NFRA Order No. NF-20012/1/2020
22nd July, 2020

No NF-20012/1/2020
भारत सरकार / Government of India
राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण / National Financial Reporting Authority
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7th Floor, Hindustan Times House,
Kasturba Gandhi Marg, New Delhi
Dated: 22.07.2020

Important Note: In terms of the order passed by the Hon'ble Delhi High Court on 26th June, 2020, in C.M.No.13452/2020 *(directions)* in W.P.(C)1524/2020 this order shall not be given effect to till 31.07.2020

ORDER UNDER SECTION 132(4) OF THE COMPANIES ACT IN RESPECT OF THE SHOW CAUSE NOTICE ISSUED TO CA UDAYAN SEN (Membership No 31220)

A. BACKGROUND

1. A Show Cause Notice (SCN) was issued on 17th January 2020 to CA Udayan Sen (the CA) in terms of the powers vested in the National Financial Reporting Authority (**NFRA**) under Section 132(4) of the Companies Act, 2013, asking him to show cause as to why action should not be taken against him for professional misconduct in respect of his performance as Engagement Partner (**EP**) in the statutory audit of ILFS Financial Services Ltd (**IFIN**) for the year 2017-18.

2. CA Udayan Sen was required by the notice to submit his reply to the notice latest by 29th February 2020. However, instead of furnishing the reply, the CA filed a writ petition W.P. (C) No.1524/2020 before the Hon'ble High Court of Delhi on 7th February, 2020. The said petition, inter alia, challenges the vires of Section 132 (4) of the Companies Act, 2013, as also that of Rules 10 and 11 of the National Financial Reporting Authority Rules, 2018. The prayer before the Court was also to withdraw and/or cancel/set aside the SCN and to stay the proceedings initiated vide the SCN.

3. The court heard the WP on 10th February, 2020 and posted for the matter for further hearing on 12th March, 2020. Vide letter dated 14th February, 2020, the CA, through his advocate, informed NFRA that he would not be filing his reply to the SCN, and that NFRA should not proceed with the matter as the same was sub judice. After hearing the matter on 12th March, the Hon`ble Court granted time to the petitioners for filing rejoinder and adjourned the matter to 28th April. There was no stay granted on the proceedings initiated by the NFRA SCN.

4. As there was no stay granted by the Hon'ble High Court, NFRA, vide reminder letter dated 18th March, asked the CA to file his reply to the SCN within 7 days. The CA, through his advocate, vide letter dated 20th March, replied that he would not be filing his reply to the SCN in light of the

writ petition pending before the Hon'ble High Court, and other factors related to the COVID-19 situation.

5. On 28th April, the Hon'ble Delhi HC issued public notice of adjournment of all cases due to COVID 19 pandemic. Following this, vide letter dated 29th April, NFRA issued a reminder to the CA to file his reply latest by 10th May 2020, as more than three months had elapsed since the SCN was issued and there was no stay on the proceedings.

6. The CA moved an urgent application on 8th May before the Hon'ble High Court seeking directions to restrain NFRA from taking a decision pursuant to the reminder letters and SCN. The application was heard by the Hon'ble Court on 13th May. NFRA was allowed 3 weeks' time to file its reply. No stay, however, was granted in respect of the SCN even on this occasion.

7. On 13th May, NFRA issued another reminder letter to the CA, asking him to file his reply to the SCN via email latest by 20th May. An opportunity of oral hearing through video conferencing mode was also granted to the CA for 20th May, in line with Rule 11(5) of NFRA Rules 2018, though not specifically requested for by the CA.

8. The CA, through his advocate, vide letter dated 17th May, requested for time till 10th June for filing "interim/protem" reply to the SCN, and for postponement of hearing till the Hon'ble High Court decided the issues raised in the WP. The request of the CA was not accepted by NFRA due to the following reasons, communicated to him vide NFRA's letter dated 18th May:

    a. Considerable time had been already given to the CA to file his reply
    b. The Audit File submitted to NFRA is in electronic form in a laptop. Very few documents were provided in hardcopy form. The electronic audit file is accessible from anywhere around the world

    c. The Audit firm has signed 9 audit reports during the period from 20th April to 8th May 2020, as evident from the Bombay Stock Exchange filings, indicating that the firm was working and accessing documents even during COVID-19 lockdown period.

    d. No stay had been granted by the Hon'ble Delhi High Court and the CA is duty bound to reply to the SCN within the stipulated period.

    e. The statutory SCN issued cannot be ignored by the CA. The pending petition in the court does not, ipso facto, allow the CA to not reply to the SCN.

f. NFRA has been providing additional time to the CA ever since 29th February to present his point of view.

g. The sequence of events and all other facts went to show that the CA had tried to continuously delay the proceedings for no justifiable cause.

9. The urgent application filed by the CA in the Hon'ble Delhi High Court got listed on 20th May, and on that date got postponed to 21st May. The Application was disposed of by the Hon'ble High Court vide order dated 21.05.2020. The Court in their order directed/observed the following:

a. "Fresh applications listed today have been filed by the petitioners to restrain the respondents from taking a decision pursuant to the show cause notices issued to the petitioners, without the petitioners having an occasion to submit their reply and of being heard".

b. "Considering the facts, we are of the opinion that the petitioners file their replies to the show cause notices issued, latest by 10th June, 2020."

c. "The senior counsels for the petitioners state that owing to the lockdown still continuing in Mumbai, some of the documents contained in hard drive are not likely to be available to the petitioners even by 10th June, 2020. It is stated that thus the replies filed by the petitioners by 10th June, 2020 would be interim replies only."

d. "The counsel for UOI controverts and states that the show cause notices were issued long back and the petitioners have already caused much delay and further time to file replies that too interim replies, is being sought to cause further delay."

e. "Without knowing the nature of the documents which the petitioners claim to be not available to them, **no permission to file only interim replies to the show cause notices, as sought can be given. The petitioners to, in the replies to be filed by them by 10th June, 2020, set out the documents which are not available and the effect thereof and it will be upto the person/authority considering the said reply for adjudicating the show cause notices, to consider whether the petitioners are entitled to further time to produce the documents which are not available or to an opportunity to file a further reply**."

f. "These petitions are already listed for hearing before this Court on 27th June, 2020. If pursuant to the replies to the show cause notices to be filed by the petitioners by 10th June,

2020, any orders are passed before 27th June, 2020 in pursuance to the show cause notices, the said orders be not given effect to till 27th June, 2020 at least".

g. "It is further clarified that the hearing, if any granted to the petitioners on the show cause notices issued, would be without prejudice to the respective contentions".

(Emphasis supplied)

10. In view of the oral observations made by the Hon'ble High Court during hearing on 20th May, not to conclude the proceedings on that date, NFRA adjourned the oral hearing proceedings on 20th May. Vide letter dated 27th May, NFRA intimated the CA of the date of 11th June 2020 for the resumed oral hearing. As directed by the Hon'ble High Court in their order dated 21st May, the last date for filing written reply had been fixed as 10th June 2020.

11. CA Udayan Sen submitted his reply vide a series of Emails starting from the first email Dated, Thursday, 11 June 2020, 2:31 AM, and 8 subsequent emails on the same date, due to the big attachment size. The emails have 10 attached documents in PDF format. An oral hearing was conducted on 11th June 2020 through video conferencing. The written record of the matters presented by the CA during oral hearing was submitted by him vide email dated, Saturday, 13 June 2020 10:17 PM having one attached document.

12. The reply filed by the CA has been titled as "interim /pro tem reply". It is also stated in the reply that "the Hon'ble Delhi High Court, however, has kept the issue of my right to file a supplemental reply open by granting the discretion to the person/authority considering the interim reply to be filed by me on 10th June, 2020." In this regard NFRA notes the following:

a. As per the direction of the Hon'ble High Court (see para 9(e) above) the CA had to set out in his reply the documents which are not available and the effect thereof in order to enable NFRA to consider whether the CA was entitled to further time to produce the documents which are not available or to an opportunity to file a further reply.

b. Based on the above submissions NFRA had to take an appropriate decision in the matter of submission of further replies, as had been made clear by the court.

c. NFRA has gone through the reply in detail and notes that certain exhibits mentioned in his reply are said to be not submitted and are mentioned by him as "to be submitted". Other than the said exhibits, the CA has not mentioned any other information as required by the directions of the Hon'ble High Court. Instead he has made general statements that: -

i. "For all the submissions made in the above written statement regarding the audit procedures performed and evidences obtained by me, the relevant documents that are available with me can be produced on request" and

ii. "Certain work papers and documents maintained by the firm are presently stored in the firm's office/s and are therefore not remotely accessible. Unless I have the opportunity to access my firm's office it is not possible for me to evaluate fully which of those documents would help to support my case and the completeness of the copies of such documents that I am submitting herewith."

d. However, vide email dated 20th July 2020, 5:51: PM, the CA has submitted a "supplemental response to the Show Cause Notice" containing two attached documents, namely, a covering letter dated 20 July, 2020, and a note dealing with evidence pertaining to seven issues, and the exhibits related thereto. The CA now says that "I state that the supplementary response should be read along with my Interim response and together they constitute my response to the SCN".

e. Keeping in view the principles of natural justice and of fairness, NFRA has examined all the replies filed by the CA, and other material on record, and has proceeded to pass this order.

13. NFRA notes that there was an explicit direction by the Hon'ble High Court in its order dated 21st May 2020, that NFRA shall not give effect to its order till 27th June 2020. The order dated 21st May has been modified by the Hon'ble High Court vide its order dated 26th June 2020, so that the date of 27th June is now extended to 31st July 2020.

B. LEGAL ISSUES

14. The reply emails, of 11 June 2020, had 10 attached documents in PDF format. Each of these documents was examined in detail. The first document is titled in the Index as "Preliminary / Prima facie submissions in respect of the SCN" and contains pages numbered from 1 to 59. The second document titled in the index as "Exhibits referred to in the preliminary / prima facie submission" The document is dated 10th June 2020 and is addressed to Secretary, NFRA.

15. In his Preliminary Prima facie submissions, the CA has made the following legal points:

a. The SCN has been issued by the Secretary, which is not as per law (para 2 of the reply). However, this assertion has been contradicted by the CA himself in para 11 of his submissions where he acknowledges that the Secretary has issued the SCN under authorisation from the Executive Body of NFRA.

b. The SCN has been issued without fully considering the responses submitted by his firm before the issuance of the Audit Quality Review Report dated 12th December, 2019, ("AQR") and also his firm's request for a meeting vide its letter dated 23rd December, 2019, in order to explain their position with regard to the conclusions and findings arrived in the AQR.

c. He further reiterates that all that is stated in his firm's submissions dated August 3, 2019 and November 4, 2019 in response to the prima facie opinion and DAQR issued by the Authority, respectively, should be considered as part of his reply, as if the same had been incorporated therein by reference.

d. Various issues challenging the constitutional validity of Sec 132(4) of the Act, the jurisdiction of NFRA, etc., have been raised in a Writ Petition before the Hon'ble Delhi High Court, and NFRA should not proceed with the disciplinary proceedings until the High Court has pronounced its judgement.

e. Due process has not been followed by NFRA, since investigation into professional misconduct cannot be based on monitoring activities; and the procedure to be followed for the disposal of the SCN has not been made known.

f. The investigation into professional misconduct is quasi-criminal in nature.

g. Paras 59 to 61 of the judgement in Council of ICAI vs. Somnath Basu [reported at AIR 2007 Cal 29] have been quoted to argue that "Even if there is any negligence in performance of duties or errors of judgment in discharging of such duties, the same - cannot constitute misconduct unless ill-motive in the aforesaid acts are established."

h. Tri-sure India Ltd. vs. A.F. Ferguson Co. & Ors. [reported at (1981) 61 CompCas 548 (Bom)] has been cited to say that "In judging whether an auditor exercises reasonable care and skill, it would not be appropriate to proceed on matters which have subsequently transpired, but one must place oneself in the position of the auditor as when the accounts were audited and find out how the matters appeared for ought to have appeared to a man of reasonable care and skill…".

i. Kishorelal Dutta vs P.K. Mukherjee [reported at AIR 1964 Cal 131], has been quoted to say that ""Whether there is an error of judgment, and a claim of bona fide exercise of normal and reasonable care, particularly in cases outside his special province of accountancy; whether it was a case of technical breach though he acted with due diligence or whether he acted mala fide." **needs to be examined while coming to a conclusion relating to professional misconduct**. (emphasis supplied). It needs to be noted even here that the portion extracted by the CA is from para 36(5) of the judgement which is the para that deals with the **considerations that should be borne in mind at the time of imposing the type of penalty**. (emphasis supplied).

j. Chander Kanta Bansal vs Rajinder Singh Anand [reported at (2008) (5) SCC 117 has been cited to define "due diligence". It has to be noted that this is a judgement under the Civil Procedure Code and having no direct reference or bearing to the Second Schedule to the CAs Act.

k. Nanhelal vs Assistant Registrar, Co-operative Societies and Others [reported at AIR 1970 MP 39], has been cited to draw a distinction between negligence and gross negligence. The court had held that "In Black's Law Dictionary the expression is defined as follows: 'The intentional failure to perform a manifest duty in reckless disregard off the consequences as affecting the life or property of another; such a gross want of care and regard for the rights of others as to justify the presumption of wilful-ness and wantonness." It is to be noted that this citation also is not with reference to the Chartered Accountants Act.

16. Regarding the submission that the AQRR has been issued without considering the responses of the Audit firm and their request for meeting after issue of AQRR, it may be noted that NFRA's AQR follows a due process as set out in its internal regulations. The Chronology of events leading to the issue of the AQRR is detailed in Annexure II to the published AQRR available on the website of NFRA. As should be evident from a plain reading of the AQRR, full and adequate opportunity has been provided to the Audit Firm (Deloitte Haskins and Sells LLP or DHS) at each stage of the preparation of the AQRR to explain the material in the Audit File in the light of the views of the NFRA. As the AQRR is a time bound process carried out under the provisions of Companies Act, 2013, NFRA is duty bound to complete the exercise in a timely manner, observing reasonable care and fairness. The said meeting mentioned by the CA is a post AQRR meeting and has no support of law. Moreover, by issuing the SCN, NFRA had given adequate opportunity to the CA to explain his position again and to give his views regarding the observations in the AQRR/SCN.

17. Besides, it has to be noted that SA 230 clearly lays down that the Audit File should be capable of speaking for itself without the need for any other aids to interpretation. What has been claimed to

have been done by way of audit procedures, or what has been claimed to have been gathered as audit evidence, should be attested/supported by the audit file. No claim that is not so supported can be taken into consideration. Given this position in the SAs, there is virtually no scope for purely oral submissions or discussions. All oral representations have also to be reduced to writing so as to form part of the record, and to eliminate the scope for disputes. It is only such record, backed by pre-existing evidence from the Audit File, that can be accepted for the AQRR.

18. In any event, the letter dated 23rd December, 2019 referred by the CA very clearly says that the Audit Firm does not accept any of the findings of the AQRR. No reasoning whatsoever has been given for this conclusion of theirs. Given this stand on the part of the Audit Firm, a meeting and/or discussion with DHS was not likely to be productive of any result. Any meeting could be meaningful only if the objective was to discuss ways and means to correct the deficiencies pointed out in the AQRR, and to arrive at an understanding about the remedial action proposed and the way forward. There is no indication of such an approach on the part of the Audit Firm, and there was, instead, a completely unjustified and wholesale rejection of the findings of the AQRR, without any evidence whatsoever. In the light of this position, NFRA did not agree to the request of the Audit Firm for a post AQRR meeting.

19. Regarding the firm's submissions at the DAQRR stage, these submissions were analysed in detail and fully addressed while forming the AQRR; repeating the same without any additional grounds or evidence to support the claims is futile.

20. As far as the issues reportedly sub judice before the Hon'ble Delhi High Court are concerned, these are admittedly matters that are not within the purview of the NFRA. The Hon'ble Delhi High Court has permitted the NFRA to continue the proceedings relating to the SCN and pass orders thereon, subject to the condition that NFRA shall not give effect to them until 31 July, 2020. Therefore, it is not necessary for NFRA to go into any of those matters.

