appellants also submitted that they were mainly Branch Auditors & their role was specific and confined. The Appellants were not involved in expressing

their opinion on true and fair picture on the financial statements of DHFL.

- Per contra, it is the case of the Respondent/ NFRA that the principles and procedures laid down in these relevant SAs including professional skepticism, audit documentation, sufficiency and appropriateness of audit evidence, audit planning, materiality, engagement risk, nature, timing and extent of evidence-gathering procedures and reporting are all applicable in the branch auditors as well, being an audit of historical financial information. Branch auditors appointed under section 143(8) read with Section 139 of the Companies Act, 2013 are statutorily required to comply with the SAs since section 143(9) requires "every auditor" to comply with the SAs. Thus, even if the opinion was not expressed on the true and fair view of financial statements of the Company, opinion was expressed on the true and fair view of the branches based on the financial information related thereto and the Appellants were required to comply with the SA.
- The Respondent also denied the averments of the Appellants that the appointment and qualification process are different for statutory auditors and branch auditors and therefore, the Appellants, being Auditors of such branches, were not required to follow the appointment procedure. The Respondent stated that the, w.r.t Appointment of branch auditors the Companies Act, 1956, specifically provided that the decision as to whether the books of account of a branch should be audited by the company's auditor or by any other auditor has to be taken by the shareholders in a general meeting. It is

the case of the Respondent that the Appellants failed to adhere to basic requirement before acceptance of appointment of auditors and therefore are guilty of professional misconduct.

- The Respondent stated that the contention of the appellant that the Firm consented to similar appointment letters from DHFL as received from 2015-16 to 2018-19 pursuant to the resolution at the 30th AGM authorizing Board of Directors of the Company to appoint branch auditor(s) of the Company, cannot be accepted. The Respondent submitted that as detailed in the Impugned Orders that between 2015-16 and 2016-17, there were significant changes in circumstances relating to the branch audit. In 2015-16, the AGM decided to have separate branch auditors and company's auditors, while in subsequent years the AGM appointed single Statutory Auditors (CAS) to audit the Company and all its branches. This calls for the application of para 13 of SA 210. The Respondent also castigated the Appellants contention that mere change in the Statutory Auditors of DHFL would not invite application of para 13 of SA 210 is not valid since the change in Statutory Auditor of the Company was pivotal as the Appellant's Independent Branch Auditor's report was to be issued to the Statutory Auditor of the Company and by virtue of this event, the resolution passed at the 30th AGM authorizing Board of Directors of the Company to appoint Branch Auditor(s) was rendered ineffective. The Respondent alleged that the EP's negligence of the provisions of SA 210 resulted not only in accepting an illegal appointment and non-compliance with SA 210 but

also in the absence of professional skepticism and professional judgment in understanding the objective and scope of the audit, thereby violating SA 200 itself.

- It is the case of the Respondents that in Para 13 of SA 210, it clearly states that "on recurring audits, the auditor shall assess whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms of the audit engagement." The Respondent stated that the requirement to issue an engagement letter is not limited to initial appointment only as perceived by the Appellants and therefore, communication sent by the Firm on 12.09.2017 does not fulfil the auditor responsibility in terms of SA 210 as the communication was deficient in terms of a proper description of the objective of the audit, the responsibilities of the auditors and the management and the applicable financial reporting framework.
- During averments, we came to note that there were no documentation in the audit files or in the Supplementary Audit Files to support the Appellants claim that assessment of Internal Control System was actually performed for the subject matter audit. Further, mandatory documentation requirements in the present case did not contain any of these details.
- After noting the provisions of SAs and listening to the averments made before us, the facts emerges that SA 210 requires the Auditors to inter-alia, clearly understand the scope of the audit and comply the legal requirements. It is undisputed fact that there was a change of

Statutory Auditors (CAS) who were given task of all audit including of branches. In such case, the Appellant should have ensured the compliance of SA 210. It is also observed that change in Statutory Auditors in certainly circumstances which requires the Auditors (herein the Appellants as Branch Auditor/ EPs) to reassess and revisit terms of Agreement and comply with stipulating of related SAs especially SA 210. The Appellants statement that their role was limited to Branch Audit, will not provide any immunity from non-compliance of SA 210. Hence, we do not find any error in the assessment of NFRA on this ground.

