

भारत सरकार / Government of India
राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण / National Financial Reporting Authority

7th – 8th Floor, Hindustan Times House,
Kasturba Gandhi Marg, New Delhi

No. 62/2023

Dated: 22.11.2023

ORDER

In the matter of CA Nilesh Chheda (ICAI Membership No 124810) under Section 132(4) of the Companies Act 2013 read with Rule 11(6) of National Financial Reporting Authority Rules 2018.

1. This Order disposes of the Show Cause Notice ('SCN' hereafter) of even no. dated 16.11.2022, issued to CA Nilesh Chheda. CA Nilesh Chheda is a Member of the Institute of Chartered Accountants of India ('ICAI' hereafter) and was the Engagement Partner ('EP' hereafter) for the statutory audit of MAN Industries (India) Limited, Mumbai ('MIIL' or 'the Company' hereafter) for the Financial Year ('FY' hereafter) 2016-17.
2. This Order is divided into the following sections:
 - A. Executive Summary
 - B. Introduction & Background
 - C. Major Lapses in the Audit
 - D. Other Lapses in The Audit
 - E. Articles of Charges of Professional Misconduct by the EP
 - F. Penalty & Sanctions

A. Executive Summary

3. National Financial Reporting Authority (NFRA) is India's independent regulator, in respect of matters relating to accounting and auditing, of prescribed classes¹ of entities which can be broadly described as 'Public Interest Entities' (PIEs).
4. NFRA initiated action under Section 132(4) of the Companies Act, 2013 (**the Act**) for investigating into professional or other misconduct of the statutory auditor of MIIL, a listed company, following information received from Securities and Exchange Board of India (**SEBI**) vide letter dated 23.06.2022 regarding financial irregularities committed by MIIL.
5. MIIL is a manufacturer and exporter of large diameter Carbon Steel Line Pipes for various high pressure transmission applications for Gas, Crude Oil, Petrochemical Products and

¹ Rule 3 of NFRA Rules, 2018

Potable Water. By virtue of being listed, MIIL falls under the jurisdiction of NFRA under Rule 3 of NFRA Rules, 2018.

6. M/s Rohira Mehta & Associates, Chartered Accountants (presently RMA & Co.), Firm Registration No 118777W, was the statutory auditor of MIIL and CA Nilesh Chheda was the Engagement Partner (EP) for this statutory audit for the FY 2016-17.
7. Finding a prima facie case for investigation following the SEBI information, NFRA called for the Audit File on 03.08.2022. A review of the Audit File revealed a number of significant failures on the part of the EP and a SCN identifying the EP's professional misconduct was issued to the EP on 16.11.2022. The EP replied to the SCN on 16.01.2023 after availing extension of time. The EP availed of the personal hearing held on 21.09.2023 at the office of NFRA along with his legal counsel.
8. This Order contains our findings on the instances of professional misconduct against the EP, examined in light of his reply to the SCN, proceedings in the personal hearing and other material on record. The major lapses have been discussed in section C, while other lapses have been discussed in section D of this Order. These lapses relate to the EP's failure to identify and report material misstatements in the financial statements and sub-standard audit work in view of the following:
 - a) The EP 'Qualified' his opinion on Consolidated Financial Statements (CFS) stating that the Financial Statements reflected 'true and fair view' except for the effect of non-consolidation of a subsidiary, Merino Shelters Private Limited (MSPL). This was not correct as the impact of the grounds for qualification was both material and pervasive since the assets and liabilities of MSPL constituted about 19.20% and 28.96 % respectively of the assets and liabilities of MIIL. As per Para 8 of SA 705, the EP was required to give an adverse opinion (**para 18-21**) where the effect is material and pervasive.
 - b) Financial Statements did not contain required disclosures mandated by Ind AS 24² and the Act, in respect of critical and sensitive information pertaining to Related Party Transactions and non-disclosure of full particulars of loans etc. (**para 84-86 and 91-93**).
 - c) Disclosures in respect of Credit Risk Profile of Trade Receivables were erroneous and were not in compliance with requirements of Ind AS 107³ (**para 35-44**).
 - d) The EP did not obtain Sufficient Appropriate Audit Evidence (SAAE) in a number of critical areas of audit viz., non-consolidation of a material subsidiary (**para 18-21**), credit risk evaluation of Trade Receivables (**para 43-44**) and failure to perform risk assessment procedures and response to such risks (**para 64-72**).
 - e) The EP failed to demonstrate sufficiency and appropriateness of audit work in virtually every critical building block of an audit of Financial Statements i.e., Audit Strategy, Planning (**para 45 to 48**), Analytical Procedures (**para 50-54**), Determining Materiality (**para 55 to 61**), identification and assessment of ROMM through an understanding of the entity's environment and internal control (**para 62 to 66**),

² Indian Accounting Standard 24, Related Party Disclosures (Ind AS 24)

³ Indian Accounting Standard 107, Financial Instruments: Disclosures (Ind AS 107)

resulting in non-compliance with Standards on Auditing, notified under Section of 143 (10) and made mandatory under section 143 (9) of the Act.

9. Considering the professional misconduct of the EP, this Order imposes upon CA Nilesh Chheda a monetary penalty of Rs.5,00,000 (Rupees Five Lakhs Only). CA Nilesh Chheda is also debarred for 5 (Five) years 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.

B. Introduction and Background

10. NFRA is a statutory authority set up under Section 132 of the Act to monitor implementation and enforce compliance of the auditing and accounting standards and to oversee the quality of service of the professions associated with ensuring compliance with such standards. NFRA has the responsibility to protect the public interest and the interests of the investors, creditors and others associated with the companies or bodies corporate governed by it. Under Section 132(4) of the Act, NFRA is vested with the powers of a civil court and can investigate the professional misconduct of the auditors of prescribed classes⁴ of companies and impose penalty for professional or other misconduct of the individual members or firms of chartered accountants.
11. The statutory auditors, both individual and firm of chartered accountants, are appointed under Section 139 of the Act. The statutory auditors, including the Engagement Partners and the Engagement Team that conducts the audit are bound by the duties and responsibilities prescribed in the Act, the Rules made thereunder, the Standards on Auditing (SA hereafter), including the Standards on Quality Control and the Code of Ethics, the violation of which constitutes professional misconduct, and is punishable with penalties prescribed under Section 132(4) (c) of the Act.
12. On receipt of information from Securities and Exchange Board of India (SEBI) vide letter dated 23.06.2022 regarding financial irregularities committed by MIIL, NFRA took up for investigation, under Section 132(4) of the Act, the possible violations of the SAs by the Statutory Auditor of M/s MAN Industries (India) Limited (MIIL), a company situated in Mumbai.
13. MIIL is a manufacturer and exporter of large diameter Carbon Steel Line Pipes for various high pressure transmission applications for Gas, Crude Oil, Petrochemical Products and Potable Water. MIIL is listed on Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) and therefore falls under the jurisdiction of NFRA under Rule 3 of NFRA Rules, 2018. As per Rule 4 of the Companies (Indian Accounting Standard) Rules, 2015, MIIL 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 from the FY 2016-17. Table 1 below depicts certain key financial features of MIIL and the shareholding pattern of MIIL for the FY 2016-17, FY 2015-16, and FY 2014-15, which indicate substantial public interest.

⁴ Rule 3 of NFRA, 2018

Table 1: Some key financial features of MIIL

(Numbers except percentages are in Rs Crores)			
Particulars	31.03.2017	31.03.2016	31.03.2015
Shareholding Pattern			
<i>Public</i>	54.94%	54.94%	54.21%
<i>Individual</i>	38.92%	38.92%	40.6%
Revenue from Operations	1060.49	1391.68	1364.02
PBT	43.39	92.86	64.14
Equity			
Borrowing from Banks	221.65	276.50	264.68

14. M/s Rohira Mehta & Associates, Chartered Accountants (presently RMA & Co.), Firm Registration No 118777W, was the statutory auditor of MIIL and CA Nilesh Chheda was the Engagement Partner (EP) for this statutory audit for the FY 2016-17. The EP & the Firm (statutory auditors) were instructed on 03.08.2022 to submit the Audit File and other relevant information, which they did on 18.08.2022.
15. The examination of the Audit File revealed that the audit had been conducted in disregard of most of the SAs and the requirements of the Act but the EP had issued an unmodified opinion in Independent Auditor's Report⁵ for the Standalone Financial Statements (SFS) and a qualified opinion on the Consolidated Financial Statements (CFS) certifying that the Financial Statements of MIIL reflected true and fair view in conformity with the accounting principles generally accepted in India.
16. On satisfaction that a sufficient cause existed to take action under sub section (4) of Section 132 of the Companies Act, 2013, a Show Cause Notice (SCN hereafter) was issued to the EP dated 16.11.2022 in terms of Rule 11 of the NFRA Rules 2018 asking him to show cause why action should not be taken against him for professional misconduct in respect of his performance of the audit of M/s MAN Industries (India) Limited for the year 2016-2017. The EP was charged with professional misconduct of:
- failure 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;
 - failure to report a material misstatement known to him to appear in a financial statement with which the EP is concerned in a professional capacity;

⁵ Audit Report dated 30.5.2017

- (c) failure to exercise due diligence, and being grossly negligent in the conduct of professional duties;
- (d) failure 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; and
- (e) failure to invite attention to any material departure from the generally accepted procedures of audit applicable to the circumstances.