21. The CA has been charged with professional misconduct in terms of Sec 132(4) of the Companies Act, 2013. It is, therefore, important to lay out the background and the context to Sec 132 and to understand its implications for the present disciplinary proceedings.

22. Sec 132 of the Companies Act is the culmination of a process of fundamental reform and restructuring of the Regulatory Structure for the Audit Profession. The transformation that has been achieved over the years is summarized by the following:

    a. Creation of an independent external regulator. The Statement of Objects and Reasons for the Companies Bill said that "The Authority shall consider the International Financial

Reporting Standards and other internationally accepted accounting and auditing policies and standards while making recommendations on such matters to the Central Government which will improve the competitiveness of our companies with other companies. The Authority is also proposed to be empowered with quasi judicial powers to ensure independent oversight over professionals";

b. Removing the Self Regulatory Organisation from the structure that deals with Public Interest Entities (PIEs);

c. Providing statutory status to Accounting Standards and Auditing Standards;

d. Convergence of such Accounting Standards and Auditing Standards with the respective International Standards and minimising the deviation from such international standards;

e. Focus on the protection and promotion of the public interest, and the interests of investors, creditors and others associated with companies to be the guiding principle of audit regulation, and not the protection of either issuer or auditor interests.

23. The various sections of the Companies Act, 2013, that work together to bring about this transformation are as follows:

a. Sec 132, that establishes the National Financial Regulatory Authority (NFRA), defines its mandate and functions and vests it with the necessary powers, including the powers to levy penalties on Chartered Accountants for professional misconduct;

b. Sec 133, which empowers the Central Government to prescribe Accounting Standards under the Act. These accounting standards have now, therefore, the status of law, and are not merely guiding principles that are issued by the ICAI;

c. Sec 143(10), which empowers the Central Government to prescribe auditing standards under the Act. As explained above, auditing standards are also now law;

d. Sec 143(2) of the Act, which requires the Auditor's Report to take into account the provisions of the Act, the accounting and auditing standards and the matters required to be included in the report by either the Act or the Rules or orders made under Sec 143(11). This means that compliance with the accounting and auditing standards by a CA in his statutory audit of a company is a statutory duty, which carries with it a strict liability.

24. The explanation to Sec 132(4) says that for the purposes of the sub-section, the expression "professional or other misconduct" shall have the same meaning assigned to it under section 22 of the CAs Act, 1949. This will have to be read in the context of the specific jurisdiction that has been granted to the NFRA. The First and Second Schedules to the CAs Act define what constitutes "professional or other misconduct". These Schedules are applicable to all CAs, whether in practice, or in employment. NFRA's jurisdiction is, however, confined to auditors of Public Interest Entities (PIEs). As explained above, these auditors have to now work in terms of the framework provided by the Companies Act, 2013, and the accounting and auditing standards prescribed under the Act. "Professional or other misconduct" as defined in the Schedules has to be understood in the context of the work that the PIE auditor has to do, and the responsibility cast on him. Essentially, therefore, professional misconduct would amount to failure to comply with the auditing and accounting standards which, as explained earlier, now have the status and force of law.

25. After the Enron and other such episodes rocked the system of auditing to its very foundations, the International Auditing and Assurance Standards Board (IAASB) initiated a Clarity project to improve the clarity of its standards based on revised drafting conventions. The ICAI has aligned the conventions of drafting its standards with those adopted by the IAASB. The New Format, which has been made applicable from 1st April, 2008, incorporates the fundamental principles of the Standards of Auditing (SAs) in the Requirements section of each SA, and these are represented by the use of "**shall**", whereas prior to the new standards, the word used for this purpose was "**should**". (Page 5 of the Handbook of Auditing Pronouncements ICAI 1st Feb, 2019).

26. As mentioned above, the New Format SAs were brought into force in April 2008. The ICAI issued the Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services to be effective from April 1, 2008. Para 8 of this Preface states as follows:

> "8. **Statements on Auditing are issued with a view to securing compliance by professional accountants on matters which, in the opinion of the Council, are critical for the proper discharge of their functions. Statements are, therefore, mandatory**" (emphasis supplied)

What are today known as Standards on Auditing were earlier known as Statements of Standard Auditing Practices.

27. In this context, the very important practical difference that this change in language has made is even better understood through the Rules of the Public Companies Accounting Oversight Board (PCAOB). Rule 3101 (a) of the PCAOB Rules states as follows:

(1) Unconditional Responsibility: The words "must," "**shall**," and "is required" indicate **unconditional responsibilities**. The auditor must fulfill responsibilities of this type in all cases in which the circumstances exist to which the requirement applies. Failure to discharge an unconditional responsibility is a violation of the relevant standard and Rule 3100.

(2) Presumptively Mandatory Responsibility: The word "**should**" indicates responsibilities that are **presumptively mandatory**. The auditor must comply with requirements of this type specified in the Board's standards unless the auditor demonstrates that alternative actions he or she followed in the circumstances were sufficient to achieve the objectives of the standard. Failure to discharge a presumptively mandatory responsibility is a violation of the relevant standard and Rule 3100 unless the auditor demonstrates that, in the circumstances, compliance with the specified responsibility was not necessary to achieve the objectives of the standard.

28. Clearly, the change in language now brought about, when read also in the context of the explanation in the PCAOB Rules, which is admittedly of high persuasive value, has cast a mandatory duty on the auditor to comply with the SAs, in an unconditional manner, unlike earlier, when the use of the word "should" provided some discretion to the auditor to show that alternative methods of compliance were possible.

29. The CA has argued that the investigation and proceedings in respect of the alleged professional misconduct of a CA are of a quasi-criminal nature. No specific provision of law, or any clear authority, has been quoted by the CA in support of this argument. Perhaps, the CA intended to rely as support for this argument also on the extract from the decision of the Calcutta High Court in Somnath Basu to the effect that "Professional misconduct on the part of the person exercising one of the technical professions cannot fairly or reasonably be found, merely on a finding of a bare non-performance of a duty or some default in performing it. The charge is not one of inefficiency, but of misconduct and in an allegation of misconduct an imputation of a certain mental condition is always involved" and that "Even if there is any negligence in performance of duties or errors of judgment in discharging of such duties, the same - cannot constitute misconduct unless ill-motive in the aforesaid acts are established."

30. In deciding about the above matter, it is necessary to look into what exactly is meant by "quasi-criminal", whether the interpretation of the statute in this connection must necessarily bring out any necessary mental condition or ill-motive as an essential ingredient of the professional misconduct, whether there are any other authorities that have taken a different view from that of the Calcutta High Court in Somnath Basu etc.

31. In The Council of the ICAI vs. Shri Mukesh Gang, the Hyderabad High Court defined the following point for its determination:

"Sri S. Ashok Anand Kumar, learned counsel for the respondent, would contend that the proceedings, before the Committee and the Council, are quasi-judicial and quasi-criminal in nature. The initial onus will always lie on the Institute to prove the guilt of the respondent beyond reasonable doubt and the principle of appreciation, i.e. preponderance of probabilities, applicable to Civil Cases cannot be applied to quasi-criminal cases i.e. disciplinary proceedings before the authorities."

32. The High Court elaborately discussed several authorities bearing on this point, including the decision of the **Constitution Bench of the Supreme Court in Seth Gulabchand vs Seth Kudilal and others (1966 AIR 1734)** where it was held as follows:

"It is apparent from the above definitions that the Indian Evidence Act applies the same standard of proof in all civil cases. It makes no difference between cases in which charges of a fraudulent or criminal character are made and cases in which such charges are not made. But this is not to say that the Court will not, while striking the balance of probability, keep in mind the presumption of honesty or innocence or the nature of the crime or fraud charged".

33. The High Court's conclusion was as follows:

"In view of the law laid down by the Constitution Bench of the Apex Court, in Gulabchand v. Kudilal (referred supra), and the Judgment of the Privy Council in A, a pleader v. The Judges of the High Court of Madras (referred supra), it must be held that the standard of proof required to establish a charge, in a disciplinary proceedings, is on a preponderance of probabilities, and cannot be equated with the standard of proof in a criminal prosecution, wherein a charge is required to be proved beyond reasonable doubt. Accordingly, this point is decided."

34. The action for professional misconduct most closely approximates disciplinary proceedings carried out by government against its employees for violations of its Conduct Rules. **The Supreme Court** has held in **Uttarakhand Transport Corporation & Ors. Appellant (s) Vs. Heera Singh Parihar Respondent(s) CIVIL APPEAL NO 9520 OF 2019 (Arising out of SLP (C) No 4911 of 2019)** that:

"At the outset, it may be noted that the High Court applied the wrong test in exercising its power of judicial review with reference to disciplinary proceedings. **Disciplinary proceedings are not quasi criminal in nature**. A disciplinary inquiry is conducted by the employer to inquire into a charge or misconduct pertaining to a breach of the rules and regulations governing the service of the employer. **The standard of proof is not that governed by a criminal trial. In exercising judicial review the test is whether the findings are based on some evidence. The High Court**

may interfere with only in a case where there is no evidence to sustain the charge of misconduct. (emphasis added).

35. As mentioned above, the institutional framework of independent external regulation of the audit profession is entirely new to India, though it has been in place in other advanced countries for several years. The criteria followed by regulators such as the PCAOB or the FRC in deciding on charges of professional misconduct are persuasive evidence in respect of similar cases in India. For instance, the Rules of the PCAOB provide as follows as far as the burden of proof in disciplinary proceedings is concerned:

"Rule 5204. **Determinations in Disciplinary Proceedings**

(a) **Burden of Proof**

In any disciplinary proceeding instituted pursuant to Rule 5200(a)(1), Rule 5200(a)(2), or Rule 5200(a)(3), the interested division shall bear the burden of proving an alleged violation or failure to supervise by a **preponderance of the evidence**. A respondent raising an affirmative defense shall bear the burden of proving that affirmative defense by a preponderance of the evidence". (emphasis supplied)

36. As far as the procedure followed by the NFRA is concerned, this has been entirely in consonance with the stipulations in the NFRA Rules. Adequate notice of all the charges and the evidence in support thereof which are sought to be relied upon have been given to the CA. Full opportunity to reply to the charges, both in writing, and in person, has been provided to the CA. All the evidence and arguments that the CA has presented have been carefully considered. In this connection, it is useful to quote what the Hyderabad High Court has said in **Mukesh Gang:**

"The strict rules of evidence, under the Indian Evidence Act, and the elaborate procedure prescribed under the Code of Civil Procedure or the Criminal Procedure Code, are not applicable to proceedings before the Disciplinary Committee of the Institute except for a few provisions of the Code of Civil Procedure as stipulated under Section 21 (8) of the Act. There is nothing in the Act, or in the Regulations, which disables the Committee from evolving its own procedure in conducting an enquiry into the misconduct alleged to have been committed by a member of the Institute."

This ratio would apply a fortiori to the case of disciplinary proceedings under the NFRA Rules.

37. The CA has been charged with professional misconduct in terms of the following clauses in Part I of the Second Schedule to the CAs Act:

i. Clause 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;

ii. Clause 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;

iii. Clause 7: ***does not exercise due diligence***, or is grossly negligent in the conduct of his professional duties;

iv. Clause 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;

v. Clause 9: fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances.

Text in italics in the extracts above refer to the amended portions brought about by the amendments of 2006.

38. The Second Schedule, among other parts/sections of the CAs Act, 1949, was amended by the CAs (Amendment) Act, 2006, which came into force with effect from 17 November, 2006. It needs to be kept in mind that these amendments were part of the response to the global move towards enhancing auditor accountability that was set in motion following the Enron, Worldcom scams etc., and the establishment of independent auditor regulation. It is necessary to study the amendments to the definitions of professional misconduct carefully in order to understand the new jurisprudence this has given rise to. As a corollary, it needs to be kept in mind that the authorities cited for various propositions that are derived from judgements pertaining to the prior era need to be relied upon with caution, only after rigorously examining whether the ratio of those decisions would still hold the field.

39. In clause 5, the portion "**but disclosure of which is necessary to make the financial statement not misleading**" has been substituted by "***but disclosure of which is necessary in making such financial statement where he is concerned with that financial statement in a professional capacity***". The vital change that has been made is to remove the ingredient of making a financial statement "**misleading**". There is now an absolute liability and responsibility on the auditor to disclose all material facts known to him, irrespective of whether the absence of such disclosure has the effect of making the financial statement misleading or not. This is not only in line with the

change from "**should**" to "**shall**" in the SAs that has been referred to above, but also in line with several decided cases in advanced countries such as the USA and the UK.

40. In Clause 7, the portion "***does not exercise due diligence"*** has been added. It is **not only** gross negligence that will now constitute professional misconduct. **Even the non-exercise of due diligence will constitute actionable professional misconduct. What constitutes due diligence in any case is decided primarily by the Requirements Sections of the applicable SAs**. As explained earlier, the Requirements of the SAs impose an unconditional responsibility on the auditor. A strict liability approach has been now brought in by these changes. This is also in line with several decided cases in advanced countries such as the USA and the UK.

41. A crucial para of the Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services issued by the ICAU is para 11. This is, therefore, extracted in full here.

"11. **It is the duty of the professional accountants to ensure that the Standards/Statements/General Clarifications are followed in the engagements undertaken by them.** The need for the professional accountants to depart from a relevant requirement is expected to arise only where the requirement is for a specific procedure to be performed and, in the specific circumstances of the engagement, that procedure would be ineffective. If because of that reason, a professional accountant has not been able to perform an engagement procedure in accordance with any Standard/Statement/General Clarification, he is required to document how alternative procedures performed achieve the purpose of the procedure, and, unless otherwise clear, the reasons for the departure. Further, his report should draw attention to such departures. However, a mere disclosure in his report does not absolve a professional accountant from complying with the applicable Standards/Statements/General Clarifications."

42. The footnote to the sentence extracted in bold font above in para 41 says that "Members' attention is invited to Clause 5 of Part I of the Second Schedule to the Chartered Accountants Act, 1949, according to which a chartered accountant in practice shall be deemed to be guilty of professional misconduct, if he 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. **Further Clause 7 of Part I of the Second Schedule to the Chartered Accountants Act, 1949 states that a chartered accountant in practice shall be deemed to be guilty of professional misconduct, if he does not exercise due diligence, or is grossly negligent in the conduct of his professional duties".** (emphasis supplied).

43. Read in context, the above very clearly shows that failure to comply with the SAs, and especially the unconditionally mandatory Requirements portion thereof, would amount to not only failure to exercise due diligence, but could also be gross negligence depending upon the facts of the case. The touchstone, however, always remains the compliance with the SAs. It bears repetition to say that, as far as the PIEs, whose audits are the remit of NFRA, are concerned, the duty cast upon auditors by the SAs is a statutory duty, as explained at length earlier.

44. We also need to keep in mind Response 12 in the ICAI's Implementation Guide on Reporting Standards (November 2010 edition) that says that "**A key assertion that is made in this paragraph is that the audit was conducted in accordance with the SAs**"; and that "**If during a subsequent review of the audit process, it is found that some of the audit procedures detailed in the SAs were not in fact complied with, it may tantamount to the auditor making a deliberately false declaration in his report and the consequences for the auditor could be very serious indeed**" (emphasis added).

45. As far as the evidence on which to base a decision about the compliance with due diligence, or the gross negligence of the auditor, is concerned, the SAs have an in-built mechanism in the form of a specific SA 230 on Audit Documentation.

46. As explained by SA 230, the Nature and Purposes of Audit Documentation are to provide:

    a. Evidence of the auditor's basis for a conclusion about the achievement of the overall objectives of the auditor; and

    b. **Evidence that the audit was planned and performed in accordance with SAs and applicable legal and regulatory requirements**. (emphasis added).

47. SA 230 lists the following among the additional purposes that are served by the audit documentation: Enabling the conduct of quality control reviews and inspections in accordance with SQC 1; and **Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements**. (emphasis added).

48. Para 7 of SA 230 emphasises the "Timely Preparation of Audit Documentation" i.e. in a manner contemporaneous with the events that are being sought to be documented.

49. Apart from SA 230, there are other SAs that also require the documentation of events, data, evidence, opinions and conclusions. SA 230 makes it very clear that reliance can be placed **only** on the audit file as evidence of what was done. Para A5 of SA 230 makes this explicit in the

following words: "**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". (emphasis added).