Violation of SA 230

- **SA 230** requires the auditor to assemble all the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. This SA deals with the auditor's responsibility to prepare audit documentation for an audit of financial statements. It is to be adapted as necessary in the circumstances when applied to audits of other historical financial information. The specific documentation requirements of other SAs do not limit the application of this SA.
- On issue of violating SA 230, the Appellants refuted allegation regarding their failure to comply with the requirements of SA 230 dealing with "Audit Documentation" or any deficiency in terms of the nature, timing and extent of audit procedures performed. It has been stated that the Appellants have maintained adequate documents of

Audit Plan, Engagement Quality Assurance Review in relation to audit engagement, planning meeting with engagement team, independence checklist with declaration by all the EPs and article assistants, declaration by the audit partner in respect of audit engagement, summary of accounting policies and observations from previous audits, brief indicative scope of work and guidelines for statutory audit.

- It is submitted by the Appellants that as Branch Auditors verification of trial balance items were done with due diligence as seen from the Loan Verification Certificates, Detailed Loan Verification Sheets, including KYC and Money Laundering properly signed with name of personnel preparing the sheets, Verification of Employee Reimbursement Expenses, Bank Reconciliation Statements, verification of TDS, Service Tax compliances. It has also been stated that the EPs completed task of cross-verification of closing balances of cash deposited in bank accounts diligently and similarly conducted fixed asset verification properly.
- It is case of the Appellants that NFRA has taken stand that the "significant change" necessitated the Appellants for revisiting the audit engagement terms including the Appellants preparing Audit documentation afresh due to the fact of appointment of CAS as new statutory and Branch Auditors in F.Y. 2016-17. The Appellants submitted that nowhere in SA 230, it is mentioned that change of statutory auditor of the Company is a significant change that requires a branch auditor to revisit the terms of their audit engagements.

- It has been clarified that SA 230 describes Auditor's responsibility where the audit to be conducted is of "Financial Statements" and Financial Statements, as per Section 2(40) of the Companies Act, 2013 are the Balance Sheet, Profit and Loss Account, Cash Flow Statement and Statement of Changes in Equity along with Notes on Accounts, whereas the scope of Branch Audit only is limited audit of the Company's branches, and the EPs were not required to undertake auditing of the Company's Financial Statements. The Appellants pointed out that Scope of auditing of the Financial Statements of the Company as a whole was upon the DHFL Statutory Auditor CAS only.
- The Appellant admitted that although a Branch Auditor is accountable for the part of audit conducted by him, the Company's Statutory Auditor is required to use the works done by a branch auditor in accordance with the law and since the EP was only auditing "historical financial information" other than the Company's Financial Statements, therefore, the Appellant made appropriate adaptation as reasonable in the circumstances, to the requirements of maintenance of audit documentation, with reference to the provisions in SA 230.
- It is also the case of the Appellants that they presumed that the requirements for Audit Documentation file for the purpose of SA 230, was less strict in their case and therefore basic information collected by the audit firm at the time of initial audit of the branches of company in earlier years, which was part of audit documentation in that year were not documented again in the audit files of subsequent years including FY 2017-18, as a measure of necessary "adaptation in

the circumstances". The Appellants submitted that the information that was gathered in the first year and documented were sufficient and very much relevant for the audit of FY 17-18 also, from the point of compliance of the provisions of SA 300, 315, 320 and 330. The Appellants emphasised that they did not violate relevant SAs.

- Per Contra, the Respondent refuted the response of the Appellants on SA 230 stating that the audit files initially furnished by the Appellants to NFRA included only the basic audit documentations and that the Appellants had not submitted the complete audit documentations, part of which was kept in separate supplementary file, as according to the Appellants there were no allegations of any wrong-doing against the Appellants at the time of seeking Audit Files and other documents. The Respondent empathetically stated that such claims of the Appellants should not be accepted in view of the "Duly Notarised Affidavits issued by the Appellants certifying that "The Audit File(s) submitted by me/my Audit Firm to NFRA is complete in all respects as stipulated in the Standards on Auditing (SA) and no information as required by the SAs is omitted from such files". The Respondent further supplemented the arguments that the fundamental stipulation of SA 230 is that the auditor shall assemble the audit documentations in one audit file (and not multiple audit files of different years). Hence, it is the case of the Respondent that the Appellants clearly violated SA 230 making them responsible for professional misconduct.
- The Respondent strongly objected to the contentions of the Appellants that low amount of fees is an indicator of lower professional risk

associated with the audit. The Respondent stated that this reflect poor understanding of the Appellants. Moreover, the audit plan submitted by the Appellants to the NFRA were not forming part of the Audit File for 2017-18. Such contentions of the Appellants are against the fundamentals of SA 230 that require the maintenance of Audit Files that can enable experienced auditors having no connection with the audit to understand the nature, timing and extent of the audit procedures performed to comply with the SAs.

