

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

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

NF-25013/2/2023

Dated 26.06.2023

Circular

To

1. Auditors of the Entities Regulated by the National Financial Reporting Authority (NFRA)

Subject: Statutory Auditors' Responsibilities in relation to Fraud in a Company

In course of discharge of its statutory functions, NFRA has noticed that auditors are not fulfilling their statutory responsibilities relating to reporting of fraud as mandated under the Companies Act, 2013 (CA 2013) read with the relevant Rules and the applicable Standards on Auditing (SAs).

2 The CA 2013, the Companies (Auditor's Report) Order (CARO) and the Standards on Auditing (SAs) place mandatory reporting obligations on auditors to report fraud and/or suspected fraud to the Central Government and the Board/Audit Committee.

2.1 Section 143 (12) of CA 2013 and related Rules places certain reporting obligations on the auditor, in relation to frauds:

"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 in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as may be prescribed:"

Rule 13 of the Companies (Audit and Auditors) Rules 2014, prescribes detailed steps that need to be followed by the auditor if he has **reason to believe** that an offence of fraud, which involves or is expected to involve individually an amount of rupees one crore or above, is being or has been committed against the company by its officers or employees. The auditor is required to report the matter to the Board or Audit Committee and to the Central Government in the form of a statement as specified in **Form ADT-4**.

2.2 Clause (xi) of Companies (Auditor's Report) Order, 2020¹ also requires auditors to make statements relating to reporting of fraud in his/her report.

2.3 Section 140 (5) of the CA 2013, contains consequences for auditors if they have acted, directly or indirectly, in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers. Under the section, the auditor shall also be liable for action under section 447 of CA 2013 apart from removal and debarment for a period of five years. In this regard, it is pertinent to note that the definition of fraud under section 447 of CA 2013 is wide and states that, "fraud" in relation to affairs of a company or anybody corporate, includes any act, omission,

¹ Additional matters to be reported in the Auditor's Report in terms of Order issued by the Central Government in exercise of powers u/s 143 (11) of the CA 2013.

concealment of any fact or abuse of position committed by **any person or any other person** with the connivance in any manner, with intent to deceive, to gain undue advantage from, or to injure the interests of, the company or its shareholders or its creditors or any other person, whether or not there is any wrongful gain or wrongful loss” (emphasis supplied).

2.4 SA 240²-The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements-elaborately deals with the auditor’s responsibilities relating to fraud in an audit of financial statements. The SA requires the auditor to maintain professional skepticism throughout the audit and states:

“12. In accordance with SA 200, the auditor shall maintain professional skepticism throughout the audit, recognizing the possibility that a material misstatement due to fraud could exist, notwithstanding the auditor’s past experience of the honesty and integrity of the entity’s management and those charged with governance.”

2.5 The guidance provided in paras A59-A66 of SA 240, details the Communications to Management, Those Charged with Governance (TCWG) and Regulatory and Enforcement Authorities regarding reporting of the fraud/suspected fraud.

3 There is a misconception amongst some Auditors that resigning from an audit engagement absolves them of their reporting obligations relating to fraud and the consequences under CA 2013 for nonreporting of fraud. In this regard, the Hon’ble Supreme Court of India in a recent judgment dated 03.05.2023 (Union of India and Another versus Deloitte Haskins and Sells LLP & Anr CRIMINAL APPEAL NOS.2305-2307 OF 2022), has held that the consequences of section 140 (5) of CA 2013 will be applicable also on those auditors who resign from the their audit engagements without reporting fraud/suspected fraud. The Hon’ble Apex Court observed:

“7.... Therefore, on true interpretation, even on resignation by an auditor of a company even during the enquiry/proceedings under section 140(5) or even prior to that, there shall not be any termination of the proceedings under section 140(5) as observed and held by the High Court. At the cost of repetition, it is observed that in a given case, an auditor, who in fact has, directly or indirectly, acted in a fraudulent manner, to avoid any further consequence under the second proviso to section 140(5), resigns to avoid any consequence under the second proviso to section 140(5), it cannot be permitted.

14...Acting in a fraudulent manner, directly or indirectly, by an auditor is a very serious misconduct and therefore the necessary consequence of indulging into such fraudulent act shall follow.”

4 In view of the foregoing, the provisions of the Act, the relevant rules and the Standards relating to reporting of fraud and its consequences are reiterated.

4.1 Statutory Auditors are under a mandatory obligation to report fraud or suspected fraud if they observe suspicious activities, transactions or operating circumstances in a company that indicate **reasons to believe** that an offence of fraud is being or has been committed against the company by its officers or employees. In such an event, the Statutory Auditor shall initiate the steps prescribed under Rule 13 of Companies (Audit and Auditors) Rules 2014 which begins with reporting the matter to the Board/Audit Committee within TWO days of his/her knowledge of the fraud.

² Standard on Auditing 240, *The Auditor’s Responsibilities Relating to Fraud* in an Audit of Financial Statements (SA 240)

In the case of reporting of a fraud involving or expected to involve *individually* an amount of rupees one crore or above, the Statutory Auditor fails to get any reply / observations from the Board/Audit Committee within 45 days, the Auditor shall forward a report in the specified form viz., ADT-4 to Secretary, Ministry of Corporate Affairs, Government of India.

4.2 The Statutory Auditor is duty bound to submit Form ADT-4 to the Central Government u/s 143 (12) even in cases where the Statutory Auditor is not the first person to identify the fraud/suspected fraud.

4.3 Resignation does not absolve the Auditor of his responsibility to report suspected fraud or fraud as mandated by the law.

4.4 The Statutory Auditor shall exercise his/her own professional skepticism while evaluating fraud, and need not be influenced by legal opinion provided by the Company or its Management.

5 This issues with the approval of the Executive Body, NFRA.



(Vidhu Sood)
Secretary

Copy to:

1. Secretary, Ministry of Corporate Affairs, Government of India
2. Director General of Corporate Affairs, Ministry of Corporate Affairs, Government of India
3. Governor, Reserve Bank of India
4. Chairperson, Securities and Exchange Board of India
5. Chairperson, Insurance Regulatory and Development Authority of India
6. Director General (Commercial-II), O/o CAG of India
7. President, The Institute of Chartered Accountants of India
8. President, The Institute of Company Secretaries of India
9. Director General, Confederation of Indian Industry (CII)
10. Director General, Federation of Indian Chamber of Commerce and Industry (FICCI)
11. Secretary General, The Associated Chambers of Commerce and Industry of India (ASSOCHAM)
12. Secretary General, PHD Chamber of Commerce and Industry (PHDCCI)
13. Director, The CFO Board

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