50. The CA has cited the decision of the Supreme Court in Chander Kanta Bansal vs Rajinder Singh Anand [reported at (2008) (5) SCC 117] in order to show what "due diligence" means. In the said judgement, the Supreme Court quoted Black's Law Dictionary to the effect that ""Due diligence" means **the diligence reasonably expected from, and ordinarily exercised by, a person who seeks to satisfy a legal requirement** or to discharge an obligation" (emphasis added).The Court also quoted Words and Phrases by Drain-Dyspnea (Permanent Edition 13A) which says that ""due diligence", in law, means doing everything reasonable, not everything possible. "Due diligence" means reasonable diligence; it means such diligence as a prudent man would exercise in the conduct of his own affairs." It is to be noted that the said judgement was not in relation to a matter under the CAs Act, but a matter arising under Order VI Rule 17 of the Code of Civil Procedure. Nevertheless, what is important for the facts of the present case is that "due diligence" is what is required from a person who has to satisfy a legal requirement, which is the case with the SAs.

51. What has been stated above in para 50, as quotations from law lexicons, is a generalised proposition. This needs to be understood specifically by asking the following questions:

    i. To whom is the duty of "due diligence" owed?
    ii. What is to be done to ensure compliance with "due diligence"?
    iii. How, and in what manner, is the duty to be discharged?
    iv. What is acceptable proof of the proper discharge of this duty of "due diligence"?

52. **To whom is the duty of "due diligence" owed?** The **ICAI Framework for the Preparation and Presentation of Financial Statements in accordance with Indian Accounting Standards** says the following about the **Users of Financial Information. "**The users of financial statements include present and potential investors, employees, lenders, suppliers and other trade creditors, customers, governments and their agencies and the public"**. The management of the entity is specifically excluded from the set of users.** The purpose of financial statements is said to be "The objective of financial statements is to provide information about the financial position, performance and cash flows of an entity that is useful to a wide range of users in making economic decisions". "Due diligence" is required to meet these information needs of these users. Clearly, the duty of "due diligence" is not owed to the management.

53. **What is to be done to ensure compliance with "due diligence"?** Meeting the Requirements portions of the SAs is what is to be done to comply with "due diligence". Understood thus, this no longer remains a fuzzy, inchoate responsibility, but a clearly defined duty. It is also not a case of the judgement or opinion of the regulator as a substitute for that of the auditor. There is a clear set of positive duties that are cast upon the auditor by the SAs and which need to be complied with to claim that "due diligence" has been delivered. Legal authorities that discuss the concept of 'due diligence" in a generalised scenario have to be relied upon only for general principles.

54. **How, and in what manner, is the duty to be discharged?** As a professional, the auditor has to display the level of competence, skill, and application that is normally expected of such a professional. This is the irreducible minimum. Recognising the fact that the interests of the users as a group are at variance with the interests of the management, the SAs also require him to maintain independence from the management of the auditee company. Apart from the SAs, there are numerous restrictions and safeguards that are built into the Companies Act itself, that need to be complied with. The auditor is also required to maintain an attitude of professional skepticism which is defined 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" (Para 13(l) of SA 200) It also includes "questioning contradictory audit evidence and the reliability of documents and responses to inquiries and other information obtained from management and those charged with governance" (Para A20 of SA 200).

55. **What is acceptable proof of the proper discharge of this duty of "due diligence"?** For the reasons explained in paras 17 and 46 to 49 above, the audit file will be the sole, acceptable, proof of the proper discharge of this duty of due diligence. The CA has quoted the following extract from the decision in Tri Sure. "In judging whether an auditor exercises reasonable care and skill, it would not be appropriate to proceed on matters which have subsequently transpired, but one must place oneself in the position of the auditor as when the accounts were audited and find out how the matters appeared or ought to have appeared to a man of reasonable care and skill". As explained earlier, the audit file is a contemporaneous record of the work of audit. By using this as the sole evidence, the regulator avoids judging matters with the benefit of hindsight. Thus the contention of the CA in his reply that "the SCN and the subsequent communications from NFRA indicate that NFRA does not intend to follow the principles of natural justice" because NFRA "has directed me to provide my responses only based upon documents available in the audit file {as defined in para 6(b) of SA 230} for the engagement of the statutory audit that was subject to the investigation" is contradictory to his own submissions.

56. The reliance on the audit file as the sole permissible evidence regarding the due performance of his duties by the auditor is also the basis for the summary procedure prescribed for disposal of misconduct cases by Rule 11 of the NFRA Rules. The PCAOB's Rules can be referred to with benefit to understand the rationale and scope of this summary procedure. Rule 5427(d) of the PCAOB Rules provides that "The hearing officer shall promptly grant a motion for summary disposition if the pleadings, depositions, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a disposition as a matter of law". Where facts are not in dispute, since the only proof accepted is the audit file, a summary procedure for disposal of the misconduct proceedings is appropriate. Read together with the opinion of the AP High Court in para 36 above, it is clear that the process followed by NFRA is valid in law.

57. As far as "gross negligence" is concerned, Black's Law Dictionary, 4th Edition, defines "negligence" as "The omission to do something which a reasonable man, guided by those ordinary considerations which ordinarily regulate human affairs, would do, or the doing of something which a reasonable and prudent man would not do". The Dictionary defines "gross negligence" as "The Intentional failure to perform a manifest duty in reckless disregard of the consequences as affecting the life or property of another; such a gross want of care and regard for the rights of others as to justify the presumption of willfulness and wantonness" .In **Mukesh Gang**, the High Court held, following this definition, that " For an act of negligence to constitute gross negligence, it must be in reckless disregard of a legal duty and of the consequences to another party, or wilful or voluntary or wanton omission". The Court held further that "As seen from the definition of gross negligence, even an act of omission, or reckless disregard of a legal duty, by a statutory Auditor amounts to gross negligence". Given the statutory nature of the SAs, the mandatory Requirements portion of the SAs, and the strict guidelines and advisories issued by the ICAI, it is clear beyond doubt that failure to comply with the duties imposed by the SAs on the auditors would constitute "gross negligence".

58. In his reply to the charge in Article III of being grossly negligent, the CA has quoted the ICAI to support his arguments about not having been guilty of gross negligence. He has stated that "The words "Gross Negligence" have also not been defined in the Chartered Accountants Act. At the same time, the commentary on Clause 7 of Part I of the Second Schedule published by ICAI states that negligence per se does not constitute gross negligence, and thus does not amount to professional misconduct. Any professional accountant would be liable for misconduct only if his actions amounts to culpable negligence, which would justify holding him guilty for gross negligence". Clearly, it is not the case that "negligence" per se constitutes "gross negligence". The ICAI draws upon "culpable" negligence in order to define "gross negligence". Even admitting this

method as valid for the purposes of understanding the scope of the term, it is important to note that Black's Law Dictionary defines "culpable negligence" as " Failure to exercise that degree of care rendered appropriate by the particular circumstances, and which a man of ordinary prudence in the same situation and with equal experience would not have omitted". The particular circumstances in the present case would be the statutory duty cast upon the auditor by the SAs. Every auditor would, as a matter of prudence, comply with the SAs. Failure to do so would certainly, therefore, amount to culpable negligence, and therefore, also amount to gross negligence. This limb of the argument is without derogation to the direct definition that has been explained earlier.

59. On a detailed examination of the above judgments and legal authorities quoted by the CA, the following additional matters are evident, apart from what is explained already.

a. All these judgments are dated prior to 1st April 2014. On this date the provisions of section 143 of the Companies Act, 2013 came into effect. In this regard, as clearly stated in para 2 to Annexure 1 of the SCN, and section 143 (10) read with section 2 (7) of the Companies Act, 2013, all the standards of auditing (SAs) are required to be mandatorily complied with from the date of their respective applicability while conducting statutory audit. Section 143 (9) clearly stipulates that every auditor shall comply with the auditing standards. Since the cited judgments are before the date on which the SAs were made part of the Law, the interpretations, principles and law positions emerging from these judgments need to be analysed and revised in the light of the radical legislative changes happened in between.

b. As all the charges in the SCN are primarily on account of violations of the SAs by the CA, and consequent violations of the Companies Act, 2013, and Code of Ethics, the cited judgments are not relevant in determining professional misconduct. None of these judgments takes into account the fact that the SAs are Law now and the statutory audit shall be conducted as per SAs. Hence the concepts, principles and definitions of terms etc. as explained in these judgments are to be understood in the new context. The violations cited in the SCN are violations of law and failure to discharge the duties of the CA as statutorily required.

c. The context of the case of Nanhelal vs Assistant Registrar, Co-operative Societies is totally different from the maters in the SCN. In this case, the petitioner was not surcharged for any act of his which may have itself resulted in loss to the Cooperative Society in which the petitioner was employed , but for the loss arising from acts of misappropriation and misconduct of the employees of the Society working under his supervision. The court observed that there is no finding that the petitioner was guilty of gross negligence; the

finding merely is that the petitioner was guilty of negligence. In the absence of finding that the petitioner was guilty of gross negligence, the court ordered in his favour.

d. In Institute of Chartered Financial Analysts of India v. Council of the Institute of Chartered Accountants of India (Case No. Appeal (civil) 6835 of 2000) the Apex Court, while considering the misconduct of a clerk, drew a distinction between a misconduct committed by an employee and professional misconduct and held that, in case of professional misconduct, the person in the profession precisely knows what is expected of him. In Institute of Chartered Accountants of India v. Shri Mukesh Gang, Chartered Accountant (Andhra High Court, 2016) the court went in depth to analyse negligence and gross negligence and stated that "failure to discharge the statutory obligation or duty imposed on an Auditor by a statute i.e. issuing certificate, without verifying actual receipt of consideration, amounts to gross negligence since such omission is in utter disregard of the statutory duty imposed on the respondent, and is not a simple professional lapse on his part". The court held after examination in detail that the action of the respondent was in dereliction of his statutory duty and, therefore, was gross negligence.

e. Since the SAs are now statutorily required to be followed any violation of SAs is a violation of the statute and hence amounts to gross negligence.

C. REPLIES TO THE SPECIFIC ARTICLES OF CHARGES

60. The CA then proceeds to provide article of charge -wise replies to the SCN. He states in para 51 that "before proceeding to respond to the charges/allegations levelled in the SCN section wise, I am providing herein below a brief summary of my response to each charge/section. I specifically state and reiterate that the same should be read with the detailed response of each section that is attached hereto". The para-wise replies to the Articles of Charge are analysed with respect to respective paragraphs in the SCN. The CA has denied all the charges. No evidences or documents or work papers forming part of the audit file already submitted to NFRA have been referred in this part of the reply in support of the claims. In the absence of such evidences or new facts in support of his claim, and in light of his statement that the averments made in para 51 of his reply are the summary of detailed replies provided elsewhere, these summary replies are analysed along with the detailed replies in the subsequent paragraphs of this document.

61. The email of 13 June, 2020, second cited in para 11, contains the written summary of the oral submissions made by the CA during the oral hearing through video conferencing (VC) mode on 11th June 2020. This is as per the stipulation in the SCN that all oral explanations shall be reduced to writing for consideration by the authority. While the CA had rebutted all the charges in the SCN

during hearing, he has not mentioned anything about the specific charges in his written summary of his oral submissions/reply. This e-mail of 13 June, 2020, deals with matters relating to the procedural aspects of the hearing, manner of holding the VC, and matters under the consideration of the Hon'ble High Court of Delhi.

62. The SCN has been issued under the provisions of Sec 132 of the Companies Act. The procedure that has been followed by the NFRA is also in line with that prescribed under that Section. The specific replies to the SCN that have been by the CA with respect to the charges in the SCN are analysed with respect to the respective paragraphs of the SCN. Matters that are the subject matter of writ petitions before the Hon'ble High Court, as also the claims regarding the procedure to be followed by the NFRA, are not dealt with in this order, since this is not the appropriate forum to go into such matters.

63. The attachment to the email of 11 June, 2020, titled in the Index as "Exhibits referred to in the preliminary / prima facie submission" and contains pages numbered from 60 to 169. These are the 7 exhibits referred to in the first document (which is the preliminary/prima facie submission). However, as detailed above, none of these exhibits provide any support to the rebuttal of charges attempted in para 51 of the document titled "Preliminary / Prima facie submissions in respect of the SCN".

C.1. Examination of the reply to para 1.0 of Annexure II to the SCN

C.1.1. Summary of the Reply

64. The submission by the CA is titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 1.0 of Annexure II to the SCN" having pages numbered from 1 to 23 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 1.0 of Annexure II to the SCN" having pages numbered from 136 to 272 relate to replies to the para no. 1.0 of Annexure II to the SCN and this has been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

1.0 Actions/Omissions leading to misconduct in relation to compliance with independence requirements (Reference: para 2.2 of the AQR Report).

1.1 NFRA had examined certain engagements as detailed in the Annexure I of AQR Report, where services. had been provided by the Audit Firm and its related entities (as defined by the Explanation to Section 144 of the Companies Act 2013) to either IFIN, or its holding company, Infrastructure Leasing and Financial Services (ILFS) Ltd. In all these cases, the Audit Firm was found to have, either directly or indirectly, provided prohibited services to the Auditee, or its holding company, thus violating the provisions as per section 144 of the Companies Act 2013: Besides; none of the non-audit services provided was with the prior approval of the Audit Committee of IFIN.

1.2 CA Udayan Sen in his capacity as Engagement Partner, had failed to examine independence requirements as provided- in SA 200 and hence failed to exercise. due diligence for the check of Independence requirements on providing prohibited services mentioned under section .144 of the Companies Act, 2013. He had not independently exercised reasonable due diligence to ensure compliance with section 144 of the Companies Act, 2013. He did not adhere to the ethical requirements pertaining to independence as provided in SA 200. This resulted in compromise of the independence in mind and independence in appearance required of the auditor.

1.3 Thus CA Udayan Sen failed to exercise due diligence to verify if the Independence requirements were complied with or not and was grossly negligent in the conduct of his professional duties due to violation of the provisions of Section 144 of the Companies Act, 2013, SA 200 and the Code of Ethics applicable to Chartered Accountants.

1.4 The above actions/omissions of CA Udayan Sen; therefore amount to professional misconduct of failure to exercise due diligence, and being grossly negligent in the conduct of his professional duties (clause 7 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

65. The CA in his reply denies all the charges of professional misconduct for failure to examine independence requirements or exercise due diligence to verify compliance with Independence requirements. He submits that instances set out in Exhibit 1.1 (at pages 136 to 272) have not been considered by NFRA.

66. He submits that NFRA's observations regarding non-audit services arise from the following three aspects – (i) NFRA's interpretation of the term "management services" referenced in Section 144 of the Companies Act, 2013; (ii) self-review threat of personnel or due to scope of services provided; and (iii) the quantum of non-audit fees earned by the Audit Firm by rendering such services. He claims that none of NFRA's observations is supported by the alleged facts.

67. Regarding the definition of "management services", he submits that "the Audit Firm did not engage in any "management services" or perform any "management functions" or "management responsibilities". Instead, it provided advice and recommendations to assist management in discharging its responsibilities. In doing so, the Audit Firm did not undertake any decisions, or implement any decisions, on behalf of the management, nor did it make any judgments or take actions for management. Accordingly, the Audit Firm did not provide any management services and therefore did not violate the independence requirements that prohibit the performance of "management services.""

68. He further states that "as admitted by NFRA in paragraph 2.2.3(d) of the AQR Report, section 144 of the Companies Act, 2013 ("the said Act") does not define the term "management services." Nor has the MCA or ICAI ever clarified the term and NFRA may not and should not do so through a disciplinary proceeding. Accordingly, any allegation that the Audit Firm engaged in "management services" requires NFRA to adopt a new interpretation—and any allegation concerning my conduct therefore depends on the reasonableness of that interpretation. "An interpretation that does not find support in the applicable laws and regulations or as to which I did not have clear and prior notice cannot fairly be used to discipline me under principles of natural law or otherwise."