- The Respondent submitted that the Appellant's audit documentation, including the "Supplementary Audit File" are deficient in terms of the nature, timing and extent of the audit procedures performed, who prepared and reviewed the audit working papers and the timing of the audit procedures. The Respondent argued that as per Para A5 of SA 230 that "Oral explanations by the auditor, on their own, do not represent adequate support for the work auditor performed or conclusions the auditor reached, but may be used to explain or clarify information contained in the audit documentation", therefore, the contentions of the Appellants should not be accepted in the absence of written audit documentation. Further, appellant's contention that "Since the Appellant was not required to audit the financial statements of the branch office of the Company, there was no straight jacket application of the provisions of SA 230" is untrue.
- After going through averments of both side, we feel that the Appellants contention that Branch accounts were incapable of presenting meaningful financial statements on their own may not be completely

true in view of Appellant themselves stating that Books of accounts of the branches primarily reflected financial effect of revenue and expenses items attributed to the branch. It is also undisputed fact that the fixed assets or other minor assets / liabilities related to the branch also appeared in the branch accounts. In the annexure titled "Branch Auditor Audit of Branch's Financial Information Summary Memorandum - As A Whole", the Appellants certified that "We have audited, for the purposes of audit of financial statements of Dewan Housing Finance Corporation Limited,...the financial information as of 31st March, 2018 and for the year then ended. In our opinion, based on our audit, the financial information. as of 31st March, 2018 and for the year ended gives a true and fair view in conformity with the applicable financial reporting framework in India and the group accounting policies". Thus, in effect, the Appellants certified that the financial information of DHFL as true and fair, therefore, at this stage the Appellants cannot go back and avoid the responsibility. Similarly, this Appellate Tribunal cannot accept the argument of the Appellants that lower fee received by the Appellants meant lower responsibility.

- Based on above analysis, we find suitable logic in Respondent arguments and find that the absence of basic documents here, will hold the Appellants responsible for violation of SA 230.

Violation of SA 300, 315, 320 & 330 :-

- **SA 300** deals with the Auditor's responsibilities to plan an audit of financial statements. The fundamental objective of SA 300 is that the

Auditor plan the audit so that it audit will be performed in an effective manner. It includes involvement of key engagement team member, preliminary engagement activity, proper planning of audit alongwith suitable documentation.

- This enable the Auditor to design detect risk of material misstatement and to reduce same to an acceptable low level. This also help the Auditor to detect fraud or error by the Company.
- **SA 315**, prescribes for Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment, including internal control of the Company.
- **SA 320** also provides a definition of performance materiality, which means the amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality .
- **SA 330** deals with the auditor's responsibility to design and implement responses to the assessed risk of material misstatement identified in accordance with SA 315.

- The Appellants alleged that the Respondent falsely stated that the Appellant failed to comply with SA 315 and SA 330 for lack of documentation regarding the performance of risk assessment procedures for material misstatements at the financial statement level and assertion level and response to such risks etc. The Appellant stated that thus, did not express any opinion on the financial statements,

because the scope of audit undertaken by the Appellant did not cover expression of any opinion on financial statements of the Company.

- The Appellants reiterated that the defined scope of audit was to provide an audit report on the Trial Balance of the branch concerned and the role of a branch auditor with such defined scope of audit is to assist the principal auditor of the company. The Appellants further submitted that the Trial Balance certified by the Appellant carried no balances of loans granted, deposits collected, interests earned or spent, because these were centralized at Head Office's books of accounts. As such, the risk of material misstatement in the Trial Balance was only with respect to expenses incurred, as no other line item qualified to be tested for risk of material misstatement because of the accounting model of the company for its branches.
- It is the case of the Appellants that the documents on record, prove that the Appellant had carried a proper assessment and examination of the records for assessment and identification of material misstatement and other risks to financial statement of the company as a whole. Therefore, allegations regarding absence of an additional documentation of the process as in a check list for the purpose of these SAs are misconceived.
- Per contra, the Respondent stated that Appellants were guilty of Non-compliance with SA 300, SA 315, SA 320 & SA 330 for determining materiality, performance materiality and documentation thereof. The Respondent emphasised that the replies of the EP's showed disregard for professional standards and absence of professional behaviour on

EP's part as proper determination, application and revision of materiality are very basic to an audit which were not followed by the Appellants.