17. The EP vide letter dated 15.12.2022 requested for extension of time for submission of reply to the SCN, which was granted. The EP submitted his reply vide email dated 16.01.2023. The EP also availed the opportunity of personal hearing, which was held on 21.09.2023 at the office of NFRA, New Delhi. The EP was assisted by Mr. Nirav Mehta, Partner of the firm, and was also represented by legal counsel Mr. Karan Malhotra, Advocate. This Order is based on the review of the Audit File, written responses of the EP, submissions made during and after personal hearing and other material available on record. Each of the charges in the SCN is analysed and discussed in Part C and D of this Order.

C. MAJOR LAPSES IN THE AUDIT

C1. Failure to report non-consolidation of subsidiary

18. The EP was charged with failure to appropriately modify his audit opinion as per SA 705, even though the accounts of MIIL's wholly owned subsidiary viz., Merino Shelters Pvt. Ltd (MSPL), were not consolidated in the Financial Statements of MIIL, as per Ind AS 110.⁶ The EP had qualified his Audit Report for non-consolidation of MSPL in the Financial Statements of MIIL. MSPL was the wholly owned subsidiary of MAN Infra Projects Private Limited (MIPL), which in turn was the wholly owned subsidiary of MIIL. Pursuant to the Scheme of Arrangement approved by Hon. High Court of Bombay vide order dated 20.03.2015, which was to be made effective from 01.04.2013, the shares held by MIPL in MSPL were transferred to MIIL and accordingly MSPL became wholly owned subsidiary of the MIIL from 01.04.2013. MIIL gave effect to this Scheme of Arrangement in its Financial Statements for the FY 2014-15 but discontinued the consolidation from FY 2016-17.
19. The EP replied that they had been informed of an ongoing legal dispute between the promoters in relation to the control of MSPL pending in Hon. Bombay High Court, and that the consolidation of the financials of MSPL as a subsidiary of MIIL would not only lead to an incorrect disclosure but also result in contempt of court due to the pendency of the proceedings before the Hon. Bombay High Court. The EP submitted that he relied on a legal opinion obtained by the Company from M/s. Kanga & Co dated 18.12.2015 wherein they had advised MIIL not to treat MSPL as a wholly owned subsidiary of MIIL and not to consolidate the financials of MSPL with MIIL till the legal proceedings were disposed of. The EP stated that non-consolidation of MSPL barely had any material

⁶ Indian Accounting Standard (Ind AS) 110, *Consolidated Financial Statements*

impact on the Financial Statements of MIIL and would not be pervasive in nature and therefore, not meriting an adverse opinion.

20. In the Personal Hearing (PH) held on 21.09.2023, when specifically asked whether there was any stay granted by Hon. Bombay High Court in respect of the Scheme of Arrangement referred to in the preceding paragraph, the EP replied that there was no stay order, and his qualification was based on legal opinion provided by the Company. The EP admitted that he should have given an adverse opinion instead of a mere qualification in view of the material and pervasive effect of the non-consolidation. NFRA also sought clarification from the Company whether there was any stay order of Hon. Bombay High Court on consolidation of MSPL with MIIL and provide a copy of such order, if any. The Company vide email dated November 20, 2023, informed that the legal opinion obtained from a reputed law firm in December 2015 was that since the Hon. Bombay High Court was seized with the implementation of the Scheme of Merger and Demerger, consolidation of MSPL with MIIL be deferred until adjudication thereof.
21. The EP issued a qualified opinion on account of non-consolidation of MSPL in MIIL. The EP stated in his reply to the SCN that the consolidation would have resulted in contempt of the court of law due to the pendency of the proceedings before the Hon. Bombay High Court. We observe that the Audit File for FY 2016-17 as also the EP's reply to the SCN, do not contain any order of Hon. Bombay High Court, nor any evaluation of the legal opinion provided by the Company taken in 2015. In light of the details in paragraph 20 above, it is seen that the Hon. Bombay High Court had not stayed consolidation of the said account. Thus, the plea taken by the EP does not hold. The impact of non-consolidation of Financial Statements of MSPL into that of MIIL was material and pervasive, as the assets and liabilities of MSPL constituted about 19.20% and 28.96 % respectively of the assets and liabilities of MIIL (Table 2) and resulted in exclusion of additional information, required under Schedule III to the Companies Act, 2013, of enterprises consolidated as subsidiary/ associates /joint ventures.

Table 2

(In Rs. Crore)

Particulars	MIIL (Published Consolidated Financials) As on 31.03.2017	MSPL as on 31.03.2017	MSPL as % of MIIL
Total Assets	1356.39	260.43	19.20 %
Total Liabilities	758.11	219.57	28.96 %
Net Worth	598.28	40.85	6.83 %

In light of above, we conclude that the qualified opinion by the EP, when there was sufficient basis for an adverse opinion, was without due diligence and without obtaining sufficient appropriate audit evidence, and thus the EP failed to comply with Para 8 of SA 705. As mentioned above, the EP too during personal hearing has acknowledged this lapse.

C2. Failure to prepare audit documentation

22. The EP was charged with non-compliance with Para 8, 9 and 10 of SA 230⁷.

23. Responding to the charge, the EP submitted that the audit documentation prepared and maintained during the course of audit is sufficient to understand the nature, timing and extent of audit procedures performed to comply with legal and regulatory requirements. The EP further stated that a proper requisition list was prepared, documents were collated and post-formation of the opinion, a detailed discussion transpired with the EQCR Partner. Thereafter, final audit points were identified by the EP and discussed with the EQCR Partner Nirav B. Mehta, along with the conclusions reached and the basis of such decision has also been recorded⁸. Further, the EP referred to documentation including the valuation report for impairment testing from the external professionals⁹, actuarial valuation report from the external professionals¹⁰, confirmation for bank balance, outstanding bank loan, bank guarantee and letter of credit directly from the bankers¹¹. The EP stated that external confirmations as required by SA 505 had been undertaken by him.

24. Our review of the Audit Files submitted to NFRA shows several anomalies clearly evidencing tampering by creation of additional documents to mislead NFRA. Page Number 11 to 14 of the Audit File 1 HO contains the Audit Firm's letter dated 15 April 2017 to the Company requesting information regarding Statutory Requirements for the period from 01.04.2016 to 31.03.2017 but the letter refers to the facts relating to a later period as shown below:

i) Clause (A) 9 & 10, reproduced below, contain audit requirements relevant to Goods and Services Tax (GST) which was introduced in India on 01.07.2017. These requirements would not be relevant for the audit of Financial Statements for the Financial Year ending on 31.03.2017 as the GST was introduced at a later date.

“9. Provide reconciliation of Sales as per GSTR 1, GSTR 3B and Sales as per books of accounts.

10. Provide Reconciliation of balance of GST credit lying in the electronic credit ledger & cash ledger with the balances in the books of accounts.”

ii) Clause (A) 26 of the letter contains request for ‘Ageing of debtors and creditors o/s as 31.03.2021’ whereas the audit relates to FY ending 31.03.2017.

iii) Clause B (3) of the above referred work paper requests for details regarding payment made towards GST, which had not even been introduced in the period under audit.

iv) Clause (B) 10 requests for details of lease rental paid as per Ind AS 116, *Leases*, which came into force for accounting period starting 01.04.2019 and therefore was not relevant for FY ending 31.03.2017.

⁷ SA 230 Audit Documentation

⁸ Page 42 to 43 of Audit Paper Book

⁹ Page 1587 to 1620 of Audit Paper Book

¹⁰ Page 1188 to 1531 & 2848 to 2891 of Audit Paper Book

¹¹ Page 299 to 614 of Audit Paper Book

In view of the above, it is clear that this important work paper has been inserted in the Audit File after the SCN was issued by NFRA and the Audit File has been tampered with while submitting to NFRA pursuant to issuance of SCN by NFRA.