69. He further states that:-

    a. the Audit Firm "had referred to the IESBA Code of Ethics, which serves as the mother code from which the ICAI Code of Ethics is generally derived; it had further made a detailed study of the history of legislation; further still, the Firm applied its judgement to arrive at the conclusion regarding the applicability of these terms" and thus he concluded that the non-audit services rendered by the audit firm do not fall into the scope of management services as envisaged in the Companies Act, 2013.

    b. "With regard to the alleged self-review threat arising out of the scope of work on the non-audit engagements, no such threat existed considering that (a) the specific terms set forth in the engagement letters for each engagement precluded us from performing any management functions, roles, and/or responsibilities; and/or (b) none of these engagements impacted the Company's financial reporting process or internal controls which would be subject to our audit procedures; and/or (c) the engagements were not considered prohibited services under the ICAI Code of Ethics, including in particular because the scope of services did not entail making any decisions for management; and/or (d) based on our reasonable judgment, none of the engagements were covered under the list of prohibited services under section 144 of the said Act."

c. Each of the eight engagements to provide non-audit services during the years 2016-17 and 2017-2018 when the CA served on the IFIN audits, complied with section 144 of the Act and the ICAI Code of Ethics.

d. "NFRA has in the AQR stated that the total fees for the 15 engagements listed in Annexure I of the AQR (covering multiple years) was Rs. 666. 63 lakhs in comparison to the Audit Fee for the year 2017-18 of Rs. 401 lakhs for both the auditors. It may be noted that these 15 Engagements related to services provided to IL&FS Ltd., the holding company of the group, in addition to IFIN"

e. "The fees of the audit firm and its affiliate entities for non-audit services from the respective entity did not exceed the audit fees for that entity in each year and, indeed, were lower"

f. "Out of the non-audit service engagements referred to in the AQR, only two engagements involved services rendered to IFIN itself and therefore only those two engagements required the approval of IFIN's Audit Committee..... both these engagements were to the knowledge of IFIN's Audit Committee and board and therefore the engagements complied with the applicable Rules, Regulations and law"

g. "The non-audit engagements for services provided to IFIN were appropriately approved by, in one case, the Committee of Directors in line with its delegated powers and was noted by the IFIN's Board, and in the other, by a member of IFIN's management with delegated authority from IFIN's Board. Given that the aforesaid non-audit engagements were undertaken with the approval of IFIN's Board, which included members of IFIN's Audit Committee there is no merit in the allegation that no separate approval of the Audit Committee was sought for the aforesaid engagements."

70. Referring to para A2 of SA 220 he submits that he had exercised due diligence in the conduct of his professional duties, and that he is not guilty of professional misconduct within the meaning of clause (7) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

C.1.2. Examination of the reply

71. It was clearly stated in the SCN and AQRR that the firm had violated independence norms and provided services prohibited by section 144 of the Companies Act during the period of audit. The CA has resorted to a lengthy explanation to justify his stand that many of such services provided are in the nature of management advisory/ consultancy services and hence permitted. He states in his reply that "In the AQRR, NFRA stated in paragraph 2.2.14(a) that, "the words used in the statute

must be understood in their normal or dictionary sense and be given their literal and direct meaning". He adds that, however, NFRA has not stated anywhere its position regarding the normal or dictionary sense of "management services," let alone the basis for such position.

72. It is a well-accepted principle in interpreting statutes that the provisions of a statute should be interpreted literally and grammatically giving the words their ordinary and natural meaning (the plain meaning rule). Accordingly, NFRA had made the above observations in the AQRR, as quoted by the CA in his reply. The partly quoted para 2.2.14 (a) of AQR is reproduced more extensively for better clarity.

    a. Para 2.2.14 (a) "Admittedly, the term "management services" has not been defined in the Companies Act, 2013. In such situations, the settled principles of statutory construction require that the words used in the statute must be understood in their normal or dictionary sense and be given their literal and direct meaning. While doing so, the context in which the words are used will clearly be important. At the same time, the principles of interpretation would require that no extraneous matter should be brought in as part of the interpretation. Similarly, all the words used in the statute would have to be given their full meaning and no part of the statute can be rendered otiose."

73. As mentioned in the said para NFRA had analysed the wording of the section and had concluded that:

    a. "It is clear that the context, which is one of prohibition of provision of non-audit services by the auditor of a company, would mean that "management services" should be interpreted only as services that can be, or potentially can be, provided by the auditor to the management of the company. Given the context, it would be entirely repugnant thereto to interpret the term "management services" as "services performed or rendered by management". If this were to be the interpretation, the question would then arise as to the person/entity for whom management is performing or rendering any services. The argument of the Audit Firm that the term "management services" implies the equivalent of "management responsibilities" is unacceptable since "management responsibilities" would mean actions to be done/functions to be undertaken BY management and not services rendered TO management, which is what is required by the context in which the term appears. "Management responsibilities" have to be discharged ONLY by management and cannot be done by others. All others, including auditors, can help management in discharging such responsibilities by providing them services of various kinds."

b. "Hence, the definition of "management services", read in the context in which the term has been used in the statute, can be only understood to mean "services performed by the statutory auditor" for the management, either (a) in the form of doing actions/functions that would otherwise have to be done/undertaken by the management; or (b) providing any kind of support (inclusive of analysis, research, advice etc.) that is required by the management for the performance of those actions/functions."

c. "As explained above, it is completely impermissible in all accepted norms of statutory construction to import concepts, meanings, and definitions from extraneous sources in a situation where a plain reading of the words of the statute does not indicate that this is either permissible or has necessarily to be done."

74. It is important in this context to note that the CA has himself stated in his response that the Audit Firm "provided advice and recommendations to assist management in discharging its responsibilities". This is precisely what is comprehended by the term "management services" as explained above.

75. Regarding the argument of the CA that the "ICAI Code of Ethics 2011 the Draft ICAI Code of Ethics 2014 and IESBA Code of Ethics 2013, again repeating the language in the IESBA Code of Ethics 2010, both specifically exclude from the category of prohibited "Management Responsibilities" the provision of advice and recommendations to assist management in discharging its responsibilities, i.e., they specifically authorize an auditor to provide such non-audit services", NFRA would like to:

a. Reiterate its observation in the AQRR in para 2.2.14 (d) (reproduced above in para 73 (c)). The ICAI's Code of Ethics, 2019 are not relevant since these have neither come into force yet, nor these were in force on the date of Audit Report.

b. Without prejudice to the above, NFRA notes with shock the unprofessional method resorted to by the experienced CA in interpreting statutes to support his unjustified claim. The CA conveniently ignores the fundamental fact that the Companies Act 2013 is an Act of Parliament, unlike the ICAI Code of Ethics. The latter in no way can have the effect of changing the language of the Act and it cannot either curtail or expand the ambit of the sections of the Act. Thus, the prohibition of "management responsibilities" in the Code of Ethics has to be read independently and in addition to or supplemental to the provisions of the Act and only to the extent that it is not repugnant to the express provisions and language of the Act. If the advisory services and recommendations to assist management etc. are permitted as per the Code of Ethics, such permission can in no way be extended to define

the explicit provisions of the Companies Act, 2013, in so far as the Companies Act does not permit for such an interpretation in line with that of the Code of Ethics. Such a permission in the Code of Ethics only means that the term "management responsibility" as used in the Code does not include such services.

c. This is further explicit from para R600.8 of the Code of Ethics 2019 that provides that "**Subject to applicable restrictions under Companies Act, 2013**, to avoid assuming a management responsibility when providing any non-assurance service to an audit client, the firm shall be satisfied that client management makes all judgments and decisions that are the proper responsibility of management" (Emphasis supplied).

d. Thus by a plain reading of section 144 of the Companies Act, 2013 as rightly done by NFRA in the AQRR, the literal meaning of the words management services includes any services provided by the Audit Firm to/for the management. The dictionary meanings of the word service is "providing something" and the term management means "the act of running and controlling a business or similar organization" and/or "the people who run and control a business or similar organization" [Reference: Oxford Dictionary].

76. Apart from the above, the self-review threat exists in many of the non-audit engagements listed in the AQRR due to the reasons as detailed in the AQRR. A few cases are given below.

a. the threat of self-review is certain in the auditor providing "investment advisory services" [Services provided vide engagement letter dated 16-FEB-2018].

b. The services vide engagement letter dated 11-JUN-2018 create a self-review threat. For example, analysing computation of MAT and advance tax deals with a source of the financial information subject to the review or audit. Further, representing an income tax case before Tribunal may impact assessment of contingent liabilities under AS 29. Similarly, assistance in appeal proceedings at various other levels such as DRP and High Court, and in obtaining legal opinion, will result in a self-review threat, and compromise of independent audit.

c. There is a clear self-review threat in services provided vide engagement letter dated 03-APR-2017. The same can be noted from the scope in the EL, which, inter-alia, states that, "… assist IL&FS Ltd. and its subsidiaries and affiliates as per annexures attached herewith (collectively referred to as "Client") in tax matters for the benefit of the Client."

d. As per 290.181 of ICAI Code of Ethics, 2009, a self-review threat may be created when the litigation support services provided to a financial statement audit client include

estimation of the possible outcome and thereby affects the amounts or disclosures to be reflected in the financial statements.[Services provided vide engagement letter dated 9-SEP-2016].

77. Regarding approval of non-audit services by the Audit Committee, NFRA notes that the CA has not been able to provide any documentary evidence of Audit Committee approvals in respect of the several cases described in the AQRR.

78. Where a non-audit service is sought to be rendered by the auditor, either directly or indirectly, it has to be decided, at the threshold, if such service falls within any of the prohibited categories as per Section 144. The authority to decide this matter, in the Scheme of the Act, is vested only in the Audit Committee in the case of listed companies. It is not open to the auditor, or any of its related entities that undertakes the formal provision of the service, or even of the Board of Directors, to make this determination as to whether a service falls within the prohibited list or not. The contentions of the CA in his supplemental reply dated 20th July, 20202, that in two cases, where "approvals" had been provided by a committee of the Board of Directors, or by a delegatee of the Board, and that, therefore, it must be taken as compliance with the Act, is clearly not acceptable for the reasons explained above. Such an argument, if accepted, would result in the Audit Committee being reduced to a nullity. Such an argument by a responsible and senior CA is reflective of a contemptuous disregard for all principles of corporate governance and would itself constitute professional misconduct.

79. A feeble attempt has been made by the CA to show Audit Committee approval for at least one of the non-audit services engagements. The CA has submitted (Exhibit 1.7) an extract of what he claims are the Minutes of the Audit Committee Meeting held on 6th November 2017 (page 670). What is marked out in this page is regarding the reporting back to the Audit Committee on the action taken on the decisions of the previous meeting. It is seen that the exhibit is actually the minutes of the Audit Committee meeting held on 20th December 2017, and not that of 6th November, 2017. At the 6th November, 2017, meeting, the decision was to prepare the opening IndAS Balance Sheet as on 1st April, 2017, and examine its impact in consultation with DHS and BSR (who were the joint statutory auditors). There was no decision recorded about the giving of the consultancy in question. Neither was there any such decision on 20th December. A casual, oblique, passing reference to "consulting firms" is not the same as approval of the Audit Committee in terms of Sec144 read with Sec 177 of the Act. To construe otherwise would be to cavalierly disregard all the statutory requirements of corporate good governance. In any event, even this consultancy is clearly prohibited by Sec 144(a) "accounting and bookkeeping services" and Sec 144 (c) "design and implementation of any financial information system". In addition, there is a clear self-review

threat since the statutory auditors would be reviewing work done by themselves in another capacity as consultants. To summarise, (a) there was no approval of the Audit Committee under Sec 144; (b) The service in question is clearly prohibited by Sec 144; and (c) The service gives rise to a major self-review threat.

80. Regarding the other submissions made by the Auditor, all these matters are already addressed in the AQRR. The same is not reproduced here for the sake of brevity.

C.1.3. Conclusion

81. As explained above, in the absence of any new factual or documentary evidences that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 1.0 of Annexure II to the SCN are held as having been proved.

C.2. Examination of the reply to para 2.0 of Annexure II to the SCN

C.2.1. Summary of the Reply

82. The submission by the CA titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 2.0 of Annexure II to the SCN" having pages numbered from 24 to 43 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 2.0 of Annexure II to the SCN" having pages numbered from 273 to 398 relate to the para no. 2.0 of Annexure II to the SCN and have been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

2.0 Actions/Omissions leading to misconduct in relation to the role of the Engagement Partner (Reference: paras 2.3 and 2.10 of the AQR Report)

2.1 CA Udayan Sen, being the Engagement Partner as defined in Para 6(b) of SQC 1, had signed the audit report notwithstanding the documented facts that he had completely failed in discharging his obligations as Engagement Partner.

2.2 The list of work papers reviewed by CA Udayan Sen, clearly shows that almost all the important work of audit, i.e., independence evaluation, risk assessment, audit plan, audit procedures, audit evidence, communications with management or those charged with governance (TCWG) was not directed/supervised/reviewed by CA Udayan Sen. The date-wise schedule of hours charged by CA Udayan Sen to the engagement as Engagement Partner was not provided to NFRA, nor was any reference in the Audit File provided in support thereof. Consequent to his failure to discharge the role of EP by CA Udayan Sen, the audit quality had badly suffered. SA 220 clearly provides that the Engagement Partner shall take responsibility for the overall quality on each audit engagement to which the partner is assigned. SA 220 further provides that the engagement partner shall take responsibility for the direction, supervision and performance of the audit engagement in compliance with professional standards and regulatory and legal requirements. However, CA Udayan Sen failed to discharge these obligatory requirements as per the SA.

2.3 As per para 8 of SA 220, the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned. However, CA Udayan Sen in his capacity as engagement partner failed in discharging this obligation of ensuring the quality of audit.

2.4 Engagement Quality Control Review (EQCR) team of DHS has completely failed in documenting its working properly and separately from the work of the Audit team as required by SQC 1 and SA 230; failed to do any independent analysis nor questioned the engagement team regarding issues arising out of RBI inspection and direction, failed to carry out review work on timely manner at appropriate stages of engagement, failed in appraising the quality of the work performed, failed to document various requirements as required by Para 25 of SA 220.

2.5 EQCR team failed to prepare proper documentation related to discussion between EQCR Team and CA Udayan Sen in his capacity as Engagement Partner, that is violation of Para 3 of SA 230 as detailed in Para 2.10.6 (a) of the AQR Report.

2.6 EQCR team failed to review multiple audit work papers; there is not a single paper in the Audit File where the EQCR team has carried out independent analysis or review, which is a clear violation of Para 6 of SQC 1 as detailed in Para 2.10.6 (b) of the AQR Report.

2.7 EQCR team failed to adhere to the requirement of para 25 of SA 220 that stipulates to document reasons and the bases for conclusions and not merely provide check box "Yes" or "No" responses that EQCR team had done in this audit. The EQCR team had neither done any independent analysis nor questioned the engagement team by examining working papers (Example Working Paper 2434). The EQCR Team failed to attend Audit Committee Meetings as detailed in Para 2.10.6 (c), (d), (e), (f) & (g) of the AQR Report, in violation of Para 25. of SA 220.

2.8 Overall, the Engagement was performed by the Engagement Partner in violation of several provisions of SAs including those contained in SA 200, SA 220, SA 230, SA 240, SA 250, SA 260, SA 315, SA 570, SA 580, and SA 700. The Engagement Partner had also violated the Companies Act 2013, SQC 1, Code of Ethics, and RBI Regulations as well. While there is such a huge gap in audit procedures, the Engagement Partner signed an unmodified audit report on the general purpose financial statements of IFIN, thus concluding that the auditor had obtained reasonable assurances that the financial statements as a whole are free from material misstatements due to fraud or error. Having done all such violations, the Engagement Partner stated in his unmodified report that the audit was conducted in accordance with the standards of auditing, which is not true to the facts.

2.9 The instances of failure to comply with the requirements of the SAs are of such significance that it appears to the NFRA that the Audit Firm did not have adequate justification for issuing the Audit Report asserting that the audit was conducted in accordance with the SAs. Failure to comply with any of the Requirements of applicable SAs indicates that the Audit Firm has failed to achieve the central purpose of the audit, and that there was not an adequate basis to issue the report that it did. Thus the Engagement Partner CA Udayan Sen did not exercise due diligence in ensuring audit quality and is grossly negligent in the conduct of his professional duties by not adhering to the requirements as laid down by the relevant statutes.