- The Respondent refuted the contention of the Appellants that "Elements of risks to the group (company) as a whole from the financial reporting point also was considered as evident from Annexure IX to the Auditor's Report for each branch". The Respondent stated that this is without any basis in the absence by the Appellants of any working papers to support mandatory documentation requirements of SA 315, SA 320 and SA 330.
- The Respondent contested the Appellants arguments regarding not violation of various SAs and further submitted that without any working papers in the Audit Files by the Appellants to satisfy the mandatory documentation requirements of SA 315, 320 and 330 for which compliance is required to be demonstrated by documents included within the audit files.
- This Appellate Tribunal has noted that "the concept of materiality is applied by the auditor both in planning and performing the audit and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report. We also observe that mandatory documentation requirements of these SAs include the factors considered in the determination of materiality for the financial statements as a whole, the materiality levels for particular classes of transactions, account balances or disclosures, performance materiality

and any revision of the materiality amounts as the audit progress. The audit documentation in the present case did not contain any of these details and hence the replies of the EPs are prima-facie not acceptable.

- It appears to us that the Appellants assumed their limited role w.r.t. Branch Audit which prima-facie is contrast to legal requirements as stipulated in the relevant SAs. The Impugned Orders brought out the shortcomings on the part of the Appellants in this regard and we tend to hold that the Respondent came to right conclusions.

Violation of SA 450

- **SA 450** deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.
- It has been alleged by the Respondent that the Appellant has failed to comply with SA 450 for non-evaluation of identified misstatements and uncorrected misstatement.
- It is the case of the Appellants that in the case of the company's branch audit, there were no instances of identified misstatements and therefore, there was no case to ensure correction of misstatements or to consider the effect of uncorrected misstatements. It is the case of the Appellants that the financial statements for the company as a whole was facilitated by the accounting system at Head Office and the limited role of the branch auditor, as defined in the scope of audit, was carried out with proper diligence and care. There were no instances of material misstatement found by the Appellant within the

limited scope of the audit task assigned to them. In view of the above there is no merit in the allegation of the requirements of SA 450 in this case.

- The Respondent amplified its stand that Branch Auditors are responsible for compliance of SAs and the Appellants plea of no role or limited role is lame excuse.
- The basic plea of the Appellants is that being branches, the trial balances and other financial statements of branches were not amenable for any type of misstatements and therefore there was no scopes for the Appellants to point out the same. We are afraid that this is not true in overall scheme of system as the Appellants were conducting Branch Audit of 17 Branches of DHFL. The financials of the Branches do affect the financial of the company and the same is true for Audit of Branches.
- We also note that in absence of detailed documentations by the Appellants, the defence taken by the Appellants are not convincing. We tend to agree with the Respondent.

Violation of SA 500

- The requirement of Para 6 of SA 500 is that the auditor shall design and perform audit procedures that are appropriate in the circumstances for the purpose of obtaining sufficient appropriate audit evidence.
- The Impugned Order finds that the Appellant has failed to comply with SA 500 in not designing and performing audit procedures to

obtain sufficient appropriate audit evidence and not evaluating the reliability of information produced by the Company. The Appellant submitted that these findings are without merits.

- It is case of the Appellants that it is a matter of judgment for the auditors to design the audit procedure to obtain audit evidence. The Appellant's branch audit reports clearly indicate that the Appellant had obtained evidence on the loans during verification.
- Per-contra, the Respondent stated that the Appellants are guilty of non-compliance with SA 500 in not designing and performing audit procedures to obtain sufficient appropriate audit evidence and not evaluating the reliability of information produced by the company. The Respondent refuted plea of the Appellants that "it is a matter of judgment for the auditor to design the audit procedure to obtain audit evidences". The Respondent stated that there is no evidence in the Audit File of designing and performing audit procedures, such as an audit plan, the substantive procedures performed and the conclusions drawn.
- We are aware that it is discretion of Auditors to design audit procedure to obtain audit evidence. However, this discretion is to be demonstrated to be used and used judiciously to show that the Appellants did design and in fact obtained such audit evidence. Mere statements made by the Appellants that they have exercised their judgement in Audit of Branches and obtain required audit evidence cannot be accepted in absence of suitable demonstration of the same

and in absence of such demonstration to show their meaningful Audit of Branches.

- This Appellate Tribunal also finds absence of suitable documentations to show compliance of SA 500. The defence of the Appellants seems to be sham defence.

Violation of SA 520

- **SA 520** deals with the auditor's use of analytical procedures as substantive procedures ("substantive analytical procedures"), and as procedures near the end of the audit that assist the auditor when forming an overall conclusion on the financial statements.
- It is case of the Appellant that the applicability of SA 520 is only when an auditor has to use substantive analytical procedures when forming an overall conclusion on the financial statements.
- It is the case of the Appellants that in the case of audit of the Company's branch done by the Appellants, the scope of work was limited to auditing the Trial Balance of the branch, which did not reflect any operating assets or liabilities attributed to the Branch by virtue of centralised ERP system followed by the Company. Therefore, neither any financial statements had been prepared for branches, nor was there any case to "form any overall conclusion" as provided in SA 520. Further, items that mattered for the financial statements of the Company, carried from the Trial Balance of the branch, were insignificant. In such situations, because there is no room for use of substantive procedures by the

auditor, SA 520 has no application. Hence the allegation is misconceived.