25. When confronted with these facts during the personal hearing, the EP attributed it to a typographical error. Mr. Nirav Mehta, the EQCR Partner, stated that all such information requests to the Company were sent by email, which they shall provide along with Section 65B Certification under Indian Evidence Act. We have reviewed the copies of the emails sent by the EP vide email dated 22.09.2023 and note that the EP had sought information with reference to Accounting Standards such as, revenue recognition in accordance with AS-9, list of all related parties as per AS-18, lease rental received and paid as per AS-19, list and computation of impaired assets as per AS-28 and borrowing costs as per AS-16, which were no longer applicable to the Company as it had prepared and presented the Financial Statements for FY 2016-17 in accordance with Ind ASs. Thus, the papers presented not only establish the tampering of the Audit File but also the complete ignorance of the EP about the applicable accounting framework.
26. Internationally, alteration, backdating of Audit Work Papers, substitution or addition of new AWP's subsequent to the issue of audit report are viewed seriously. For example, PCAOB in the matter of KPMG S.A.S.¹² observed that ‘.....After learning that the Board’s Division of Registration and Inspections (“DRI”) would be inspecting the Firm’s audit work for the Issuer A Component Audit and Issuer B Component Audit, KPMG Colombia personnel improperly modified work papers and backdated those work papers to conceal from DRI that they had been modified. As a result, and as further described below, the Firm violated PCAOB Rule 4006, Duty to Cooperate with Inspectors; AS 3, Audit Documentation; and ET § 102, Integrity and Objectivity’. For this misconduct, inter-alia, a civil money penalty in the amount of USD 4 Million was imposed on KPMG S.A.S., required the firm to undertake remedial actions.
27. We also observed other deficiencies in the following work papers mentioned by the EP in his reply regarding audit documentation:

Table 3

S.No.	Working Paper No.	Particulars	Observation
I.	Working paper at Page 42 to 43 of Audit Paper Book	Working Paper regarding final audit points identified by the EP and discussed with the EQCR Partner	Signed by the EP and EQCR Partner, but no date is mentioned on the work paper. There is no proof that discussion took place and clearance given by EQCR Partner on or before the date of the auditor’s report, as required by the SQC1.
II.	Working paper at Page 1587 to 1620 of Audit Paper Book	Working Paper regarding valuation report for impairment	Valuation report is placed in the Audit File but there is no evaluation by the EP of the valuation report.

¹² PCAOB Release No. 105-2022-034 December 6, 2022

		testing from the external professionals	
III.	Working paper at Page 1488 to 1531 & 2848 to 2891 of Audit Paper Book	Working Paper regarding actuarial valuation report from the external professionals	Valuation report is placed in the Audit File but there is no evaluation by the EP of the valuation done. Actuarial Valuation report was dated 04.08.2017, after the audit report was signed on 30.05.2017. This working paper is incorporated after 60 days of Audit casting serious doubt on the integrity of Audit File.
IV.	Working Paper at Page 299 to 614 of Audit Paper Book	Working Paper regarding confirmation for bank balance, outstanding bank loan, bank guarantee and letter of credit directly from the bankers	As per Para 16 of SA 505, the Auditor shall evaluate whether the results of the external confirmation procedures provide relevant and reliable audit evidence, or whether performing further audit procedures is necessary. No such evaluation is made by the EP and no conclusion is drawn by EP and reviewed by EQCR.

28. Based on the above observations, it is evident that the EP has not prepared audit documentation as per Para 8 of SA 230 which requires the auditor to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit to understand:
- The nature, timing, and extent of the audit procedures performed to comply with the SAs and applicable legal and regulatory requirements;
 - The results of the audit procedures performed, and the audit evidence obtained; and
 - Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.
29. The averment made by the EP that the audit documentation was sufficient to enable him to understand the nature, timing and extent of audit procedures performed, is not tenable as it fails in one of the objectives of the audit documentation that is sufficient to enable an experienced auditor having no previous connection with the audit to understand (a), (b) and (c) above.
30. Further, there was no audit evidence as to who performed the audit work, who reviewed the audit work performed, and the date and extent of such review, reflecting violation of Para 9 of SA 230.
31. The EP has also failed to document discussions of significant matters with TCWG, including the nature of significant matters discussed, and when and with whom the discussions took place as per Para 10 of SA 230. We therefore conclude that the EP has

not only tampered with the Audit Work Papers but failed to comply with provisions of SA 230 thereby showing gross negligence and failure to adhere to the fundamental principles of Code of Ethics¹³ viz. Integrity and Professional Behavior.

32. The above position clearly demonstrates EP's negligence in the preparation of audit documents and conduct of audit of public interest entity in a casual manner, apart from the misconduct of Audit File tampering. He failed to meet the objectives of SA 230 to prepare documentation that provides sufficient and appropriate record for the basis of auditor's report and evidence that the audit was planned and performed in accordance with SAs. The Audit File primarily contains invoices/bills and information taken from the Company and does not record professional judgements and significant conclusions/decisions made by the EP and the basis for that. Non-documentation of the work performed is clear evidence that the work has not been performed. It is apposite to note the following observations of the Australian Audit Regulator ASIC:

*"Firms often assert that our findings relate to documentation deficiencies in their audit file. An audit file should contain sufficient detail for an experienced auditor to understand the work performed and relied on in forming conclusions. **Where this detail has not been documented, our presumption is that the work has not been performed. We have used this approach for several years and it is consistent with the approach applied globally by other audit regulators and in most firm internal quality review programs.**"*¹⁴ (Emphasis supplied)

33. Lack of sufficient documentation has been viewed seriously by national and international regulators as well. For example, in the matter of Bharat Parikh & Associates Chartered Accountants, dated 19.03.2019, the US audit regulator PCAOB took a serious view of the lack of sufficient documentation and imposed penalties and sanctions for violations including insufficient documentation. The PCAOB order states that *"....Audit documentation must contain sufficient information to enable an experienced auditor, having no previous connection with the engagement to: (a) understand the nature, timing, extent, and results of the procedures performed, evidence obtained, and conclusions reached, and (b) determine who performed the work and the date such work was completed as well as the person who reviewed the work and the date of such review.....the documentation for each of those audits was insufficient to demonstrate the nature, timing, extent, and results of the procedures performed, evidence obtained, and conclusions reached, including in those areas of the audits involving significant risks. For the FY 2016 and 2017 Issuer A audits, the documentation also failed to demonstrate who performed the work and the date such work was completed. Additionally, in each of the Issuer A and Issuer B audits, the audit documentation was insufficient to demonstrate which aspects of the audit and which audit documentation Bharat Parikh reviewed."*

34. The Executive Counsel to the Financial Reporting Council (FRC), the UK Audit Regulator, in the matter pertaining to Deloitte LLP and John Charlton in the audit of Mitie Group plc.

¹³ Para 100.4 (a) and (e) of Code of Ethics 2009 issued by the Institute of Chartered Accountants of India

¹⁴ Refer Page 7 of ASIC Audit Inspection Report – Report 743 October 2022

for the year ended 31 March 2016, imposed a financial sanction of Two Million Pounds, a published statement in the form of severe reprimand against Deloitte and a financial sanction of 65,000 Pounds and a published statement in the form of a severe reprimand against Charlton besides other things, for breach of ISA 230 as they failed to adequately document the audit work papers.

C3. Failure to report issues related to disclosure of Credit Risk Exposure

35. The EP was charged with failure to report issues related to disclosure of Credit Risk Exposure of financial instruments -Trade Receivables as per Ind AS 107¹⁵. The EP failed to report that the Company had not made disclosure as required by Para 35 M and 35N of Ind AS 107 regarding credit risk profile of its Trade Receivables based on well accepted parameters such as provision matrix used for credit risk management and recognising and measuring the impairment loss allowance of this category of financial assets. The company failed to disclose the ageing bucket of trade receivables, and the EP failed to report this non-disclosure in his audit report, which is a material non-compliance with the requirements of the applicable financial reporting framework.
36. The Ind AS Implementation Guidance-Guidance on implementing IFRS 7 Financial Instruments: Disclosure, IG20D, reproduced below at Table 4, illustrates the disclosures required by Paragraph 35M and 35N.

Table 4

20XX CU'000	Trade receivables days past due				
Dealer financing	Current	More than 30 days	More than 60 days	More than 90 days	Total
Expected credit loss rate	0.10%	2%	5%	13%	
Estimated total gross carrying amount at default	CU20,777	CU1,416	CU673	CU235	CU23,101
Lifetime expected credit losses—dealer financing	CU21	CU28	CU34	CU31	CU114
Customer financing					
Expected credit loss rate	0.20%	3%	8%	15%	
Estimated total gross carrying amount at default	CU19,222	CU2,010	CU301	CU154	CU21,687
Lifetime expected credit losses—customer financing	CU38	CU60	CU24	CU23	CU145

¹⁵ Indian Accounting Standard (Ind AS) 107, *Financial Instruments: Disclosures*

37. Further, the Company should have shown disclosures as per Ind AS Implementation Guidance-Example 12-Provision Matrix of Illustrative Examples of IFRS 9¹⁶ Financial Instruments (shown in Table 5 & 6 below), which illustrates the disclosures required for impairment loss allowance of Trade Receivables.