2.10 The above actions/omissions of CA Udayan Sen, therefore amount to professional misconduct of failure to exercise due diligence, and being grossly negligent in the conduct of his professional duties (clause 7 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

83. The CA in his reply has denied all the charges. He states that he has discharged all his duties as engagement partner consistent with the Auditing Standards and all significant aspects of the audit were appropriately supervised and reviewed by a partner, both through his own review, and the review of CA Shrenik Baid, to whom he delegated certain responsibilities and who ultimately reported to the CA. Throughout the audit, the CA had numerous discussions with CA Shrenik Baid about the delegated matters and/or that CA Shrenik Baid supervised directly on a day-to-day basis.

84. He submits that "I was closely involved in the consideration of each of the issues that I deemed to be most important and I personally reviewed and assessed workpapers relating to significant areas of the audit, that I had oversight of the work performed by other members of the Engagement Team, and that I had understood and agreed with the conclusions reached by them."

85. Quoting para 17 of SA 220, he further states that "NFRA ignores information I obtained through discussion with the Engagement Team, which, together with my review of workpapers, satisfied me that sufficient appropriate audit evidence had been obtained to support the conclusions reached and for the audit opinion to be issued".

86. He claims that he was engaged in numerous communications beyond what is assembled as the work papers, including onsite meetings with the Engagement Team, meetings with management, and meetings with those charged with governance, as well as numerous emails with the Engagement Team (refer Exhibits 2.13.1 to 2.13.17), apart from review of audit workpapers during the approximately 180 hours spent by him on the engagement. He stated that "during May 2018, I was onsite at IFIN's offices frequently in order to meet with the client management and the Engagement Team, and to review the status and details relating to the audit procedures performed and evidence

obtained in the audit, as well as to review and provide comments regarding documentation provided by the client management and drafts of workpapers". He cites certain email exchanges to support his claims. He also lists a few workpapers (already reviewed by NFRA) to prove his claims.

87. He states that the "conclusion memo summarised the discussions Mr. Baid and I had prior to the issuance of the Auditor's Report regarding the process of the audit, the key matters observed during the audit and the conclusions reached (Refer Exhibit 2.11 (to be submitted))".

88. It is stated in para 2.3.3 of his reply that "The reporting of the matter relating to NOF/CRAR arising from the observations of the RBI in their inspection reports as an Emphasis of Matter was discussed with the EQCR and then with a technical specialist, and then was the subject of a formal consultation through the Firm's internal consultation process. The consultation was raised as the issue warranted further consideration by additional experienced professionals within the Audit Firm. This is just one example of how I exercised my professional judgment in responding to issues of elevated significance. Refer Exhibit 2.12 work paper 30516 for the concurrence obtained on the manner of reporting relating to the NOF/CRAR matter."

89. He further states that he attended Audit committee meeting and worked directly with CA Shrenik Baid, the other audit partner on the engagement, the other members of the Engagement Team, and the Joint Auditors, in preparing for the discussions of the significant audit matters at the meeting and in drafting the presentation to the Audit Committee. He quoted Paragraphs 49 and 50 of SQC 1 to support his claim that he reasonably and appropriately performed all the contemplated supervision and review.

90. Regarding time spent on the engagement he states that "to the extent that NFRA relies on the specific allegation that my date-wise schedule of hours charged as Engagement Partner was not provided to NFRA, nor provided in the Audit File, such allegation has no basis whatsoever in the professional standards. On that basis, the aforesaid allegation is denied. NFRA's use of the phrase "timing" in paragraph 9 of SA 230 reflects a misinterpretation and misapplication of its meaning because it does not relate in any respect to time recording. Instead, it relates to the timing of when a given procedure was performed and/or reviewed".

91. Regarding EQCR he states that "As explicitly provided in SQC 1 and its Implementation Guidance, I do not select or supervise the EQCR, and the EQCR is not part of the engagement team and does not participate in the performance of the engagement. Instead, the EQCR has certain (defined) responsibilities with respect to engagement quality control that are independent of the engagement team. Accordingly, my submission does not address the specific performance of the EQCR other than as it relates to my own professional responsibilities relating to the EQCR" The requirements

as per paragraph 19 of SA 220 he claims have been complied by him and he refers to Exhibit 2.14 for copy of affirmation of completion of engagement quality control review and Exhibits 2.16 through 2.17 which reflect the Engagement Team's request for engagement quality control review of the draft IFIN Financial Statements and confirmation that such review was completed prior to the issuance of the opinion.

92. He states that "The AQR does not identify any instance where I have violated, as part of my reporting obligations, any provisions under the RBI Regulations as alleged in paragraph 2.8 of Annexure II to the SCN."

93. He stated that the audit was performed in accordance with the professional standards and regulatory requirements after exercising due care and professional skepticism, and applying his professional judgment in that process, and denies any violation of the provisions of SAs including those contained in SA 200, SA 220, SA 230, SA 240, SA 250, SA 260, SA 315, SA 570, SA 580, and SA 700.

C.2.2. Examination of the reply

94. In para 2.3.1 of his reply, he lists work papers which relate to the significant areas of audit that were personally reviewed by him. None of these workpapers shows conclusive evidence of review of independence evaluation, risk assessment, audit plan, audit procedures, audit evidence, communications with management or those charged with governance. Thus, the charge in the SCN reading his failure to review the important work of the Audit remains.

95. The argument of the CA is that he has delegated the key tasks to his partner CA Shrenik Baid. It is pertinent to note that no documents in the Audit File show such a delegation and the nature and extent of duties delegated by the CA. Instead, Exhibit 2.12, Email concurrence by the Consultation team for Emphasis of Matter (Source: EMS WP 30516 Request - 2401 Reviewed Agreed by Consultation team for the year ended March 31, 2018) mentions that the engagement Partner is CA Shrenik Baid. Thus, it is clear that there was no proper communication among the engagement team that the engagement partner is CA Udayan Sen. None of the exhibits mentions that engagement partner is CA Udayan Sen, though the CA had signed the Audit Report on behalf of the Audit Firm. This is in violation of SA 220 and SQC-1.

96. The email correspondences submitted by the CA as exhibits clearly show that the involvement of the CA was primarily in coordinating with the top management of the auditee and arranging meetings with them, rather than reviewing the works done by the engagement team. It is, in fact, this aspect of the function performed by the CA that was referred to in para 2.2.9 of the AQRR to

prove the familiarity threat to independence of the auditor. The emails only serve to corroborate this conclusion. The mails other than meeting requests were intended only to pass on certain information to the CA by the engagement team. There are neither evidences to indicate that any review has been carried out on such intimations nor replies in the nature of review/observations given by the CA. Most of such mails are from the engagement team, not from CA Shrenik Baid (though he is copied in many mails) to whom it is stated that the key responsibilities were delegated.

97. The SCN points out violations of SAs and SQC-1 based on such instances pointed out in the AQRR. In reading the AQRR as a whole, all these violations are proved in the absence of any evidences to the contrary submitted by the CA. Hence the claims by the CA that there is no violation of SAs is not admitted. As there are so many instances of violations, the charge in the SCN that the CA in his capacity as engagement partner failed in discharging this obligation of ensuring the quality of audit is established beyond any trace of doubt. This is a violation of para 8 of SA 220, which stipulates that the engagement partner shall take responsibility for the overall quality on each audit engagement to which that partner is assigned.

98. Time recording by Auditor (Engagement Partner and members of the Engagement Team) is mandatory in light of Para 9 of SA 230 that requires the auditor to record the nature, timing and extent of audit procedures performed in the Audit documentation. As such, the CA did not comply with the mandatory requirement of recording time as required both by SAs as well as the Quality Policy of the Audit Firm.

99. The instances of failure of the EQCR partner has been brought out in the SCN for making it clear that the engagement is performed in violation of the applicable SAs. The CA states that since the EQCR is done separately, the EQCR Partner is not part of the engagement team, and does not participate in the performance of the engagement, and that, therefore, he has complied with the requirements of per paragraph 19 of SA 220. This contention is not correct because:

    a. There is no documentary evidence for discussion of significant matters arising during the audit engagement, including those identified during the engagement quality control review, with the engagement quality control reviewer. From the side of the Engagement Partner, it was his duty to document such discussions irrespective of whether the EQCR Partner had done so or not in fulfilment of his obligations.

    b. Para 15 of SA 220 further provides that the engagement partner shall take responsibility for the direction, supervision and performance of the audit engagement in compliance with professional standards and regulatory and legal requirements. The CA has not fulfilled this

responsibility since the overall engagement, and EQCR, has been conducted in violation of the SAs as noted in the SCN and AQRR.

The exhibits now provided as part of the supplemental reply are documents that are part of the audit file and have already been examined in detail for making this order.

C.2.3. Conclusion

100. As explained above, in the absence of any new factual or documentary evidences that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 2.0 of Annexure II to the SCN are held as having been proved.

C.3. Summary of the reply to para 3.0 of Annexure II to the SCN

C.3.1 Summary of the Reply

101. The submission by the CA titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 3.0 of Annexure II to the SCN" having pages numbered from 44 to 52 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 3.0 of Annexure II to the SCN" having pages numbered from 399 to 442 relate to the para no. 3.0 of Annexure II to the SCN and have been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

Actions/Omissions leading to misconduct in relation to communication with Those Charged With Governance (TCWG) (Reference: paragraph 2.4 of the AQR Report)

3.1 The Reserve Bank of India (RBI) had pointed out in various reports and letters that the IFIN was in serious violation of Net Owned Funds (NOF) requirement and Capital to Risk (Weighted) Assets Ratio (CRAR) requirement. Due to lending to the group companies in reckless disregard of the RBI's directions, the Net Owned Funds (NOF) for IFIN was recomputed by the RBI at (-) Rs.4123.76 crore as on 31.03.2016 as compared to (-) Rs.45.93 crore as on 31.03.2015. This was against a regulatory requirement of minimum Rs. 2 crore of NOF by IFIN. Similarly, the CRAR was (-) 42.61% against a requirement of minimum 15%. Thus, the regulatory non-compliances identified by RBI on the part of IFIN were very serious, material and appear to have been deliberate/willful. The specific instances of regulatory non-compliances by Auditee as noted by RBI during their inspections vis-a-vis RBI norms are listed in paragraph 2.4.6 (e) of AQR Report.

3.2 Paragraph A22 of SA 260 (Revised), inter alia; requires the auditor to communicate to TCWG, significant matters or business conditions affecting the entity. As per SA 250 (Revised) the Audit Firm was mandatorily required to communicate about the non-compliance of regulatory instructions by the Auditee (as detailed in Paragraph 2.4.6 of the AQR Report) to all TCWG at the earliest. But the Engagement Partner did not communicate the RBI inspection findings to TCWG; even once before the date of signing of Audit Report.

3.3 Thus CA Udayan Sen did not exercise due diligence in communicating such serious and material facts to TCWG and he was grossly negligent in the conduct of his professional duties by not complying with the requirements of SA 260 (Revised) and SA 250 (Revised).

3.4 The above actions/omissions of CA Udayan Sen, therefore amount to professional misconduct of failure to exercise due diligence, and being grossly negligent in the conduct of his professional duties (clause 7 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

102. The CA denies the charges. He stated that the RBI inspection findings and the matters relating to NOF/CRAR were the topic of multiple discussions between the Audit firm and TCWG, including as an agenda item at every audit committee. The communications between RBI and IFIN relating to the NOF/CRAR matter were addressed directly to TCWG, including, in particular, IFIN's Managing Director & CEO and CFO.

103. He then list out the details of audit committee discussions and attendance by the engagement team in such meetings, the details of correspondences between RBI and IFIN, presentation made by him in the Audit committee and states that "In the case of IFIN, since in our professional judgment, independently exercised by me and CA Sampath Ganesh, partner representing the Joint Auditor, it was concluded that TCWG was already seized of the matter and the facts and circumstances, in our professional judgment, did not require a modification in the audit report, the need to again discuss this matter with TCWG before the Audit Committee meeting did not arise."

104. He quotes para 23 of SA 250 and states that "I had regular communications with the TCWG on this matter, and, in other instances, I directed CA Shrenik Baid to do so, as documented in the Audit Committee Minutes. In any event, paragraph 23 of SA 250 refers to non-compliance "believed to be intentional and material". Referring to his reply to paragraph 6 of Annexure II to the SCN in this matter and "in particular to the fact that RBI provided IFIN with a period of time through March 31, 2019 to meet the modified NOF/CRAR requirements", he states that there was no matter falling within paragraph 23 of SA 250.

C.3.2. Examination of the reply

105. As per the minutes of the meetings of the Board of the Auditee in the Audit file, none of the Board meetings during the period when the audit was carried out was attended by any person from the Audit Firm. The CA claims that his review of the minutes of the Board meetings showed that the subject was discussed at the meetings. Without going into the verification of whether this was in fact so, it is clear that, in the context of the responsibility of the Audit Firm to communicate with TCWG, any reference to discussions in Board Meetings of the Auditee, at which meetings no representative of the Engagement Team was present, is totally irrelevant and a deliberate attempt by the Audit Firm to mislead this Disciplinary Proceeding by NFRA.

106. After analysing the workpapers, NFRA had concluded in the AQRR that said regulatory non-compliances with RBI norms on the part of auditee were very serious, material and deliberate/willful. Accordingly, as per SA 250, the Audit Firm was mandatorily required to communicate about the said non-compliance of RBI instructions by the auditee to all TCWG at the earliest. But the Audit Firm did not communicate this to TCWG, even once before the date of signing of Audit report.

107. Though there were many indications (as listed in the AQRR) to believe that the regulatory violations were intentional and material, thus attracting para 23 of SA 250, there is no evidence either in the audit file or in the submissions by the CA to prove that the engagement team had evaluated this matter and arrived at a reasoned conclusion. In the absence of such an analysis and evidence, the contention of the CA that the non-compliance is unintentional and not material cannot be accepted.

108. The assertion of the CA that he had exercised his professional judgement in making their communications cannot be taken to justify that nothing was required to be communicated. There were serious issues like non-compliance of RBI guidelines, issues relating to going concern, NPAs, etc. which were very significant and were mandatorily required to be communicated to TCWG as per SA 260 (Revised).

109. Regarding his submission that the TCWG "were fully aware of the matters raised by the RBI in its inspection report, including matters related to NOF/CRAR, and that these matters were the topic of multiple meetings of the Company's Audit Committee and Board of Directors", it is reiterated that, this, obviously, cannot substitute for the Engagement Team discharging their responsibility under the SA for communicating with TCWG. In fact, even the claim made by the CA in this connection is only that "As such, we were aware that the TCWG were knowledgeable of the matter since at least July 29, 2016".

C.3.3. Conclusion

110. As explained above, in the absence of any new factual or documentary evidences, that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 3.0 of Annexure II to the SCN are held as having been proved.

C.4. Examination of the reply to para 4.0 of Annexure II to the SCN

C.4.1 Summary of the Reply

111. The submission by the CA titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 4.0 of Annexure II to the SCN" having pages numbered from 53 to 84 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 4.0 of Annexure II to the SCN" having pages numbered from 443 to 582 relate to the para no. 4.0 of Annexure II to the SCN have been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

4.0 Actions/Omissions leading to misconduct in relation to the evaluation of Risk of Material Misstatement (ROMM) matters (Reference: para 2.5 of the AQR Report).

4.1 Working Paper No.13501 indicates that in contradiction to the requirement of Section 143(9) read with Section 2(7) and Section 143(10) of the Companies Act 2013, the Audit Firm had made references to certain other International Standards instead of compliance to Auditing Standards prescribed under section 143(9). Hence there is a clear non-compliance with Section 143(9) of the Companies Act, 2013. The Companies Act refers only to SAs prescribed by that statute and to no other. Hence, any reference to any SAs other than so prescribed is non-compliant with the Companies Act.