- The Respondent stated the Appellants were responsible for non-compliance SA 530 which relates to the determination of sample design, sample size and required audit procedures. The Respondent assailed the EP who submitted that the "basis of selection of sample was defined in the appointment letter itself, and the skills of judgment and competence of the auditor were applied to draw the required sample data.
- The Respondent stated that the conditions in the appointment letter do not evidence basis for EP's work and conclusions. It is the case of the Respondent that the SAs casts a responsibility on the auditor to design and perform audit procedures to obtain sufficient appropriate audit evidence on which to base the audit opinion. The terms dictated by the company cannot substitute this responsibility. There is no evidence that any of the sampling and the related procedures as detailed in SA 530 have been complied with by the EP, while the audit opinion is based on sample testing. In the absence of any evidence to show compliance with the determination of sample design, sample size and audit procedures performed on it, the contentions of the EP are not accepted.
- We have already examined and came to conclusion that all rules and procedure are equally applicable for the Audit of Company as a whole as well as for the Branches. Similarly, the SAs are applicable for entire company audit including Branch Audit, albeit,

as applicable. Although, it is a fact that the Appellants had limited role as Branch Auditors than the main Statutory Auditors, however, we can't ignore the fact that the firm were auditing 17 of branches of DHFL. This definitely affect the proportion of financial statement and as such SAs were applicable to them also. In view of this, we do not find error in the Impugned Order in this account.

- Based on above detailed SA wise analysis, we hold that the Appellants were rightly held responsible for violating of relevant SAs especially SA 210, SA 230 & SA 700. We do not find any error in Impugned Orders on these accounts.

Violation of SA 530

- The Appellants denied that they failed to comply with relating to the determination of sample design, sample size and required audit procedures. It is the case of the Appellants that the scope of the branches, and the scope of audit of one branch had specified 25 samples to be selected and reported and the Appellants selected 25 samples, examined and found no adverse remarks. The Appellants stated that the verification loan accounts the loan ledger accounts were centralized and not reflecting in the Trial Balance of the branches and the audit documentations contains 15 specific sample cases of top loans examined by the Appellants for every branch and about which observations were made.

- The Appellants pointed out that the basis of selection of sample was defined in the appointments letter itself, and the skills of judgment and competence of the auditors were applied to draw the required sample data and therefore, NFRA misconceived on false assumptions, without appreciating the facts on records.
- Per contra, it is the case of the Respondent that there is no evidence that any of the sampling and the related procedures as detailed in SA 530 have been complied with by the Appellants while executing the audit including for selection of random loan accounts to be reviewed, while the audit opinion is based on sample testing. In the absence of any evidence to show compliance with the determination of sample design, sample size and audit procedures performed on it, the contentions of the Appellants are without any basis. The Respondent also castigated the pleas of the Appellants that the basis of selection of sample was defined in the appointment letters itself. The Respondent stated that in the appointment letters nowhere specified any criterion for selection of "random" loan accounts for verification. The Respondent refuted that the Appellants claim that "the audit files clearly established that 25 samples had been duly examined and there were no adverse remarks" stands no merit in view of the various adverse remarks related to loan files noted by the appellant in the "CERTIFICATE" issued by them and pointed out in the Impugned Orders.

- We have noted contention of both the Appellants and the Respondents on SA 530. This Appellate Tribunal notes the contention of the Appellants that sample size was contained in the appointment letters of the Appellants and therefore their liability was limited and the SA was not applicable. However, we also noted averments of the Respondent/NFRA that there was no evidence of such sampling being complied by the Appellant. We find force of logic that mere selection of sample even though it might have been advised by the company gives any right to the Appellants not to comply with the relevant SAs. In view of these details, we do not find any error in the Impugned Order on this ground.