Table 5

IE76 On that basis, Company M estimates the following provision matrix:

	Current	1–30 days past due	31–60 days past due	61–90 days past due	More than 90 days past due
Default rate	0.3%	1.6%	3.6%	6.6%	10.6%

Table 6

IE77 The trade receivables from the large number of small customers amount to CU30 million and are measured using the provision matrix.

	Gross carrying amount	Lifetime expected credit loss allowance (Gross carrying amount x lifetime expected credit loss rate)
Current	CU15,000,000	CU45,000
1–30 days past due	CU7,500,000	CU120,000
31–60 days past due	CU4,000,000	CU144,000
61–90 days past due	CU2,500,000	CU165,000
More than 90 days past due	CU1,000,000	CU106,000
	CU30,000,000	CU580,000

38. As can be seen from Table 4, 5 and 6, the EP failed to report in his audit report the non-disclosure by the Company of material information regarding credit risk profile of Trade Receivables as per Para 35M and 35N of Ind AS 107.

39. The EP was required to obtain independent external confirmations according to the requirements of SA 505 in respect of Trade Receivables which constituted a material (25.09%) percentage of total assets of MIIL to ascertain the accuracy, existence, genuineness, and recoverability of these balances. On perusal of the Audit File, no documentation was found evidencing that EP had performed the critical, generally accepted audit procedure of obtaining independent external confirmation of Trade Receivables balances, which is in violation of SA 505. The EP's reasoning that the majority of transactions were with foreign parties is not convincing as the international trade transactions are also prone to risk of fraudulent or spurious transactions.

¹⁶https://indasaccess.icaai.org/download/2019/asb052019/147/147BB2019_B_IFRS9%20Financial%20Instruments.pdf

40. The EP was also charged for not questioning the disclosure by the Company in its Financial Statement for 2016-2017 that the credit risk from Trade Receivable was perceived as historically low. It is observed that during the previous FY i.e., 2015-16, the Company had written off substantial amounts of Trade Receivables (Rs. 28.12 Crore), a significant class of account balance constituting a material percentage (30.43 %) of the PBT for FY 2015-16.
41. Responding to this charge, the EP stated that determination of credit risk exposure as low, medium, or high is based on indicators as on the date of the balance sheet, past record etc. and professional judgement of the auditor. The EP further stated that he had compared the bad debts written off by the Company in the past five (5) years which was Nil in 2016-17; Rs.28 Crores in 2015-16; Rs.5.33 Crores in 2014-15, and Nil in 2013-14; and formed the opinion regarding low credit risk on the basis of evaluation of historical data of last 5 years. The EP also mentioned that merely a rise in the write-off in the previous year, 2015-16 shall not in any way warrant determination of the exposure to be higher. The EP also stated that low risk was borne out by the bad debts written off in the subsequent years (2017-18: Rs.1.49 Crores; 2018-19- NIL; 2019-20-Rs. 8.93 Crores) and by the fact that during FY 2016-17, the Non-Current Trade Receivables was at the same level (Rs.17.65 Crores to Rs.17.75 Crores) even though the total Trade Receivables had increased by 30% from Rs. 263 Crores in 2015-16 to Rs. 341 Crores in 2016-17.
42. The EP stated that the Trade Receivables of Rs.341 Crores as on 31.03.2017, consisted of Secured Trade Receivables of Rs.172 Crores (50.4%), and Unsecured Trade Receivables of Rs.169 Crores (49.6%), out of which Rs.121 Crores (72%) were from one major customer, Tecnimont, from which there was regular inflow and at the time of closure of the Audit File, only Rs. 42 Crores was outstanding against Tecnimont. Of the remaining amount of Rs. 48 Crores of Unsecured Trade Receivables, disputed Trade Receivables amounted to Rs.17 Crores (5% of the total Trade Receivables as on 31.03.2017), which was not material. The EP also stated that he had obtained Management Representation Letter dated 30.05.2017, which stated that there was strong chance of recoverability of the total Trade Receivables including the disputed ones.
43. The EP reiterated the position during the personal hearing adding that the unsecured Trade Receivables accounting for over 49% of the total outstandings balances were within the ageing bucket of 6-8 months; that there was no previous outstanding and that the recovery was regular and some of it was recovered during the audit. Based on this, the EP stated that he had identified the credit risk as low; and that most of the transactions were with foreign customers with Tecnimont being the major debtor. He, however admitted that this analysis and judgment is not documented in the Audit File.
44. We observe that there is no evidence in the Audit File of the Letter of Credit stated as security for the secured Trade Receivables. There is no evidence of receipts from M/s. Tecnimont after 31.03.2017 and no ageing analysis of the Trade Receivables performed by the EP. In the absence of such evidence, the reply of the EP seems an afterthought and is

not acceptable. It is evident that the EP's conclusion about the credit risk being low was not based on sound documented analysis. In light of the above, we find that the EP was negligent in not reporting the non-disclosure of trade receivables in accordance with Para 35M and 35N of Ind AS 107, not obtaining external confirmation as per SA 505 and not exercising due care in the audit of Trade Receivables.

C4. Failure to plan the audit of Financial Statements

45. The EP was charged with non-compliance with Para 6, 8 and 11 of SA 300 which require the auditor to establish an overall audit strategy that guides the development of the audit plan and not documenting the audit strategy and any changes made thereto during the engagement, on the basis that there was no evidence in the Audit File of performance of these activities.
46. Responding to the charge, the EP referred to documentation such as preliminary audit requirement list¹⁷, engagement letter¹⁸, audit programme¹⁹, CARO and Ind AS checklist²⁰ which purportedly include a description of nature and extent of planned risk assessment procedures carried out and audit procedures executed so that the engagement complies with the SAs.
47. We observed the following deficiencies (Table 7) in Audit Work Papers referred to by EP in reply to charge on failure to plan the audit of Financial Statements:

Table 7

S.No.	Working Paper No	Particulars	Observations
I.	Working paper at Page 11 to 14 of Audit Paper Book	Working Paper regarding preliminary audit requirement list	As mentioned in preceding paras, this work paper has been either tampered with or created as an afterthought subsequent to the issuance of SCN by NFRA. Notwithstanding the doubt regarding genuineness of this work paper, nowhere in the Audit File the status of information sought and obtained is recorded. The working paper was signed by the EP and EQCR partner, however, no date is mentioned on such work paper casting doubt on its integrity.
II.	Working Paper at Page 4 to 10 of Audit Paper Book	Working Paper regarding Engagement Letter	The EP has mentioned that his responsibility is to report if the Financial Statements do not comply in any material respect with the Indian Accounting Standards prescribed in

¹⁷ Page 11 to 14 of Audit Paper Book

¹⁸ Page 4 to 10 of Audit Paper Book

¹⁹ Page 15 to 27 of Audit Paper Book

²⁰ Page 28 to 41 of Audit Paper Book

			the new Companies Act, 2013 and Companies (Accounting Standards) Rules, 2006. It is to be noted that the Companies (Accounting Standards) Rules, 2006 was no longer applicable to MIIL but the Companies (Indian Accounting Standards) Rules, 2015 (Ind AS Rules) was applicable to MIIL. This shows EP's ignorance of the applicable standards and the related statutory requirements. Further, the working paper was signed by the EP and EQCR partner, however, no date is mentioned on such work paper casting doubt on its integrity.
III.	Working Paper at Page 28 to 41 of Audit Paper Book	Working Paper regarding CARO and Ind AS checklist	It is observed from the check list of Ind AS signed by EP that the Ind AS 101 ²¹ is shown as not applicable to the Company which is incorrect as the Company was required to and has reportedly adopted the Ind ASs from the FY 2016-17 under audit by the EP. This shows ignorance of the EP regarding applicable financial reporting framework, the relevant standards and the related statutory requirements. Further, the working paper was signed by the EP and EQCR partner, however, no date is mentioned on such work paper casting doubt on its integrity.

48. The above not only reflect the EP's lack of competence to perform audit of public interest entities, but his failure to identify and evaluate events or circumstances that may adversely affect the auditor's ability to plan and perform the audit engagement as per SA 300. We, therefore, conclude that the explanations given by the EP fail to establish compliance with SA 300.