4.2 Thus, the above actions/omissions of CA Udayan Sen amount to professional misconduct as he:

i. was grossly negligent in the conduct of his professional duties as he failed to perform his professional duties as mandated in Section 143(9) of the Companies Act, 2013 by following Auditing Standards other than those provided in the said section of Companies Act, 2013 (clause 7 of the Part I of the second schedule to the Chartered Accountants Act 1949); and,

ii. failed to invite attention to a material departure from the generally accepted procedure of audit applicable to the circumstances, as he did not disclose the deviation from Standards of Auditing applicable in India (clause 9 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

4.3 IFIN was identified and notified by the RBI as a Systemically Important Non-Banking Finance Company (SI-NBFC). Nowhere in the Audit File was there any evidence that the auditors took note of the SI-NBFC character of the Client Company into its risk assessment, thus failing in understanding the Auditee and its environment as stipulated in SA 315.

4.4 As an Auditor of an SI-NBFC, the Audit Firm had certain special responsibilities to the RBI as detailed in Para 2.5.4 (b) of the AQR Report. Given the special position of the auditor of an SI-NBFC, it was incumbent on the auditor to challenge the management on the matters relating to the RBI inspection reports and, in the absence of satisfactory explanation from the management, to directly ascertain and verify the position from the RBI. However, CA Udayan Sen had not done so, and had accepted the stand of the management without question, which amounted to gross dereliction of duty and negligence on the part of the Engagement Partner.

4.5 Due to lending to the group companies in reckless disregard of the RBI's directions, the NOF for IFIN was recomputed by the RBI at (-) Rs.4123.76 crores as on 31.03.2016 as compared to (-) Rs.45.93 crores as on 31.03.2015. This was clearly a very specific evidence of risky management practices. Given this, the Engagement Partner should have worked out the NOF as on 31.03.2017 and 31.03.2018 to make an assessment of the compliance with the law by the company. However, CA Udayan Sen failed to do so, resulting in an underestimated risk categorisation of the Auditee by the Auditor.

4.6 The RBI assessment of gross Non-Performing Assets (NPA) of IFIN was substantially higher than the reported gross NPAs and RBI had asked the company to submit their detailed response/submission to these Inspection observations regarding NPA. In spite of such an evidence on record, the Engagement Partner has taken the listing of NPAs provided by the management as given and has subjected only the interest recognition and calculations in these accounts to verification. However, the basic question of whether the list of NPAs provided was itself comprehensive and did not leave out any case that needed to be considered has not been subject to testing. In accordance with Para 12 of SA 240 and Para 15 of SA 200, the auditor should have maintained professional skepticism throughout the audit, recognising the possibility that a material misstatement due to fraud could exist in the areas of revenue recognition and NPA as detailed in para 2.5.20 (i), notwithstanding the auditor's past experience of the honesty and integrity of the entity's management and those charged with governance.

4.7 As detailed in para 2.5.14 to 2.5.17 of AQR Report, CA Udayan Sen was grossly negligent in performing adequate audit procedures and, where required, substantial audit procedures, to evaluate risk of material misstatement on account of management override of control in the areas of loan sanctions and disbursements, which is the core business of the Auditee. Cases like the few referred to in para 2.5.17 of the AQR Report provide clear evidence of negligence on the part of the Engagement Partner in performing adequate audit procedures and, where required, substantial audit procedures; to evaluate risk of material misstatement on account of management override of controls, as stipulated in SA 315.

4.8 The fact that a manual override of controls had to be undertaken by the Auditee is indicative of the need to relax the conditions of viability, credit worthiness of the borrower, collaterals required etc., in specific cases. This would have been clear from an analysis of the Credit Appraisal Memorandums (CAMs). The Audit File does not provide any evidence in support of procedures performed and CAMs scrutinised to understand the reasons for manual override of controls in specific cases of loan sanctioning by the Auditee. To this extent, the large number, and proportion of value, of manual overrides was a fraud risk that was not met by adequate response in terms of the audit procedures conducted. This was subsequently brought out by RBI also in its report dated March 22nd, 2019. Details are given in Para 2.5.20 (k) of the AQR Report. Thus CA Udayan Sen had failed to exercise due diligence in exercising his judgment to identify fraud risk as mandated in SA 315.

4.9 Thus, the Engagement Partner grossly failed in evaluating Risk of Material Misstatements in the financial statements audited by them in violation of SA 240, SA 200, SA 315 and RBI directions. He, therefore, failed to draw up and implement an Audit Plan to satisfactorily address the risk of material misstatements. He failed to obtain sufficient information, with respect to NPA and manual override of controls for loan sanctioning, failed in evaluating and reporting NOF and CRAR, failed in noting the special status of the Auditee and failed in proper risk categorisation of the Auditee. Despite these, omissions, which are otherwise necessary matters for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion, he went ahead with giving his unqualified opinion on the financial statements of IFIN. Thus, he violated section 2(7) read with Section 143(10), of Companies Act, 2013 by not

complying with the provisions of SA 240, SA 200 and SA 315. Hence he did not exercise due diligence, and is grossly negligent in the conduct of his professional duties.

4.10 *The above actions of CA Udayan Sen amount to professional misconduct of*

i. 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 (clause 8 of the Part 1 of the second schedule to the Chartered Accountants Act 1949); and,

ii. failure to exercise due diligence, and being grossly negligent in the conduct of his professional duties (clause 7 of the Part 1 of the second schedule to the· Chartered Accountant Act 1949).

112. The CA denies that there is non-compliance with the applicable Standards on Auditing prescribed by Section 143(9). To support this he states that the audit was performed as per the Auditing Standards prescribed by Section 143(9) read with Section 2(7) and Section 143(10) of the Companies Act, 2013 and cites numerous workpapers that reflect how the audit procedures were tailored to the specific requirements of the SAs.

113. He further explains the alignment of ISAs with SAs and states that in the limited instances in which there are differences between the ISAs and SAs, the EMS (the proprietary audit documentation tool utilized by the Audit Firm) content utilized by the Engagement Team in the IFIN audit has been supplemented to reflect the requirements of the applicable SAs.

114. He states that in the electronic application used by the Audit Firm, where an engagement team selects the option of performing the audit under Indian GAAS/Standards on Auditing issued by the ICAI, the audit procedures are supplemented so as to meet India specific requirements to the extent there are any differences with the ISAs.

115. Regarding Systemically Important (SI) NBFC status of the auditee, he submitted that as per paragraph 25 of SA 315 the size of an organisation is not cited as a factor for consideration in determining such risk classification. The classification of an NBFC as SI-NBFC is based solely on size and does not take into consideration any risk characteristics. In accordance with the requirements of Paragraph A24 of SA 315, the Engagement Team, under his guidance and supervision, identified risks specific to the industry (e.g., NBFC Prudential Norms with regard to Asset classification and provisioning not adhered to). In addition, and in accordance with the above requirements, the Engagement Team included members with appropriate relevant knowledge and experience in this industry.

116. He further states that "Standards on Auditing do not include any requirement or guidance mandating that an auditor grade "engagement risk" based on any specific nomenclature or on classifications of normal, greater than normal, or much greater than normal. Such terms are simply the Audit Firm's internal classifications to consider, enhance, and strengthen the consideration of risk and the overall audit process beyond the requirement of the SAs."

117. He states that "NFRA's allegation that "there is no evidence that the auditors took note of the SI-NBFC character of the Client Company into its risk assessment," is demonstrably wrong. For example, WP 11104 'Memo on Risk Classification' (Refer Exhibit 4.6.A) includes an explicit recognition that "The Company is registered as a NBFC- ND –SI with the RBI…" in the section titled 'Justification for risk classification.' The memo addresses the Engagement Team's risk classification for the IFIN engagement, including through the Engagement Team's consideration of various qualitative and quantitative factors."

118. He states that "The reporting requirements addressed in Paragraph 2.5.4(b) of the AQRR are the reporting requirement for specified NBFCs to the RBI and do not relate to any additional reporting requirements on the financial statements. An auditor, in its role of expressing an opinion on the Financial Statements of a SI-ND-NBFC, does not have any additional responsibilities as compared to an auditor of a Non-SI-ND-NBFC when reporting on the financial statements. Thus, I do not understand the basis for the statement in the SCN regarding the auditor's role based on which the allegation is being made."

119. Regarding the charge of accepting the stand of the management without question, the CA submits that he critically evaluated the management responses in accordance with applicable law, standards and regulations, and had exercised due diligence and professional skepticism in this matter. In support of the claim, he states that the Minutes of the meetings between the Company officials and the RBI Officials were provided to him and the Engagement Team by the Company's management as supporting evidence relating to the RBI Matters, which meeting details were noted by the Audit Committee, comprising of eminent persons from banking industry. The Board of directors of the auditee included three eminent former Managing Directors of large Scheduled Banks who were well versed with RBI matters and communications, and the Board took note of the representations set forth in the minutes without reservation. Such minutes partake the character of a written representation and he understood them to be as such as he considered those representations as part of the overall set of audit evidence obtained relating to the RBI matters. He critically evaluated these Minutes in the context of all of the information available to him, including the fact that RBI itself had granted time to the Company until March 31, 2019 to comply with the norms for lending to companies in the same group.

120. Regarding his alleged failure to make an assessment of the compliance with the RBI regulations by the company, the CA states that matter reached finality for the first time in November 2017 only. Hence this would not have affected the position as on 31st March 2017.

121. Regarding NPA classification he submits that "RBI's final decisions regarding these credit facilities (11 cases) were not available at the time I signed the audit report on the standalone financial statements for the financial year ending March 31, 2018. As a result, I, along with the Engagement Team, evaluated the audit evidence available based on the procedures performed and reached a considered view regarding those credit facilities…….. Thus, the conclusions arrived by NFRA are again wholly unsubstantiated and unjustified. The fact that the RBI came to the same conclusion as the Engagement Team, which worked under my guidance and supervision, clearly demonstrates that I, along with the Engagement Team, have in fact performed the necessary audit procedures and reached reasonable conclusions based on the evidence obtained. Such contemporaneous evidence must be taken into account."

122. He states that "In an NBFC, a determination that a loan is an NPA is triggered based on overdue interest and principal outstanding for more than 90 days. Therefore, our audit procedures included testing the Company's internal controls over identification of the NPAs as well as substantive testing of interest income and NPA provisioning."

123. He submits that "as documented in the walkthrough of the Corporate Lending process, the Engagement Team performed testing of multiple aspects of the process. Such testing included, among other areas, (1) Follow up with borrower for overdue amounts, (2) Credit Monitoring, (3) Credit Review, (4) Provisions and Recognizing NPAs, and (5) Problem Account Management….. The Engagement Team also performed tests of operating effectiveness relating to relevant controls, including to address internal controls in the area of Corporate Lending…... The Engagement Team, determined based on its tests of operating effectiveness that such controls were operating effectively."

124. He also stated that the Engagement Team, under his guidance and supervision, also performed a number of substantive audit procedures relevant to the testing of matters relating to NPAs, provisioning, and the sufficiency of collateral.

125. He states that the Engagement Team designed and performed appropriate audit procedures to address the related risk of material misstatements, at the respective account balance level, in relation to interest income and lending activities.

126. The reply further sates that:

a. "In considering the Company's processes, NFRA has failed to note that its internal control processes, inter alia, mandated under its UAF that any loan sanctioned required the approval of more than 10 senior people in the organisation, including the Regional Head, HOD Resources, HOD Legal, HOD Accounts/CFO, All India Asset Head, Head Investment Banking, Head of Credit Risk Management Group, Group CFO, and CoD Approvers (including 5-6 directors). As such, the susceptibility of loan sanctioning to management override of controls was remote given that any such override would require collusion by practically the entire senior management of the Company, including Board members. Thus, in our professional judgment, the same was not considered as a fraud risk at the account balance level..... the Engagement Team explicitly recognised management override of controls as a pervasive risk at the financial statement level and appropriately addressed such risk in the audit."

b. "When the Company sanctioned loans manually during the year, it did not mean there had been an override of controls. Instead, it simply meant that the approvals had been obtained by hard copy signatures on physical documents or sent via email rather than electronically through IFIN's AXAPTA IT system. Those manual sanctions followed the Company's laid down procedures and do not equate with a manual override of controls. A manual sanction, as with all loan sanctions, required the approval of all of the required approvers pursuant to the Company's UAF and thus represented a transaction properly authorised and recorded in the Company's accounting records. In sum, NFRA's confusion of "manual override of controls" with "manual sanctions and controls" needs to be corrected".

c. "It is surprising that, on one hand, I have been reproached by NFRA for "repeated references to Inspection Report dated June 19, 2018," which report the Audit Firm has referred to because it affirms the appropriateness of the Engagement Team's professional judgments made during the course of the audit and, on the other hand, NFRA relies on an RBI Report dated 9 months after the Audit Firm issued the Report, that relies on hindsight in considering the circumstances following the issuance of such report and the Audit Firm's rotation out as auditors. Of course, I could not have had access to such a report at the time I signed the Audit Report for FY 2017-2018. Such a consideration completely vitiates the SCN and is highly inappropriate."

C.4.2. Examination of the reply

127. NFRAs comment in the AQRR regarding use of international standards was in the context of the Audit Firm drawing support from such standards vide their written statement that "approach of

applying both Indian and international standards and complying with the requirements of those which are, as between them, more stringent, ensures adequate and full compliance with all Indian requirements and laws on 'Independence.'". There is nothing in the reply contradicting this statement of the Audit Firm. All auditors of companies that are registered under the Act will be monitored by NFRA only with reference to standards in force in India. The supposed equivalence of International Standard to, or their even greater rigour in comparison with, Indian Standards is entirely irrelevant for the purposes of NFRA. NFRA has already clearly stated that nowhere in the Audit File is there any evidence that the auditors took note of the SI- NBFC character of the Client Company into the risk assessment. This is not contradicted by the CA. NBFCs whose asset size is ₹500 crores or more as per last audited balance sheet are considered as systemically important NBFCs. The rationale for such classification is that the activities of such NBFCs will have a bearing on the financial stability of the overall economy. (Ref. FAQ No. 8, All you wanted to know about NBFCs, Updated as on January 10, 2017, as provided by the RBI in their website "https://www.rbi.org.in/Scripts/FAQView.aspx?Id=92")

128. Given the above, it is clear that audit procedures for an SI-NBFC would have to be substantially more rigorous than for a non-NBFC of the same asset size. Clearly, if companies of the same asset size in another industry (non-NBFC) are classified as "normal", an SI-NBFC would undoubtedly qualify for a higher risk category.

129. Certainly, it is not merely the size of the business, but its nature, and its linkages with the economy at the macro level, which is relevant for risk categorization of an engagement. Asset size combined with linkages to the rest of the financial sector and the economy are what determine SI nature, not merely asset size alone. The RBI, as the chief regulator of financial and monetary matters, makes this determination, which needs to be respected and not treated cavalierly.

130. The workpaper no. WP 11104 does not take into consideration the SI NBFC status of the auditee for risk classification. Under the heading " Justification for risk classification as normal" it simply states "The Company is registered as a NBFC- ND –SI with the RBI and a 100% subsidiary of Infrastructure Leasing and Financial Services Ltd (IL&FS). In line with the overall strategy of the Group, to create distinct verticals for each business and provide a clear framework for growth and profitability, as per the scheme of restructuring, sanctioned by Hon'ble High Court of Mumbai, the Investment Banking division was hived off from IL&FS to the Company and in result all Investment Banking Assets and Liabilities were transferred to the Company with effect from April 1, 2007….." . NFRAs findings in the AQRR about a higher risk classification and reporting obligations to RBI of auditors of SI NBFCs in this regard may be referred to.

131. The special reporting obligations are detailed by RBI in Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016. Though these directions are also applicable to certain other classes of NBFCs, they are not applicable to all Non-SI ND NBFCs, as claimed by the CA.

132. Understanding the legal and regulatory environment is fundamental to all statutory audits. Also, para 11 of SA 315 requires the auditor to obtain an understanding of the relevant industry, regulatory, and other external factors having a bearing on the entity. Having ignored this basic requirement, the argument of the CA quoting para 25 of SA 315 does not make any sense.