Violation of SA 700, "Forming an Opinion and Reporting on Financial Statements"

- **SA 700** deals with a company's auditor obligation to form an opinion and report on the "financial statements" of a company.
- As per SA 700, in order to form an opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. Such a conclusion shall take into account, inter alia, whether sufficient appropriate audit evidence has been obtained and whether uncorrected misstatements are material, individually or in aggregate.
- It is the case of the Appellants that the said SA has no applicability to a branch audit of the for the work conducted by the Appellants. The

Appellants submitted that the term "financial statements" has a specific meaning and connotation both under Section 2(40) of the 2013 Act as well as under SA 700 itself. It was clarified by the Appellants that DHFL made only one set of "financial statements" as a whole. The Appellants stated that there was no question for the Appellants for expressing any "opinion" on the "financial statements" of a branch office of a company. The Appellants submitted that in the present case, there was only one Statutory Auditor for the company to express opinion of the financial statements i.e., CAS. The Appellants, as a branch auditors, had limited scope of work - to provide Trial Balance after audit apart from certain predefined annexures. Therefore, the allegation with respect to the scope of SA 700, was based on incorrect perception of the relevant legal provisions and facts of the case presented above.

- It has been alleged by the Appellants that the Respondent has cherry picked stray statements from the Appellant's audit report and read them without any context. The final certification is evidently subject to the remarks made in other parts of the certificate and the incorporation of such remarks in the certificate itself indicates that the proper process of examination of the loan documents had been carried out by the Appellants. Moreover, the findings that there was absence of materiality levels documented in the audit file and that there was no assessment of the risk of misstatements and test of controls were also unfounded.

- Per contra, the Respondent denied all averments of the Appellants regarding non-violation of SA 700. The Respondent also assailed assumptions of the Appellants that their role was confined to only Branch Audit and they were not responsible for Audit of Company and they applied SA as necessary in circumstances. The Respondent submitted that Section 143(8) of Companies Act, 2013 clearly stipulate and specifies only Company Auditors and does not differentiate with Branch Auditors. Hence, the Appellants were fully responsible.
- It is the case of the Respondent that SA 700 was applicable to the Appellants and they were duty bound to evaluate effect of mis-statement and decided to appropriately modify the opinion.
- The Respondent elaborated the pitfalls of the Appellants and brought out some instances of failure on the part of the Appellants. The Respondent cited few specific instances of that from the audit file that in respect of loan files with loan code 1107 the EP noted in the "CERTIFICATE' for Kottayam Branch, that "Market Value Funding but amenities agreement not obtained'. For loan file with loan code 1275 the EP noted that "Market Value Funding, Broken Period Search Report not obtained". For loan file with loan code 1187 the EP noted that "Original plan not obtained. Similar "Remarks" were noted for other branches as well. All of these indicate the deficiencies identified by the EP during the audit. Despite such deficiencies, the EP issued a "CERTIFICATE " stating *"We also confirm the following:- ... The required documents including the security documents have been properly*

obtained". Nowhere in the audit file the EP has documented how these deficiencies were resolved while reaching the conclusion that all documents were properly obtained by him and how their impact was considered in forming the audit opinion.

- The Respondent also brought to our notice they such lapses relating to the verification of documents during the audit are viewed seriously by audit regulators.· For example, a Chartered Accountant, in the audit of a Bank branch, did not verify the securities for debts and was held guilty of professional misconduct of absence of due diligence and gross negligence. (A.N.Kapur -vs.- R.N. Budhiraja; Page- 374 of Vol. IX (1) of the Disciplinary Cases- ICAI Council's decision dated 11th and 12th April 2008).
- We have examined all these averments of both parties. We had already noted that the Appellants were responsible for Branch Audit of 17 Branches of DHFL. Even presuming the Appellants role as Branch Auditors and use of centralized ERP by DHFL, we cannot ignore the facts that for all such loan accounts the respective branches were directly involved. It is not difficult for us to imagine the adverse impact of non-adherence of SA and non expressing of correct opinion on financial statements of DHFL, when such large loans are with the domain of Branches directly or indirectly. The Branch Auditors cannot absolve themselves of their responsibilities.
- The reply of the EP regarding their non-violation of SA 700 cannot be accepted since it is apparent from the Trial Balance certified by the EP

that the loans were primarily appearing in the branch's Trial Balance and then transferred to the head office through entries in the branch books. The EP's claim in the "annexure" that rectification entry was recognized in books in the next financial year (i.e. on 02.04.2018) is also not supported by any evidence in the audit file. Hence, in the absence of materiality levels documented in the audit file, the pleadings of the Appellants are not convincing.

- We also note that NFRA did not find any documentation evidence from the Appellants to have complied with requirements of the SA 700 by the Appellants.
- In view of above discussions, we do not find any error in the Impugned Orders on this account.

Issue No. (VIII) Alleged violation of the Code of Ethics issued by ICAI and impact on Appeals before this Appellate Tribunal.