49. Failure to make an appropriate audit plan has been viewed seriously by other regulators as well. For example, PCAOB, the US Regulator, charged L.L. Bradford & Company, LLC (the "Firm") for its failure to develop an appropriate audit plan for the audit of WebXU Inc.'s ("WebXU") and concluded that the *"the Firm violated PCAOB rules and auditing standards with respect to an audit and a quarterly review of one issuer audit client. Specifically, the Firm in conducting its audit of the financial statements of WebXU for the*

²¹ Indian Accounting Standard (Ind AS) 101, *First-time Adoption of Indian Accounting Standards*

year ended December 31, 2011, failed to properly assess the risks of material misstatement. As a result, the Firm failed to properly identify significant risks in connection with the 2011 WebXU audit. The Firm also failed to properly establish an overall strategy for the audit and develop an audit plan that included planned risk assessment procedures and planned responses to the risks of material misstatement. In addition, the Firm failed to perform sufficient audit procedures that addressed the risks of material misstatement." PCAOB for this misconduct among others, censured the Firm, revoked its registration permanently, and imposed a civil money penalty of \$12,500 upon the firm.

C5. Failure to perform Analytical Procedures

50. The EP was charged with failure to comply with Para 3(b) and Para 6 of SA 520 which require the auditor to design and perform analytical procedures to assist the auditor in overall conclusion of the audit as to whether the financial statements are consistent with the auditor's understanding of the entity. The SCN noted that there was substantial decrease in key financial parameters vis-a-vis the previous financial year; revenue from operations decreased by 23.80 % (from Rs. 1391.68 Crore in FY 2015-2016 to Rs. 1060.49 Crore in 2016-2017) and profit before tax decreased by 53.27 % (from Rs. 92.86 Crore in FY 2015-2016 to Rs. 43.39 Crore in 2016-2017). Further, the Company had written off substantial Rs. 28.12 Crore of Trade Receivables as bad debts in the previous FY 2015- 2016, compared to no write off for the year 2016-2017, which appears unusual in view of the fact that substantial amount (Rs 17.00 crore) of Trade Receivables were under litigation and a significant part (49%) of outstanding balances was unsecured.
51. In response, the EP submitted that he relied on management representation stating strong recoverability of the Trade Receivables in the year under consideration²² and has referred to the final audit discussion letter wherein he had raised concern regarding non-provisioning for expected credit loss on Trade Receivables but after satisfactory reply of the Company and applying professional judgement, had concluded that no provision for write-off of Trade Receivables was required to be made²³.
52. We observe the following deficiencies (Table 8) in the work papers referred to by EP in his reply to the charge regarding non-performance of Analytical Procedures:

Table 8

S.No.	Working Paper No	Particulars	Observations
I.	Working Paper - Para 8 @ Page 86 of the Audit Paper Book)	Management Representation Letter	No analytical procedure performed by the EP. The EP referred to Management Representation Letter of MIIL 2016-17 placed in Audit File where no analysis, judgement/conclusion is done or documented by the EP. There are no reasons

²² Para 8 @ Page 86 of the Audit Paper Book

²³ Para 5 @ Page 43 of the Audit Paper Book

			recorded by the EP regarding substantial decrease of revenue from operations by 23.80 % and profit before tax by 53.27 %.
II.	Working Paper - Para 5 @ Page 43 of the Audit Paper Book	Working Paper regarding final audit points identified by the EP and discussed with the EQCR Partner	Working paper was signed by the EP and EQCR partner, however, no date is mentioned on such work paper. There is no proof that discussion took place with EQCR partner and clearance given by EQCR partner on or before the date of the auditor's report. No analytical procedure performed by the EP.

53. The Audit Working Papers referred to by the EP nowhere establish that the EP has raised queries to the management or had discussions with them regarding the substantial changes in figures in FY 2017 from FY 2016 as shown in Table 9 below.

Table 9

Item	2016 (Rs. crores)	2017 (Rs. crores)	% Change
ASSETS			
NON-CURRENT ASSETS			
Capital work-in-progress	18.89	5.28	-72.05
Other non-current assets	11.18	8.08	-27.73
CURRENT ASSETS			
Inventories	127.51	108.91	-14.59
Trade receivables	246.17	323.64	31.47
Cash and cash equivalents	148.73	118.25	-20.49
Bank balances other than above	18.77	36.20	92.86
Loans	130.93	174.36	33.17
Other current assets	63.69	107.83	69.30
LIABILITIES:			
NON-CURRENT LIABILITIES			
Borrowings	190.49	131.33	-31.06
CURRENT LIABILITIES			
Borrowings	76.66	225.41	194.04
Other financial liabilities	95.96	120.54	25.61
Other current liabilities	41.96	19.23	-54.17

54. In view of above, it is evident that the Audit File does not evidence any analytical procedures performed, which proves that the EP failed to design and perform analytical procedures and enquire with the management regarding fluctuations in the figures from previous FY. We, therefore, conclude the EP has violated Para 3(b) and Para 6 of SA 520.

C6. Failure to determine Materiality

55. The EP was charged for failure to comply with Para 10 and 14 of SA 320, which requires an auditor to determine materiality for the Financial Statements as a whole while establishing the overall audit strategy and document the amounts and the factors considered in his determination of materiality for the Financial Statement as a whole and for performance materiality.
56. Responding to the charge, the EP responded that “.... *nothing has been set out in the SCN or let alone proved to indicate that alleged misstatements have significantly impacted the usability of financial statements. It is submitted that materiality for the audit of financial statements as a whole had been determined, to form a true and fair opinion on the same*”.
57. According to Para 10 of SA 320, when establishing the overall audit strategy, auditor **shall** determine the ‘Materiality’ for the Financial Statements as a whole. In addition, Para 11 of SA 320 states that the auditor shall determine ‘Performance Materiality’ for the purposes of assessing the risks of material misstatement and determining the nature, timing and extent of further audit procedures.
58. Para A2–A6 of SA 320 provides application material. Para A2 states that a percentage is often applied as a starting point in determining materiality for the Financial Statements as a whole and gives factors that affect the appropriate benchmark such as elements of the Financial Statements (e.g., assets, liabilities, equity, revenue, expenses). Para A6 provides more specific guidance that the auditor may consider five percent of PBT from continuing operations to be appropriate for a profit-oriented entity in a manufacturing industry and one percent of total revenue or total expenses to be appropriate for a not-for-profit entity. Also, the thematic review of Financial Reporting Council, UK²⁴ mentions Profit Before Tax (PBT), Adjusted PBT, Average PBT, Total Revenue and Total Equity as the commonly observed benchmarks for determining materiality and reports 3 to 10% and 0.5 to 2% of the PBT, Total Revenue/Total Assets, respectively, as the commonly observed percentages used in the audit of public interest audits.
59. The use of the expression ‘**Shall**’ in Paras 10 and 11 of SA 320, as well as the pronouncement of ICAI, make it clear that the requirements part of the SAs are mandatory. The following quote from the Handbook of Auditing Pronouncements issued by the Council of Institute of Chartered Accountants of India or ICAI²⁵ about the new format of SA applicable from 1st April 2008²⁶ are relevant:

“III. Members may also note that recently, the Council of the Institute of Chartered Accountants of India has approved the Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services. The said Preface introduces a totally new format of writing Standards, in line with that adopted by the International Auditing and Assurance

²⁴ Audit Quality Thematic Review Materiality December 2013, FRC UK

²⁵ Section I of the Handbook of the Auditing Pronouncements issued by Audit and Assurance Standards Board of the ICAI (2019)

²⁶ Page 5 of Handbook of the Auditing Pronouncements issued Audit and Assurance Standards Board of the ICAI (2019)

Standards Board pursuant to its Clarity Project. According to the new format the Standards on Auditing (SAs) would now contain two distinct sections, one, the Requirements section and, two, the Application Guidance section.

IV. The fundamental principles of the Standard are contained in the Requirements section and represented by use of “shall”. Hitherto, the word, “should” was used in the Standards, for this purpose. ...”

60. The EP’s assertion that nothing has been set out to indicate or prove that alleged misstatements have significantly impacted the usability of Financial Statements is false and misleading. Examination of the Audit File revealed that EP did not even determine materiality or performance materiality in the audit of Financial Statements of MIIL. As brought out in this Order, non-consolidation of a material subsidiary (para 18-21 of this Order), failure to report non-disclosure of Related Party loans on gross basis (para 84-86 of this Order), failure to report non-disclosure of Trade Payable under MSME Act (para 87-90 of this Order) and failure to report full particulars of RPTs (para 91-93 of this Order) constitutes material misstatements impacting the Financial Statements materially and pervasively. The stand of the EP that such misstatements have not impacted the Financial Statements cannot be accepted. We emphasise that materiality is one of the most important concepts in the audit of Financial Statements. Where material information is omitted or misstated, the Financial Statements will not be in compliance with the requirements of the SAs and therefore of the Law as Section 143(9) of the Companies Act, 2013 requires the auditors to comply with the SAs.

61. As there is no working paper in the Audit File evidencing determination of materiality by the EP, we conclude that the EP has failed to adhere to the mandatory requirements of determining Materiality in accordance with SA 320 and falsely stated in his report that he had conducted the audit in accordance with the SAs specified under Section 143(10) of the Act.