133. Regarding the comment of the CA in para 116 above, NFRA does not say that the categorization is directly derived from and is based on any particular SA. The NFRA comment in the AQRR in this regard is reproduced here for clarity.

a. As far as the risk categorization is concerned, there does not seem to be any objective basis for slotting an engagement or client risk into normal, or greater than normal, or much greater than normal categories. The portions of the QC documentation made available in this regard (3210 – Engagement Acceptance and Risk Classification Annexure 2.4D) are worded in extremely general terms.

b. The requirement to slot the engagement risk into one of these three categories is seen to arise out of the Audit Firm's Policy document 'DPM 3210 — Engagement Acceptance and Risk Classification'. **The purpose of SQC 1 is to establish standards and provide guidance regarding a firm's responsibilities for its system of quality controls for assurance and related service engagements. Based on these standards and guidance, a firm is expected to develop specific and clearly defined policies and procedures in order to comply with professional standards and regulatory and legal requirements, to ensure that reports issued by the firm are appropriate in the circumstances** (emphasis supplied). The internal policy manuals must be read as forming part of the compliance with this mandate. Para 26 of DPM 3210 provides that "Each Member Firm should establish and document procedures and guidelines to establish that all Professional Services performed by the Member Firm are properly classified in one of the following categories." Para 34 lists the kind of users who may rely upon its work. Keeping all these factors into consideration, the Audit Firm needed to have established and documented the procedures and criteria for risk categorisation. Despite claims to the contrary, NFRA is unable to find any such criteria listed either in the policy or the Audit File.

c. The comments refer only to the inadequacies in the Audit Firm's own quality control system.

134. From the reply by the CA as summarised in para 119 above, it is evident that in a crucial matter such as regulatory non-compliance by the auditee, the CA had relied completely on auditee's internal documents. Also the contention that the minutes of the meeting of RBI officials with the auditee partakes the character of a written representation is not acceptable, as it is only an internal document of the auditee, not a written representation addressed to the auditor. Para 16 of SA 250 states "The auditor shall request management and, where appropriate, those charged with governance to provide written representations that all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements have been disclosed to the auditor". The said minutes of the meeting do not meet this criterion. Importantly, the said minutes was not a mutually agreed and signed minutes. It was prepared by the auditee themselves, not acknowledged by any of the RBI Officers.

135. Regarding the RBI communications, the matter was addressed in great length in the AQRR (para 2.5.20 (d), (e)). Without ambiguity, there is clear evidence of non-compliance by the Auditee Company, and also of the RBI being firm and consistent in its findings and stand. It is also very clear that the Audit Firm has sought to rely on interpretations of the law and correspondence that are unjustified and unsustainable. The CA totally ignored all these facts as evident from the Audit File.

136. Though the CA has explained the details of verification of the NPAs, the evidence for checking the completeness NPAs, and evidence of applying the NPA classification norms to the complete list of NPAs is not available in any of the workpapers referred. The audit evidence is not complete due to the following reasons:

a. It is stated by the CA that "please note that the Interest and principal overdues report relied on in performing such procedures was an automated report generated from the Company's IT Application system and had been identified as IPE (Information Produced by the Entity). Therefore, the Engagement Team tested the completeness and accuracy of the information provided in the report, which involved testing the appropriateness of the report logic and the report parameters, and ascertaining the appropriateness of the source data considered for generating the report. In performing such procedures to test the report, the Engagement Team involved IT experts who, based on their testing, concluded that the report was complete and accurate. (Refer Exhibit 4.14.B, 4.14.C for evidence of such testing)". However, the said exhibits do not mention anything about the involvement of IT Experts

and testing of principal overdues. Also, the statement in exhibit 4.20 mentions only about the interest overdue.

b. It is stated in Exhibit 4.18 Lending Process Note Source: EMS WP 12113.05.01 Process Note- "As per RBI norms, in case where interest or loans are not serviced by clients for 90 days, the loan asset is to be classified as Non- Performing Asset ("NPA") and appropriate provision is to be made against the same." However, as per RBI "Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016", there are 8 scenarios in which an asset can become NPA. Interest overdue is one among the eight conditions. It is unclear from the Audit File whether the Audit Firm had taken note of these conditions and whether they had tested the applicability of the remaining seven conditions of NPAs for IFIN audit. Conditions like overdue status of principal amounts, loans made available to the same borrower/beneficiary when any of the other credit facilities becomes NPA etc are in any case needed to be tested by the auditor.

c. In Exhibit 4.20, Corporate Lending Annexure to Walkthrough- Source: EMS WP 12113.05.07 Annexure to Walkthrough (Evidence Verified), it is stated that "The Axapta system provides alerts to all concerned Account officers and members of the Finance and Accounts team , as and when a receivable has remained outstanding for 30, 50 and 80 days. Based on such updates, the account officers follow up with the client and ask them to remit the amount at the earliest. However if the same does not happen and the amount remains outstanding for more than 90 days, the borrower account is classified as a Non Performing asset (NPA)." This is also silent about the applicability of the remaining conditions for NPA.

d. In Exhibit 4.32.B, Email Attachment - Source: Email Attachment, it is stated that "On Nov 15, 2017, RBI sent to the Company a copy of a complaint received containing the following key allegations: ..... A draft Inspection report for the year ended Mar 31, 2017 was received on Dec 20, 2017 wherein RBI has identified certain transactions in ____ borrower accounts belonging to 6 groups as evergreening and has proposed NPA classification. These groups were also covered in the Complaint letter". However, the aspect of evergreening is not at all seen checked by the auditor.

e. The statement of the CA that "The combined testing documented by the Engagement Team in the above-mentioned workpapers enabled us to conclude that the list of NPAs provided by the Company was comprehensive and did not exclude any NPAs." is not true as there

is in only one reference in the said testing regarding the completeness of the NPAs, i.e, the involvement of IT expert, which is not seen documented in the Audit File.

f. There is no evidence of independent evaluation of NPAs by applying the RBI Norms.

137. As far as testing of manual overrides of controls is concerned, Para 32(c) of SA 240 states that "the auditor shall evaluate whether the business rationale (or lack thereof) of the transactions suggests that they may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets". If it is in fact the case that all instances of decisions where manual override of controls took place were again put through the required approval process, with the result that approvals were obtained twice over, the reasons for a manual override in the first place itself would not subsist. This finding in the AQRR is reinforced by the submission of the CA that "A manual sanction, as with all loan sanctions, required the approval of all of the required approvers pursuant to the Company's UAF and thus represented a transaction properly authorised and recorded in the Company's accounting records" and the observation in Exhibit 4.19, Corporate Lending Walkthrough- Source: EMS WP 12113.05.06 Walkthrough Corporate lending, that "In case the CAMs, are not raised through the system owing to shortage of time or other constraints, approvals on the same are sought manually or via emails. Upon approval of the Manual CoD, the same is later regularized in the system after taking approval of all the required members."

138. The fact that a manual override had to be undertaken is indicative of the need to relax the conditions of viability, creditworthiness of the borrower, collaterals required etc. in specific cases. This would have been clear from an analysis of the Credit Appraisal Memorandums (CAMs). The Audit File does not provide any evidence in support of procedures performed and CAMs scrutinized to understand the reasons for manual override in specific cases. To this extent, the large number, and proportion of value, of manual overrides was a fraud risk that was not met by adequate response in terms of the audit procedures conducted.

139. The CA cannot take shelter of any evidence created after the date of audit report. Hence, repeated references to Inspection Report dated 19 June 2018 cannot be accepted as evidence for NPA testing. It may be noted this observation in the AQRR is with reference to the "audit evidence" as per SAs only. After failure to perform the required audit procedures, the audit firm cannot and shall not rely on RBI's conclusions after the audit report date, to substantiate the view taken by the CA at the time of signing the report. In para 2.5.20 (k), after arriving at its observations based on the audit file, NFRA concluded that para with the statement that "This was subsequently brought out by RBI also in its report dated March 22nd, 2019." Nothing from this report is quoted or relied to arrive at the observations of NFRA. The submissions of the CA to the contrary are clear

indications of deliberate misrepresentation of facts, which is resorted by the CA at a few other instances also in the reply to the SCN.

140. The auditor is required 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. The audit documentation, therefore, should be adequate in itself for all purposes. Nevertheless, and quite contrary to the contention of the CA that there were no discussions by the NFRA with them during the process of its review, it is to be noted that right from the beginning, and at every successive stage, the CA and the Audit Firm has been given sufficient opportunities and time to present their case and clarifications.

141. The following exhibits submitted as part of the supplemental reply dated 20 July, 2020, have also been examined:

a. Exhibit 4.10 – Evidence that "demonstrates that the Company's Board of Directors were aware of management's discussions with the RBI and had accepted minutes of those discussions without reservation" This is no argument for the Audit Firm accepting the said "minutes" as proof of RBI's agreement to the course of action proposed by the auditee company. The CA's contention is only proof, if at all, of the pathetic lack of professional scepticism, and lack of due diligence.

b. Exhibit 4.13 - RBI's letter dated June 19, 2018 retained only four credit facilities as to which the RBI required additional provisioning. Without going into the contents of this letter, this clearly would not be acceptable audit evidence for an audit report that had already been signed on 28th May, 2018.

c. Exhibit 4.26 - Extracts of Term sheet for facility of 900 million to Sahej E Village Limited indicating time of 90 days for creation of security - Document used for testing sample in WP 23300.01.02.10 Lending made in last quarter of the FY 2017-18. The same was admittedly not retained as part of Audit file, and hence does not require any further examination.

d. Exhibit 4.29 - Hypothecation Agreement between IFIN and Siva Shelters and Constructions Private Limited - Document not retained in EMS file but referenced in WP

30301 Audit Committee Presentation Slide no. 23 and in WP 23150.04.02. Admittedly, this document is not part of the Audit File. As has been pointed out in the AQRR, the cap on the amount payable under this Hypothecation Agreement has been placed at Rs 150 crores, while the amounts it is supposed to secure is upwards of Rs 440 crores. Besides, there is no evidence of any due diligence undertaken by the Audit Firm to assess the reasonableness of the recovery of even this amount of Rs 150 crores.

For all the reasons explained above, the exhibits provided by the CA in his supplemental reply do not serve to disprove the charges relating to Actions/Omissions leading to misconduct in relation to the evaluation of Risk of Material Misstatement (ROMM) matters.

C.4.3. Conclusion

142. As explained above, subject to the observations of NFRA under para 6.0 of Annexure II to the SCN, in the absence of any new factual or documentary evidences, that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 4.0 of Annexure II to the SCN, are held as having been proved. On perusal of the replies by the CA, the charges in para 4.1 and 4.2 are apparently also due to the failures of the Audit Firm, since they involve a fundamental flaw in the QC policies of the firm, rather than ones for which the CA can be held fully responsible personally. However, the senior position held by the CA, namely that of Managing Partner and CEO of Deloitte India, cannot be ignored, and he owed more than the normal responsibility of an employee or ordinary partner of the firm to correct this firm-wide non-compliance. This will be taken appropriately into account in the order to be made under Sec 132(4).

C.5. Examination of the reply to para 5.0 of Annexure II to the SCN

C.5.1. Summary of the Reply

143. The submission by the CA titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 5.0 of Annexure II to the SCN" having pages numbered from 85 to 97 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 5.0 of Annexure II to the SCN" having pages numbered from 583 to 754 relate to the para no. 5.0 of Annexure II to the SCN have been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

5.0 Actions/Omissions leading to misconduct in relation to the RBI Inspection Matters - Tata Tele Services Limited (TTSL) Shares and Derivative Assets (Reference: para 2.6 of the AQR Report).

5.1 The Auditee invoked pledge of shares of TTSL upon certain loan defaults. The said shares of TTSL were taken to the balance sheet of IFIN at a value of Rs.253.55 crore. RBI, in its inspection reports had observed that the break-up value. of the investment in TTSL worked out as Nil, due to negative net worth of the TTSL. RBI suggested a provision of Rs.253.55 crore on March 31, 2015. However, in order to offset the impact of provisioning that was long overdue, the engagement partner went along with the management in including in the balance sheet a derivative asset (put option on TTSL Shares) of zero value, at Rs.184.31 crore and taking credit for the same in the profit and loss account as detailed in para 2.6 of the AQR Report. Th.is has resulted in inflating the profit substantially. If the option value had not been taken at Rs.184.30 crore and the resulting credit not taken into the profit· and loss account, the profit before tax would have been only Rs.17.66 crore, thus clearly making the transaction a very material one in determination of net profit for IFIN.

5.2 CA Udayan Sen did not obtain sufficient, appropriate audit evidence to support the value of the derivative assets based on TTSL shares included in the Balance Sheet as at 31st March, 2018. He has not critically evaluated such evidence as was provided by the management, has also not challenged the contention of the management of the Auditee in relation to such derivative assets. He failed to disclose the fact that the derivative assets had only Zero value though presented at more than Rs.180 crore in the balance sheet. Hence he did not exercise the required due diligence in verification of this material transaction.

5.3 While the full provision for the TTSL shares was correct and, in fact, overdue by three years, the full valuation of the put option at over Rs.180 crores was completely unsupported by any evidence whatsoever. Clearly, this has been taken to offset the loss arising out of providing for the TTSL shares. What has been practiced is, therefore, clearly fraudulent accounting. CA Udayan Sen failed in his professional duties by not disclosing the material fact of derivative assets having zero value being shown at over Rs 180 crore, which is not disclosed anywhere. in the financial statements, without which the true and fair view of the financial, statement is compromised. He failed to report this material fact that the· reported profit includes a· material item valued inappropriately. He failed to obtain sufficient information necessary for verification of this crucial transaction in the accounts. Despite all these failures, he went ahead with issuing an unmodified audit report for IFIN.

5.4 Thus the above details of commission and omission on the part of, CA Udayan Sen amount to professional misconduct of:

i. failure to disclose a material fact known to him which is not disclosed in the financial statement o f/FIN, but disclosure of which is necessary in making such financial statement, where he is concerned with that financial statement in a professional capacity (clause 5 of the Part 1 of the second schedule to the Chartered Accountants Act 1949);

ii. failure to report a material misstatement known to him to appear in the financial statement with which he is concerned in a professional capacity (clause 6 of the Part 1 of the second schedule to the Chartered Accountants Act 1949);

iii. 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 (clause 8 of the Part 1 of the second schedule to the Chartered Accountants Act 1949); and,

iv. failure to exercise due diligence and of being grossly negligent in verifying such a material transaction (clause 7 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

144. He denies the charges of professional misconduct under clauses (5), (6), (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949. He has also enclosed six email conversations as exhibits to the detailed response, which do not form part of the Audit File. However, without prejudice to the fact that any document not comprising Audit File cannot be treated as Audit Evidence, the same has been referred to and analysed by NFRA as appropriate to the circumstances. The response goes on to say that on the one hand, NFRA alleges that he had complete information about certain material facts that were not disclosed in the financial statements. "In the same breath, it also alleges that I failed to obtain sufficient information. The contradictions contained in the charges reflect their lack of basis," the response states.

145. One of the overall objectives of the auditor as per SA 200 is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. NFRA in its review found that the valuation of the put option at over Rs.180 crore was completely unsupported by any evidence whatsoever. In this reference, he states that the auditor and audit does not involve preparing of accounts and stated that the allegations have been made against him without appreciating the applicable technical accounting, or facts underlying the transaction.

146. Regarding existence of the Put Option, he states that the Company entered in the enforceable tripartite 'Shareholders' and Option Agreement' dated December 23, 2015 with Shanmuga Real Estate and Promoters Private Limited (SREPPL) - a Siva Group Company and Chennai Properties and Investments Limited. He claims that as the market (fair) value of the TTSL had declined, the option correspondingly gained value because on exercise of the option, the entity would receive from the counter party/guarantor (SREPPL/CPIL), the decline in value as per the Put Option agreement. Regarding the negligible value of TTSL shares from the beginning, and as also for the applicability/inapplicability of the 'Guidance Note on Accounting for Derivative' by the ICAI, he states that the matter was discussed with others, including a technical specialist from the Audit Firm, to confirm that such Put Option qualified as a derivative under the stated Guidance Note.

147. Regarding the valuation of put option, he states that the Engagement Team utilised the services of the auditor's valuation experts to evaluate the Company's Put Option valuation, and that the Put Option's value was further supported by the fact that its payment was guaranteed by the expected cash flows from a land development transaction that was entered into contemporaneously. The Engagement Team considered all of the documentation supporting the

guarantee. The Engagement Team provided the valuation experts with the underlying facts of the transaction and the Company's valuation model, which applied the Black-Scholes model. About exercise of professional scepticism, he states that the Engagement Team took the average of the two scenarios and understood that the difference between the valuations of the two was immaterial.