- The ICAI Code of Ethics, 2009 stipulates few fundamental principles like integrity, objectivity, professional competence and due care, confidentiality, professional behaviour. It is the duty of incoming Auditors to ascertain and ensure that the company has full filled all laid down norms before Auditors accept the assignment.
- It has been argued before us that the term “ascertain” means “ to find out for certain”. It is the case of the Respondent that the auditor should have found out for certain as to whether the Company has complied with the provisions of Sections 224, 224A and 225 of the Companies Act. It is the case of the Respondent that it would not be

sufficient for the auditor to accept a certificate from the management of the Company that the provisions of the above sections have been complied with. It is necessary for the incoming auditor to verify the relevant records of the Company and ascertain as to whether the Company has, in fact, complied with the provisions of the above sections.

- It is the case of the Appellants that ambiguity in the law is the reason for difference of views between the Appellants and the Respondent NFRA on the procedure that was to be followed for the appointment of the Appellant's firm as Branch Auditors of DHFL for 17-18. That is a matter of professional judgement. Therefore, there was no case for alleging not exercising due diligence or gross negligence against the Appellant.
- As regards, violation of Code of Ethics, the Appellants denied and stated that Clause (9) of Part I of First Schedule to the ICAI Act requires an incoming auditor to ascertain compliance of Section 225 of Companies Act, 1956 before accepting the appointment as an auditor of a company. The Appellants were not the incoming auditor of the company. The Appellants were existing Branch Auditors for the branches, and had no right or access to the other records of the company beyond the records of the branches concerned. It is the case of the Appellants that the intent of Clause (9) as part of the ICAI Act is reinforcement of an ethical requirement in the interest of CA profession, to ensure that an incoming auditor ascertains himself before accepting his appointment as an auditor of a company, that an

existing auditor was not removed without following due process as laid down in Section 225. The Appellants submitted that, therefore, the application of Clause (9) has altogether a different purpose and it must be in the context of a grievance by a previous auditor or by a shareholder, unlike the context in which NFRA has applied the provision against the Appellant.

- This Appellate Tribunal finds the code of ethics to be very important to any profession to maintain high integrity and high standards, it expects its members to follow to keep public trust. In this regard, we find the judgment in the matter of ***Institute of Chartered Accountants of India Vs. Vivek Kapoor & Ors***. *[(2016) SCC OnLine P&H 7501].* The relevant portion reads as under :-

> *"15. International Federation of Accountants in its Code of Ethics had given great importance to public interest. It was framed with objectives of credibility, professionalism, quality of service and confidence keeping in view fundamental principles of integrity etc.*
>
> *16. From the facts, noticed above, it is clear that respondent No. 1 grossly violated the code of ethics for Chartered Accountants. He admitted his guilt before the Income-tax authorities, which resulted in defrauding the revenue. Thereafter, he left the country. He did not avail of the opportunity afforded to him at different stages to defend the case against him. A professional, who behaves in this manner, deserves to be dealt with sternly. In our opinion, the conduct of respondent No. 1 is wholly unworthy of a*

Chartered Accountant, who is expected to maintain high standard of professional conduct. The punishment proposed by the Institute in these circumstances is quite lighter. Such a professional deserves to be debarred from practice for life time. Hence, in exercise of powers conferred under Section 21(6) of the Act, we deem it appropriate to direct that name of respondent No. 1 be removed from the register of members of the Institute for life. Ordered accordingly."

(Emphasis Supplied)

- Thus, violation of Code of Ethic will hold the Auditor to be liable for the penalty as stipulated in Section 132 of the Companies Act, 2013.
- It is clear from ICAI Code of Ethics, 2009 that it is responsibility of the auditors to ascertain and ensure compliance with the provision of law is applicable and therefore, the Respondent has correctly pointed out that it is incumbent on the part of Auditors to verify the relevant record of the company to ascertain whether the company has complied with the provisions regarding appointment and other relevant issues rather than accepting the statements of the company that they have complied with.
- It is undisputed fact that the Appellants themselves did not verify if DHFL followed correct procedures for appointment of Branch Auditors before the Appellants accepted the same. The submissions of the Appellants are therefore not convincing.

- We, therefore, do not find any error in the Impugned Orders on this issue.

Issue No. (IX) Excessive V/s adequate imposition of penalty on Appellant, herein..

- We have already discussed at length the penalty provisions as available in Chartered Accountants, Act 1949 to ICAI and penalty provision as available in Companies Act, 2013 as available to NFRA.
- We have noted that under Section 132 (4) (c) of Companies Act, 2013, NFRA can impose fine of :-

> ***"132. Constitution of National Financial Reporting Authority-***
> *(4) Notwithstanding anything contained in any other law for the time being in force, the National Financial Reporting Authority shall—*
> *(c) where professional or other misconduct is proved, have the power to make order for— (A) imposing penalty of— (I) not less than one lakh rupees, but which may extend to five times of the fees received, in case of individuals; and (II) not less than ten lakh rupees, but which may extend to ten times of the fees received, in case of firms;*
> *(B) debarring the member or the firm from engaging himself or itself from practice as member of the Institute of Chartered Accountant of India referred to in clause (e) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 for a minimum period of six months or for such higher period not*

exceeding ten years as may be decided by the National Financial Reporting Authority.