C7. Failure to perform risk assessment procedures and response to such risks

62. The EP was charged with failure to comply with Para 5, 6 and 11 of SA 315²⁷ which require that the auditor shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement (RoMM) at the financial statement and assertion levels. It also requires the auditor to obtain an understanding of the entity and its environment. Further, the EP was charged with failure to comply with Para 1, 5 and 6 of SA 330²⁸ which require the auditor to design and implement overall responses to the RoMM identified and assessed during audit.

63. Responding to the charge, the EP has simply mentioned the objectives of SA 315 and SA 330 without providing evidence of any work having been performed. Further, the EP has stated that he has performed necessary risk assessment procedures in identifying the RoMM

²⁷ Standard on Auditing (SA) 315, Identifying and assessing the Risk of Material Misstatement through understanding the Entity and its Environment

²⁸ Standard on Auditing (SA) 330, The Auditor’s responses to Assessed Risk

due to fraud or error and there are no material misstatements in the Financial Statements. The EP submitted that he has given qualified opinion to make the users of the Financial Statements aware of non-consolidation, that he has performed necessary risk assessment procedures and that there are no material misstatements in the Financial Statements. The EP has also stated that he has maintained adequate audit documentation to show that he has performed risk assessment procedure for material misstatement.

64. We observe that there is no evidence in the Audit File to show that any risk assessment procedures have been performed by the EP. Also, the EP's reply does not refer to any work paper where he has performed risk assessment procedures for material misstatements at the Financial Statement and Assertion levels and his audit responses to such risks etc.
65. As per Para 5 of SA 315, the auditor is required to perform risk assessment procedures at the Financial Statement and Assertion levels. Assertions generally used by the auditor to consider the different types of potential misstatements that may occur are shown in the Table 10 below:

Table 10

Assertions used by the Auditor to consider different types of material misstatements. (Refer to Para A110-113 of SA 315 for more details)			
Assertions	Material Misstatement Categories		
	Class of Transactions/Events during the audit period	Account balances at the period end	Presentation and Disclosure
Occurrence	√	-	√
Completeness	√	√	√
Accuracy	√	-	-
Cut-off	√	-	-
Classification	√	-	-
Existence	-	√	-
Rights and obligations	-	√	-
Valuation and allocation	-	√	-
Classification and understandability	-	-	√
Accuracy and valuation	-	-	√

66. Para 11 (c) of SA 315 states that *“The auditor shall evaluate whether the entity’s accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry. (Ref: Para. A34)”*. It is observed from the Audit File and the reply submitted, that the EP has failed to identify and document the applicable financial reporting framework where he is found wanting with non-identification of Ind AS 101, an Ind AS having most critical impact on the financial statements for the year ending 31.03.2017 under investigation. We have noted a number of errors in the financial statements and non-compliances of Ind ASs by the Company, which the EP has failed to identify and appropriately modify his audit report. As

a result, there are a number of fundamental fatal lapses in the audit work which render the audit of financial statements for FY 2016-17 unreliable.

Audit of Internal Financial Control Over Financial Reporting (Clause (i) of sub-section 3 of Section 143 of the Companies Act, 2013 (the “Act”))

67. The EP has expressed unmodified opinion on the adequacy and operating effectiveness of Internal Financial Controls Over Financial Reporting (IFCoFR) as at March 31, 2017. The Auditor’s opinion further states that they have conducted audit in accordance with the Guidance Note on Audit of IFCoFR (the "Guidance Note") and the Standards on Auditing deemed to be prescribed under Section 143(10) of the Act to the extent applicable to an audit of internal financial controls.
68. Para 16 of Section II of the Guidance Note states that a benchmark system of internal control, based on suitable criteria, is essential to enable the management and auditors to assess and state adequacy and compliance of the system of internal control. Para 17 of the Guidance Note mentions that the requirements in Appendix 1 of SA 315 provide necessary criteria for IFCoFR.
69. Section IV of the Guidance Note prescribes technical guidance on audit of IFCoFR. Some of the critical prescriptions are:
 - 69.1 While the auditor should combine the audit of IFCoFR and the audit of Financial Statements, the objectives of the audits are not identical. However, the auditor must plan and perform the work to achieve the objectives of both audits.
 - 69.2 The auditor should design his or her testing of controls to accomplish the objectives of both audits simultaneously:
 - 69.2.1 To obtain sufficient evidence to support the auditor's opinion on IFCoFR as of year-end, and
 - 69.2.2 To obtain SAAE to support the auditor's control risk assessments for the purposes of the audit of Financial Statements.
 - 69.3 Planning the audit, role of risk assessment, addressing the risk of fraud, materiality, identifying entity-level controls, identifying significant accounts and disclosures and their relevant assertions., testing controls-testing operating effectiveness, forming an opinion.
 - 69.4 Audit Documentation: It requires that the auditor should comply with the requirements of SA 230, Audit Documentation to the extent applicable.
70. In respect of the audit work relating to IFCoFR, there is no evidence at all except for a copy of the unsigned and unauthenticated copy of a document titled “Policies & Procedures on Internal Financial Control”²⁹. Further, as elaborated in para 62 to 64, the EP has not performed any work relating to SA 315 which is the benchmark to be used by the management and auditors to assess and state adequacy and compliance of the system of internal control. Further, as elaborated in para 47, the audit programmes used in the audit of Financial Statements are significantly deficient and do not provide any

²⁹Ref: Page 1532 to 1543 of Audit File 4

information about nature of tests performed i.e., test of controls and the timing of those tests etc. Also, there is no documentation of the results of the test of controls performed, based upon which the adequacy and operating effectiveness of the IFCoFR has been concluded.

71. In the absence of any evidence of the audit work performed by the EP in respect of IFCoFR, the unmodified audit opinion issued by them is without any basis. As can be seen from preceding paras, the EP is found to have been grossly negligent in his professional duties and has failed to obtain SAAE, thereby violating SA 200 and the Guidance Note.
72. In light of the above facts and circumstances, we conclude that the EP has been grossly negligent in the conduct of his professional duties and made false declaration in the audit report of the true and fair view of the Financial Statements, and failed to comply with the requirements of SA 315 and 330 to:
 - (a) Identify and assess the risks of material misstatement through understanding the entity and its environment, including the entity's internal control.
 - (b) Exercise professional scepticism, professional competence and due care.
 - (c) Document significant matters arising during the audit, the conclusions reached thereon, and significant professional judgements made in reaching those conclusions.

C8. Failure to obtain Sufficient Appropriate Audit Evidence (SAAE)

73. The EP was charged with failure to comply with SA 200³⁰ as he did not obtain reasonable assurance whether the Financial Statements were free from material misstatements and failed to obtain sufficient appropriate audit evidence.
74. Responding to the charge, the EP submitted that the charge does not survive on account of the submissions made by him hence, the allegation of failure to obtain reasonable assurance that the financial statements were free from material misstatement is incorrect.
75. The response of the EP which is casual is not acceptable. As we discussed in this Order, the EP failed to obtain SAAE to support his assurance that the Financial Statements were free from material misstatements in the following critical areas of audit:
 - (i) Non-consolidation of a material subsidiary (Para 18-21),
 - (ii) Credit risk evaluation of Trade Receivables (Para 40-44) and
 - (iii) Failure to perform risk assessment procedures and response to such risks (Para 62-72)

The EP during the personal hearing held on 21.09.2023 admitted that he had not kept in the Audit File a copy of stay order granted by Hon. Bombay High Court regarding Scheme of Arrangement as explained in para 19 and 20 of this Order. The EP also admitted that instead of a qualified opinion, he should have given an adverse opinion in

³⁰ SA 200 Overall objectives of the Independence Auditor and the Conduct of an Audit in accordance with Standards on Auditing

view of the material and pervasive effect of non-consolidation. The EP has also not documented in the Audit File the analysis and judgement regarding credit risk of Trade Receivables and need for impairment loss, if any. Further, performing risk assessment by understanding the entity and its internal control requires obtaining extensive audit evidence. However, as mentioned at para 64 of this Order, there is no evidence at all of work done in this fundamental audit area. In the light of the EP's failure to adhere to the requirements of SAs and failure to report non-compliance of Ind AS and Companies Act, 2013 provisions, we, conclude that the EP has been grossly negligent in his professional duties and has failed to obtain SAAE in critical areas of audit mentioned above, thereby violating SA 200.