Explanation.—For the purposes of his sub-section, the expression "professional or other misconduct" shall have the same meaning assigned to it under section 22 of the Chartered Accountants Act, 1949."

(Emphasis Supplied)

- As against minimum penalty of Rs. 1 lakh in case of individual Charted Accountant and maximum penalty of five times of fee received; NFRA has imposed minimum penalty as stipulated in Companies Act, 2013 i.e., Rs. 1 Lakh on all four Appellants herein.
- As regards debarment of the Appellant for one year, NFRA has power to debar for a period of minimum six months and maximum ten years. The penalty of one year debarment on all four Appellant cannot be considered excessive.
- We find that NFRA applied the principle of proportionality and imposed minimal permissible penalty i.e., a monetary fine of Rs. 100,000 and the Appellants have been barred from practicing for a period of one year which is 10% of max. penalty permissible.
- The need to deter fraud or collusive behaviour and reckless behaviour of the Auditors and repercussions of negligent audits are quite evident.
- Hence, we consider the penalty as imposed by NFRA on all four Appellants were imposed as deterrent, perhaps keeping in mind all facts, including limited role as branch auditors. This cannot be

considered excessive after all; it is fact that there has been fraud in DHFL of Rs. 31,000 Crores and Auditors can't pretend to be ignorant of what was happening.

Issue No. (X) Can automatically stay is triggered on deposited of 10% penalty and appeal is made before NCLAT.

- This Appellate Tribunal observes that the averments of the Appellants regarding interpretation of Rule 11 & 12 of NFRA Rules, 2018 are not correct as this Appellate Tribunal has discussed at length the interpretation of Rule 11&12 of NFRA Rules, 2018 and clarified that mere filing of appeal does not affect the order on debarment with respect to compliance of Rule 12. The relevant Paragraphs of our earlier Order dated 02.06.2023 passed in Company Appeal (AT) No. 68, 87, 88, 89,90, 91, 92, 93 & 94 of 2023 are reproduced below:

> *"20. However, we hasten to add that when order passed under Section 132(4)(c) is challenged by filing an Appeal, it is for the Appellate Court to consider as to whether the implementation of the order impugned is to be stayed or not. It is, thus, clear that unless any interim order is obtained in an Appeal, filed challenging the order passed under Section 132(4)(c), the Auditor against whom order of debarment has been passed, ceases to function after expiry of thirty days from the order, unless order indicate otherwise...*
>
> *21. In view of the foregoing discussions and conclusion, we are of the view that filing of the Appeal by the Appellant(s) with deposit of 10% of the penalty shall have no effect on the order of 'debarment' passed against the Appellant(s) under Section 132(4)(c) and under head (B).*

Order of 'debarment' shall continue to operate unless an order is passed by the Appellate Tribunal."

(emphasis supplied)

- We will also add that the above judgment of this Appellate Tribunal has already been challenged in the Appeal by the Appellants with a prayer to grant stay and the Hon'ble Supreme Court of India in Civil Appeal No. 4606/ 2023 has not granted the stay and the Appeal is under consideration by the Apex Court.

Final Conclusions:

87. We feel that it is of utmost importance that Auditors realise their responsibilities which is necessary not only to the company but also to the public. In view thereof, giving effect to the Impugned Orders which highlights the professional misconduct and other misconduct on the part of the appellant vis-à-vis a public listed company become quintessential so as to make public aware and enable them to make informed and sound financial decisions and investments. Any deviation to this will only result is catastrophic effect on economy of the nation and cause immense prejudice and harm to the public, shareholders and various stakeholders such as banks, lenders, and creditors. NFRA, as an independent audit regulator has been entrusted by the Parliament after great debate for protecting public interest including of the creditors by exercising effective oversight over accounting and auditing functions.

88. Based on above detailed analysis earlier, we do not find any error in the Impugned Orders of NFRA as challenged in four Appeals before us.

89. In fine, all four Appeals fail and stand dismissed, devoid of any merit. No Cost. Interlocutory Application(s), if any, are Closed.

[Justice Rakesh Kumar Jain]
Member (Judicial)

[Mr. Naresh Salecha]
Member (Technical)

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