C9. Failure to prepare documentation regarding Auditor's responsibilities relating to fraud in an Audit of Financial Statements

76. The EP was charged with failure to comply with the requirements of Para 16 and 24 of SA 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements.
77. Responding to the charge, the EP submitted that necessary inquiries with the management were made and as per the information and explanation given by the management no fraud on or by the Company was noticed during the period of audit. The EP referred to clause 3(x) of CARO 2020 and reported that, *"Based upon the audit procedure performed for the purpose of reporting the true and fair view of the financial statements and as per the information and explanation given by the management, we report that no fraud by the company or on the company by the Company or on the company by its officers or employees has been noticed or reported during the period covered by our audit."*
78. We observe that there is no evidence in the Audit File that the EP had identified and assessed the risks of material misstatement to comply with the requirements of Para 16 of SA 240 where Auditor is required to perform the procedures as mentioned in Paragraphs 17 to 24 of SA 240, to obtain information for use in identifying the risks of material misstatement due to fraud. Further, the EP failed to evaluate whether the information obtained from other risk assessment procedures and related activities performed indicates that one or more fraud risk factors are present and therefore did not comply with Para 24 of SA 240. We also observe that it is nowhere documented in the Audit File whether EP had inquired from the company's staff in respect of internal control processes or observed the staff performing the controls. The reply is an afterthought to mislead NFRA and hide his deficiencies in conduct of audit. In the light of above, we conclude that the EP failed to comply with the requirements of Para 16 and 24 of SA 240.

C10. Failure to communicate with Those Charged with Governance (TCWG)

79. The EP was charged with failure to determine TCWG and communicate with TCWG about the responsibilities as an auditor, overview of planned scope, timing of the audit and deficiencies in Internal Control etc. The EP was also required to maintain audit documentations of such communication with TCWG. The SCN noted that the examination of Audit File revealed that there is no documentation indicating that there was any communication with TCWG. Thus, the EP did not exercise due diligence and

was grossly negligent in not communicating with TCWG and, therefore, failed to comply with the requirements of SA 260³¹ and SA 265³².

80. Responding to the charge, the EP submitted that he had maintained an Audit Engagement Letter³³ which confirms the acceptance of the audit besides the planned scope, statutory and professional duties; that the Audit Engagement Letter had been signed by the auditee thereby promoting two-way communication; that as per the discussion with TCWG, valuation report was obtained for impairment testing of investments of Rs 10,229.83 Lakhs in MSPL. However, the EP admits that while there is no documentation for every communication with the TCWG, every material item pertaining to the financial statements was discussed with the management and TCWG via meetings and decisions were made accordingly.
81. We observe that the EP failed to identify TCWG and failed to understand the importance of TCWG as a body that has the responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity which includes overseeing the Financial Reporting process. It is pertinent to mention that impairment testing of investment of MSPL was a significant matter. However, the EP submitted that he had discussed the same with the management and TCWG and obtained a valuation report. There is no evidence in the Audit File of his discussion with TCWG in support of this assertion. Para 19 of SA 260 states that the Auditor shall communicate in writing with TCWG regarding significant findings from the audit if, in the auditor's professional judgement, oral communication would not be adequate. Further, Para 23 of SA 260 states that, where matters required by this SA to be communicated are communicated orally, the auditor **shall** include them in the audit documentation, which the EP failed to do so. Further, Para 9 of SA 265, requires that the auditor **shall** communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis for which there is no evidence in the Audit File.
82. In the light of above, we conclude that the EP has failed to exercise due diligence and was grossly negligent in not identifying and communicating with TCWG and consequently, failed to comply with the requirements of SA 260 and SA 265.
83. Failure to appropriately communicate with Audit Committee (which is a part of the TCWG) has been viewed seriously by international regulators too. For example, PCAOB, the US Regulator, charged the public accounting firm L.L. Bradford & Company, LLC (Audit Firm) for its failure to communicate with the audit committee during the audit of WebXU Inc.'s ("WebXU") and noted that the *"Firm also violated a PCAOB rule that requires a registered public accounting firm to communicate, in writing, to the audit committee"* The PCAOB, for this misconduct among others, censured the Firm, revoked its registration, and imposed a civil money penalty of \$12500.

³¹ Standard on Auditing (SA) 260: Communication with Those Charged with Governance (Para 15,11,14,16 & 23)

³² Standard on Auditing (SA) 265: Communicating Deficiencies in Internal Control to Those Charged with Governance and Management

³³ Page 04 to 10 of Audit Paper Book

D. Other Lapses in Audit

D1. Failure to report non-disclosure of Related Party Loans on gross basis

84. The Company in its Annual Report for 2016-2017 has disclosed loan to subsidiary and its receipt on net basis. Para 18 of Ind AS 24 requires an entity to disclose the amount of the transactions entered into with a related party. The EP was charged with failure to comply with Para 15 & Para 25 of SA 550 by not reporting such non-disclosure as per Ind AS 24 which rendered the financial statements misleading.
85. Responding to the charge, the EP submitted that there is no requirement that the amount of loan transactions must be disclosed on gross basis; that Para 18 of Ind AS 24 only states that the entity shall disclose the amount of transactions entered in the relevant FY and the outstanding balances at the year end with related parties. The EP cited example of related parties shown on net basis in disclosure of other entities and stated that the allegation of non-compliance with SA 550 does not sustain.
86. We observe that the EP's understanding is erroneous. The objective and purpose of Ind AS 24 is to ensure that an entity's Financial Statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties. A combined reading of various prescriptions of Ind AS 24 in Para 18, Para 20, Para 21 and Para 24, shows that they require the entities to disclose Related Party Transactions (RPT) on gross basis, since the overarching objective of Ind AS 24 is to disclose information that is relevant to understand the effect on financial position as well as profit or loss of the entity. For example, outstanding receivables and payables to a related party, though arising from transactions in earlier years would affect the financial position or nature of its assets and liabilities. Further, disclosure of RPTs on a net basis would obscure the extent (volume) of quantitative effect of RPTs on the financial performance and cash flows of the entity, if they have been squared off or netted before the year end. We find that the EP has erred by failing to exercise due professional care by not reporting such non-disclosure.

D2. Failure to report non-disclosure of Trade Payable covered under the Micro, Small and Medium Enterprises Development Act, 2006

87. The EP was charged with failure to report the non-disclosure of the amount of principal and interest outstanding as required under the Micro, Small and Medium Enterprises Development Act, 2006 during the year as per Schedule III of the Companies Act, 2013. As per the Annual Report of the Company for 2016-2017, there is no disclosure of information required to be disclosed under the Micro, Small and Medium Enterprises Development Act, 2006 to the extent such parties have been identified and amount of principal and interest outstanding during the year as per Schedule III of the Companies Act, 2013.
88. Responding to the charge, the EP submitted that queries were raised to TCWG regarding the same and the management vide their representation letter intimated that such non-disclosure was on account of non-identification of suppliers³⁴. The EP referred to the notes

³⁴ Ref: Para 24 @ Page 92 of Audit Paper Book

to account no. 48(i) contained in the SFS, wherein it has been expressly disclosed that the Company had not initiated the process of identifying 'suppliers' covered under the MSME Act and hence such disclosure had not been made. In view of the above, the EP stated that no further reporting was required to be made.

89. The disclosure of information related to MSMEs is an important aspect of corporate reporting. If a Company has not made adequate disclosure related to MSMEs, it is considered a material non-compliance and can have implications for the Financial Statements and the audit report. The auditor in such situation is required to assess the materiality of the missing disclosure and evaluate the impact it has on the Financial Statements. If the auditor determines that the missing disclosure is material, they will need to modify their audit opinion to reflect this. The auditor may also need to perform additional procedures to gather evidence to support the modified audit opinion. Auditors play a critical role in ensuring that the Financial Statements are fairly presented and that any material non-compliances are identified and addressed.
90. In his audit report, the EP has failed to address the non-disclosure in respect of MSME and explain its impact on the Financial Statements. The EP also failed to state his opinion on the Financial Statements, taking into account the inappropriate disclosure. In view of this, we conclude that the EP failed to report the non-disclosure of the amount of principal and interest outstanding as required under the Micro, Small and Medium Enterprises Development Act, 2006 during the year as per Schedule III of the Companies Act, 2013.

D3. Failure to report full particulars of loan to Related Party

91. The EP was charged with failure to report the non-disclosure of the rationale and purpose of loan transactions as per Section 186(4) of the Companies Act, 2013. The annual report of the Company for 2016-2017 showed loan to MSPL amounting to Rs. 50.01 crores. However, there is no disclosure as per Section 186 (4) of the Companies Act, 2013 and Schedule V of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, which require a Company to disclose in the Financial Statements the full particulars of loans, and the purpose for which a loan is proposed and its utilisation.
92. Responding to the charge, the EP submitted that non-disclosure of rationale and purpose of loan transactions in compliance with Section 186 (4) of the Act is on account of MIIL enjoying the exception under Section 186(11) of the Companies Act, being a company involved in infrastructural facilities and therefore, there was no violation as alleged. The EP stated that the management vide its letter dated May 30, 2017 had given a confirmation that they have not contravened any provisions of the Companies Act, 2013³⁵.
93. The company is absolved from disclosure requirements of Section 186(4) provided it is a company exempted under Section 186(11) i.e., a company established under the object of and engaged in the business of providing infrastructural facilities. We have reviewed the provisions of Section 186(11) and related Schedule VI vis-a-vis the actual activities of MIIL and its main object clause in its Memorandum of Association and are of the opinion

³⁵ Ref: para 14(d) @page 87 and para 27 @ Page 93 of Audit Paper Book

that it is not explicitly clear whether MIIL is eligible for exemption under Section 186 (11) of the Act. Notwithstanding the above, there is no evidence of any comment/conclusion/judgement recorded in the Audit File that MIIL enjoys exemption as envisaged under Section 186(11) of the Act being a company involved in infrastructural facilities. Further, there is also no evidence to show that the EP discussed this issue with the management and TCWG. As Related Party Transactions are often prone to misuse, including diversion of funds and therefore a material area of audit and subject to stricter legal scrutiny, the EP was required to be more cautious and exercise professional skepticism in this sensitive area of audit. We, therefore, conclude that this is a clear case of afterthought, and the EP has failed in his attempt to cover up for his nonchalant attitude by not performing the duties of a statutory auditor of a PIE.

D4. Failure to report non-disclosure of Material Information relating to pledge of fixed deposits

94. The EP was charged with failure to report non-disclosure of material information in accordance with Para 14 of Ind AS 107 "Financial Instruments: Disclosures", wherein a lien created on the fixed deposits held by MIIL amounting to Rs. 83 crores for overdraft facility availed by MRL (related party of MIIL) was not disclosed in the Financial Statements of MIIL. The EP was charged that he had falsely reported that the Financial Statements comply with Ind AS, despite the violation of the requirements of Para 14 of Ind AS 107 in the audit report.
95. Responding to the charge, the EP stated that in compliance of SA 505, a letter dated 14.04.2017³⁶ was addressed by the Firm to the Dombivli Nagari Sahakari Bank (DNSB), Fort branch, Mumbai requesting the bank to confirm the outstanding balance, including details of fixed deposit along with any lien created on them as on 31.03.2017; that confirmation from DNSB regarding principal balances and accrued interest as on 31.03.2017 was received but the said letter did not convey the existence of any lien marked on such deposits³⁷; that the company had provided a letter dated 11.05.2017 to EP from DNSB which did not convey the existence of any lien marked on such deposits³⁸; and that the management representation letter dated 30.05.2017 that included details of contingent liabilities, did not state anything regarding lien of the fixed deposit³⁹. In addition, the EP states that not only the MRL but also the board minutes and audit committee minutes did not state anything with respect to the lien on fixed deposits with DNSB.⁴⁰ In the light of this, the EP submits that he cannot be held responsible when both external and internal audit evidence gathered reflected that there was no lien on the fixed deposit.
96. We have considered the reply of the EP. In view of the explanation and workpapers submitted by the EP, the charge is dropped.

³⁶ Ref: Page 357 of Audit Paper Book

³⁷ Ref: Page 359 of Audit Paper Book

³⁸ Ref: Page 358 of Audit Paper Book

³⁹ Ref: Para 15(c) Page 88 of Audit Paper Book

⁴⁰ Ref: Page 1624 to 1734 of Audit Paper Book

E. Articles of Charges of Professional Misconduct by the EP

97. As discussed in the paragraphs above, the EP has made significant departures from the standards and the Companies Act, 2013 in the conduct of the audit of MIIL for 2016-2017. Based on above discussion, we note that the EP has given an unmodified opinion in SFS and a qualified opinion on the CFS without obtaining SAAE. The poor quality of audit, incomplete documentation, attempt to mislead through tampering of the Audit File, and evasive replies establish that CA Nilesh Chheda committed professional misconduct, as defined defined in Section 132 (4) of the Companies Act, read with Section 22 the Chartered Accountants Act 1949 (the CA Act), as amended from time to time, and as detailed below:

- (i) CA Nilesh Chheda committed professional misconduct as defined in clause 5 of Part I of the Second Schedule of the CA Act which states that an EP is guilty of professional misconduct when he *“fails to disclose a material fact known to them 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”*.

This charge is proved as explained in para no. C.3, D.1 to D.3 above.

- (ii) CA Nilesh Chheda committed professional misconduct as defined in clause 7 of Part I of the Second Schedule of the CA Act, which states that an EP is guilty of professional misconduct when he, *“does not exercise due diligence, and being grossly negligent in the conduct of professional duties”*.

This charge is proved as explained in para no. C.1 to C.10 and D.1 to D.3 above.

- (iii) CA Nilesh Chheda committed professional misconduct as defined in clause 8 of Part I of the Second Schedule of the CA Act, which states that an EP is guilty of professional misconduct when he, *“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”*.

This charge is proved as explained in para no. C.1, C.3 to C.10 and D.1 to D.3 above.

- (iv) CA Nilesh Chheda committed professional misconduct as defined in clause 9 of Part I of the Second Schedule of the CA Act, which states that an EP is guilty of professional misconduct when he, *“fails to invite attention to material departure from the generally accepted procedures of audit applicable to the circumstances”*.

This charge is proved as explained in para no. C.1 to C.10 and D.1 to D.3 above.

F. PENALTY and SANCTIONS

98. Section 132(4) of the Companies Act, 2013 provides for penalties in a case where professional misconduct is proved. The seriousness with which proved cases of professional misconduct are viewed, is evident from the fact that a minimum punishment is laid down by the law.
99. Independent Auditors of Public Listed Companies serve a critical public function of enabling the users of Audited Financial Statements to take informed decisions.
100. In the absence of a robust system of auditing, investors, creditors, and other users of Financial Statements would be handicapped and their work compromised. The best of systems fails if the professionals implementing the system do not perform their job. This could lead to a serious failure of the financial system which could ultimately result in a breakdown in trust and confidence of investors and the public at large.
101. Thus, the Auditor is duty bound to examine and ascertain the integrity of Financial Statements of such entities⁴¹ in larger public interest. The Auditor's duty of exercising due diligence is owed to the users of the Financial Statements.
102. The Auditor in the present case was required to ensure compliance with SAs to achieve the necessary audit quality and lend credibility to Financial Statements to facilitate its users. As detailed in this order, substantial deficiencies in audit, abdication of responsibility, failure to act with due diligence and inappropriate conclusions on the part of CA Nilesh Chheda establish his professional misconduct. Despite being a qualified professional, CA Nilesh Chheda has not adhered to the Standards and has thus not discharged the duty cast upon him. Under the circumstances, we proceed to order the following sanctions keeping in mind deterrence, proportionality, and the signalling value of sanctions.
103. As per information, the statutory audit fee of MIIL for FY 2016-17 was Rs. [REDACTED] and fees towards other services (Certifications) received was Rs. [REDACTED]. CA Nilesh Chheda received remuneration of Rs. [REDACTED] and earned share of profit amounting to Rs. [REDACTED] for FY 2016-17.
104. Considering the fact that professional misconducts have been proved and considering nature of violations and principles of proportionalities, we in exercise of powers vested under Section 132(4) (c) of the Companies Act, 2013, order:
- (a) Imposition of monetary penalty of Rs.5,00,000 (Rupees Five Lakhs Only) upon CA Nilesh Chheda.

⁴¹ As defined in Rule 3 of NFRA Rules 2018

- (b) In addition, CA Nilesh Chheda is debarred for 5 (Five) years 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.

105. This order will become effective after 30 days from the date of its issue.

Signed
(Dr. Ajay Bhushan Prasad Pandey)
Chairperson

Signed
(Dr. Praveen Kumar Tiwari)
Full-Time Member

Signed
(Smita Jhingran)
Full-Time Member

Authorised for issue by the National Financial Reporting Authority,

Date: 22.11.2023
Place: New Delhi


(Vidhu Sood)
Secretary

To,

CA Nilesh Chheda,
ICAI Membership No.124810,
M/s Rohira Mehta & Associates, Chartered Accountants
(presently RMA & Co.),
Firm Registration Number - 118777W,
B-202 2nd Floor,
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Near Jari Mari Temple
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सचिव / Secretary
राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण
National Financial Reporting Authority
नई दिल्ली / New Delhi

Copy To: -

- (i) Secretary, Ministry of Corporate Affairs, Government of India, New Delhi.
- (ii) Securities and Exchange Board of India, Mumbai.
- (iii) Registrar of Companies, Mumbai.
- (iv) Secretary, Institute of Chartered Accountants of India, New Delhi.
- (v) M/s MAN Industries (India) Limited, Mumbai.
- (vi) IT Team, NFRA for uploading the order on the website of NFRA.