148. He states that he obtained independent third party valuation reports on a sample basis for a selection of the HCPL land parcels that substantiated the expected cash flows supporting the guarantee. He also states that the Engagement Team also tested, on a sample basis, the charges created on HCPL Properties during the audit of the financial statements for the year ended March 31, 2018. However, NFRA notes that sufficient appropriate reference to Audit File workpapers has not been evidenced in support of the claim.

149. He states that the shares of TTSL were invoked on March 31, 2015. Shareholders' and Option Agreement (derivatives agreement) between IFIN, Shanmuga Real Estate and Promoters Private Limited (SREPPL)-Siva Group Company and CPIL, among other related agreements were signed on December 23, 2015.

C.5.2. Examination of the Reply

150. Reference is invited to para 5.2 of Annexure II to the SCN that "CA Udayan Sen did not obtain sufficient, appropriate audit evidence to support the value of the derivative assets based on TTSL shares included in the Balance Sheet as at 31st March, 2018. He has not critically evaluated such evidence as was provided by the management, has also not challenged the contention of the management of the Auditee in relation to such derivative assets. He failed to disclose the fact that the derivative assets had only Zero value though presented at more than Rs.180 crore in the balance sheet. Hence he did not exercise the required due diligence in verification of this material transaction". As mentioned in the SCN para 2.6 of the AQRR provides the basis for para 5.0 of annexure II to SCN. In para 2.6.8 (r) (iii) it is observed that "As far as the TTSL shares are concerned, they had to be treated as current investments in terms of the RBI Master Directions and valued accordingly at the lower of "break-up value" or "earning value". As has been pointed out by the RBI in its Inspection Report, this valuation was to be made as of 31.03.2015 itself. The obtaining of "independent third party valuation reports" and basing the valuation of TTSL shares on these reports was completely unwarranted and incorrect".

151. The submission of the CA is silent on this aspect. It was pointed out by NFRA in the AQRR that: -

a. The RBI had, as early as in 2015, when the transaction first took place, directed the Company to make provision for the entire value of TTSL shares as of 31.3.2015, treating it as current investment.

b. The audit form in their reply to the draft AQRR stated that "The criteria to classify the investments into current and long term investments shall be spelt out by the Board of the Company in the Company's Investment Policy" However it was made clear in the AQRR that the investment policy referred to by the Audit Firm is not found in the audit file which means that the ET had not even examined the investment policy of the company to confirm whether such a policy spells out criteria for classifying investments into current and long-term. It was also observed that the extract of the investment policy quoted by the Audit Firm is irrelevant to the present context since it makes reference to enforcement of securities as a recovery measure of the Company.

152. As is evident, even when sufficient information was available to the auditor as mentioned above, the CA failed in confirming the fundamental aspect of classification of the investment into current or long-term. Without verifying and ruling out the case for treating it as current investment, the CA straightaway supported the management classification as long-term investments.

153. The AQRR also observed that:

a. The Audit Firm have themselves confirmed that assessment of the financial statements of SREPPL was not considered necessary considering that the credit risk of SREPPL was guaranteed by CPIL. CPIL guarantee in turn was based on the MoU signed with HPCL, which was a wholly owned subsidiary of IL&FS. The Audit Firm's statement implies that the credit risk evaluation of the receivable by IFIN from Siva Group was solely on the basis of a guarantee backed by revenue generated from an IL&FS Group Company itself. There is no explanation forthcoming from the Audit File as to why an IL&FS Group company bound itself to sell its land using only the services of a Siva Group company, and also to part with as much as 20 % of the sale proceeds in return for such services as might be rendered by the Siva Group company. The Audit Firm has out right denied the need of credit risk evaluation of the borrower to assess its independent ability to meet the borrowings out of its own resources. Thus, while the financial statements of the principal debtor may not reveal the full story about its creditworthiness, the requirement of having to obtain sufficient appropriate evidence to assess the credit risks involved in this case requires that the financial statements of SREPPL, at a minimum, should have been seen and analysed.

a. As regards audit procedures said to be done with regard to HCPL properties, the working papers submitted by the Audit Firm do not support the Audit Firm's submission of verifying "original" title deeds of land mortgaged and charge creation document. Details of how the original title deeds were obtained and/or copies thereof are not available in the Audit File. Besides, it is not clear how "original" title deeds of properties that were under equitable mortgage were available for checking by the Audit Firm.

b. Not only did the Audit Firm fail to recognise this set of transactions as restructuring, but it also failed to insist upon its categorisation as NPA when there was no proof forthcoming of the account meeting the required viability benchmarks. No disclosure of this restructured account was made in the Financial Statements, though required by the RBI Directions.

154. The reply by the CA is silent on the above aspects as well. As there is no audit evidence to prove that the CA had in fact considered these aspects in arriving at his conclusions, NFRA is not in a position to appreciate the selected procedures done by the auditor to support the suspected attempt of the auditee to artificially boost profits.

155. The CA has, in his supplemental reply dated 20th July, 2020, submitted Exhibit 5.7B saying that this document is "title deeds for land mortgaged by Hill County Properties, which support the Engagement Team's procedures and testing to physically verify the original title deeds and affirm the existence of the land supporting the sale/development MOU between HCPL and CPIL". On examination of Exhibit 5.7B, it is seen that this is not the case at all. Though titled as "Documents submitted for Safe Custody", the 3 documents listed as thus being deposited are Copy of Legal OK, Loan Agreement dated September 11, 2015, and Demand Promissory Note for Rs 2400mn. Clearly, this is no evidence for having verified the original title deeds as claimed.

156. The valuation of the Put Option on TTSL shares is one of the most important elements of the Financial Statements for the year 2017-18. The value finally taken, viz, Rs 184.30 crores has inflated the profit, and the asset value in the balance sheet. It is 1043.6% of the profit before tax excluding the said option value. If the option had not been valued at Rs.184.30 crores and the resulting credit taken into the profit and loss account, the profit before tax would have been only Rs 17.66 crores. Given the trend of declining profits, this was clearly a situation where significant pressures existed on management as far as the results of the company were concerned, and one that was susceptible to fraud risk. It is in this context that the CA needed to exercise extra skepticism and challenge the management on:

a. The theoretical model used for option valuation;
b. The data sources for the inputs required by the model;
c. The computation method;
d. The fundamental principles behind the computation, so as to not result in a mechanical arithmetic exercise in a clearly inapplicable context;

e. The adjustments, if any, that needed to be made to the output of the model.

157. However, by ignoring the fundamentally problematic aspects of the transaction, as detailed in the AQRR, a few of which have been referred to above, the CA exhibited failure of due diligence and gross negligence and failed completely in challenging the management and in exercising professional skepticism. Exhibit 5.8, Clearance Memo from the Valuation Team for Derivative Assets, that has now been submitted as part of the supplemental reply dated 20 July, 2020, is part of the Audit File and has already been considered in this order.

C.5.3. Conclusion

158. As explained above, in the absence of any new factual or documentary evidences, that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 5.0 of Annexure II to the SCN are held as having been proved.

C.6. Examination of the reply to para 6.0 of Annexure II to the SCN

C.6.1. Summary of the Reply

159. The submission by the CA titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 6.0 of Annexure II to the SCN" having pages numbered from 98 to 113 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 6.0 of Annexure II to the SCN" having pages numbered from 755 to 804 relate to the para no. 6.0 of Annexure II to the SCN have been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

6.0 Actions/Omissions leading to misconduct in relation to the RBI Inspection Matters: Net Owned Funds (NOF) and Capital to Risk (Weighted) Assets Ratio (CRAR) (Reference: para 2.7 and 2.8 of the AQR Report).

6.1 The serious instances of regulatory non-compliances with respect to NOF and CRAR by Auditee as noted by RBI during their inspections are listed in para 2.4.6 (e) of AQR Report. CA Udayan Sen failed to present the impact of such calculations as per RBI Inspection Reports as it had to be disclosed in the Notes to Accounts of the audited Financial Statements as detailed in para 2.7 read with para 2.5.20 (t) of the AQR Report. The NOF/CRAR disclosure is prescribed to be appended to the Balance Sheet by the Master Direction 2016 by RBI. Also, the 'Framework for the Preparation and Presentation of Financial Statements' issued by ICAI and notified under the Act further establishes the fact that the financial statements contain notes and supplementary schedules and other information. The disclosure of NOF and CRAR being part of the notes and supplementary schedule, and hence, also being an indivisible component of the notes and schedules. and other information forming part of the financial statements, is clearly a direct requirement of law and a deemed requirement of the accounting standards. NOF and CRAR are very important indicators for investors, lenders and other creditors of an NBFC, who are defined as the users of the financial statements, thus making its disclosure a material one.

6.2 CA Udayan Sen failed in exercising due diligence and professional scepticism while examining the management argument regarding definition of "companies in the same group", which the management had taken as the basis for non-compliance with RBI inspection reports. The Engagement Partner ignored the overwhelmingly clear legal position as brought out by Companies Act 1956, Companies Act 2013, RBI Act 1934, RBI Master Directions 016 and RBI Inspection Reports and chose to accept the stand taken by the management without questioning it even once. The Engagement Partner did not critically evaluate the management response or the applicable law or the regulatory directions. He relied on internal evidences like unapproved minutes prepared by IFIN of its discussions with RBI. The Engagement Partner failed to exercise due diligence and professional skepticism, as required by the SA 250 and disclosure requirements of SA 700 among other reporting and disclosure related non-compliances.

6.3 The requirements of SA 580 needed the Auditor to obtain corroborating evidence for the matters covered by the written representation before accepting the same. However, the written representation forwarding the unacknowledged minutes of the meetings with the RBI officers regarding NOF and CRAR was inconsistent with available past evidences, and the Auditor was duty bound in terms of SA 580 to perform other audit procedures to attempt to resolve the matter. In the event of being unable to resolve the matter: a disclaimer of opinion is needed to have been made in line with SA 580. Thus the Engagement Partner failed in obtaining sufficient appropriate corroborative evidences as mandated by SAs.

6.4 Thus the above actions/omissions on the part of, CA Udayan Sen amount to professional misconduct of:

i. failure to disclose material facts relating to NOF and CRAR, which was known to him and duly noted in the audit workpapers but was not disclosed in the notes to financial statement though the disclosure of which is necessary, as mandated by the RBI Master Directions 2016, in making such financial statement, where he is concerned with that financial statement in a professional capacity (clause 5 of the Part 1 of the second schedule to the Chartered Accountants Act 1949);

ii. failure to obtain sufficient information regarding the management stand on RBI inspection matters, which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion as mandated by SA 580 (clause 8 of the Part 1 of the second schedule to the Chartered Accountants Act 1949);

iii. failure to report a material misstatement in the form of incorrect NOF and CRAR, in the financial statements with which he was concerned in a professional capacity (clause 6 of the Part 1 of the second schedule to the Chartered Accountants Act 1949; and

iv. failure to 'exercise due diligence as mandated by SA 250 by failing to take into account the legal position regarding the companies in the same group, which formed the very basis for the management stand and amounts to gross negligence in the conduct of his professional duties by not complying with SA 250, SA 580 and SA 700 (clause 7 of the Part 1 of the 'Second schedule to the Chartered Accountants Act 1949).

160. The CA denies the charges of professional misconduct drawing attention towards the standards and statute which states that the said disclosures are the responsibility of the management.

a. He quotes Para A1 of SA 250 stating that its management's responsibility in ensuring the proper conduct of operation according to law and regulation of the entity and these laws and regulation may affect the disclosure in financial statements in different ways.

b. In the Companies Act 2013, Section 134(5): "The Directors' Responsibility Statement referred to in clause (c) of sub-section (3) shall state that— (f) the directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively."

161. He states that underlying NFRA's assertions is a misunderstanding regarding the import of the term "companies in the same group" in the RBI Prudential Norms. Section 45-IA (7) of the RBI Act, 1934 provides that "companies in the same group" shall have the same meaning assigned to them in the Companies Act, 1956. The Companies Act, 1956 does not define the term "companies in the same group". Other sections of the 1956 Act use similar terminology to address different points and contexts, but none refers to "companies in the same group".

162. He further submits that the Company received the RBI letter dated May 6, 2016 whereby management wrote to the RBI in May 2016 setting out in detail the Company's rationale for using the definition of 'companies in the same group' that it had applied since 2007. The RBI was aware of the aforesaid definition of "companies in the same Group" that was being followed by the Company and did not raise any grievance or concern prior to May 6, 2016.

163. He also submits that the Company had, vide its letter dated March 31, 2015, sought clarification from the RBI regarding the applicability to the Company of a new RBI definition in November 2014 for 'companies in the group,' a term that was different than 'companies in the same group.' To which RBI stated that it is only for the purpose of applicability of Prudential Norms on multiple NBFCs in a group and will not apply on concentration of credit/investment norm. He states that it was reasonable to have understood and believed that RBI had accepted the Company's definition and that no further concerns existed at that point. Only in RBI's inspection report dated November 1, 2017 that RBI reached a point of final clarification with regarding the method of determining "companies in the same group." Once that point was clear, the Company accepted the method and RBI in turn expressly provided the Company with time until March 31, 2019 to comply with the NOF/CRAR requirements as they would apply per the new methodology.

164. He refers to extracts of para 18, 19, 22 and 25 of SA 250 "Consideration of Laws and Regulations in an Audit of Financial Statements" and states that the Engagement Team performed the following procedures in compliance with SA 250, as documented in the workpapers:

a. Gained an understanding of the RBI Matter and documented our consideration of the RBI's observations

b. Discussed the matter with the management of the Company, including the Company's key members of management and those charged with governance

165. He also submits that in respect of the definition of 'companies in the same group', the Company has adopted a policy which was approved by the Board of Directors in October 2007. This policy has been consistently followed, till date, for purpose of disclosure and computation of various ratios per RBI directions and has been used for current financial statements. The RBI in its inspection reports adopted a different method, which requires the Company to consider exposures as per section 370 (1B) of the Companies Act, 1956 for determining 'companies in the same group'. This impacts computation of Net Owned Funds (NOF) and Capital to Risk Assets Ratio (CRAR) of the Company. The RBI has given time up to 31st March 2019 to fulfil the minimum NOF and CRAR requirements. In this regard, the Company included a disclosure in Note 4 of Explanatory Notes in Annexure I and II of Note 27 (a) and 27(b) to the standalone financial statements. The identities of

most of the entities that were later deemed to be "companies in the same group" were disclosed in other areas of the financial statements, so there plainly was no effort to hide the various relationships with related parties. There was no basis for him to report anything beyond what the Audit Report addressed relating to such matter, including the inclusion of an EOM. In both his professional judgment and the professional judgment of the technical team within the Audit Firm with whom he consulted, and the Joint Auditor, the EOM was appropriate and adequate and there was no need for it to quantify the potential impact of the calculations.

166. He adds that the Joint Auditors also independently reached the same conclusion with respect to management's disclosure in its financial statement notes. He along with the Joint Auditors, discussed the above matter at length with IFIN's management throughout the audit, and shared with management a draft of the EOM in advance of the May 28, 2018 audit committee meeting.

167. He denies the charge that the written representation forwarding the unacknowledged minutes of the meetings with the RBI officers regarding NOF and CRAR was inconsistent with available past evidences, and the Auditor was duty bound in terms of SA 580 to perform other audit procedures to attempt to resolve the matter.

168. In connection with the above denial, he submitted that Company had written to the RBI on April 17, 2018 requesting RBI to continue disclosing calculations of the NOF/CRAR as per the extant manner followed over the past 10 years given that the new methodology would not require the Company's compliance until the year-ended March 31, 2019. RBI orally granted such request on April 23, 2018. The minutes of the meeting were provided to the engagement team as a supporting document relating to RBI matter.

169. He submits that the absence of specific confirmation from the RBI officials for the minutes of the discussions IFIN's management had with those officials does not negate the validity of such minutes, as the minutes partake the character of a written representation. Also, RBI itself had granted time to the Company until March 31, 2019 to comply with the Prudential Norms for lending to 'companies in the same group'. Based on all of the information available, including from the RBI's own communications to the Company, he had any reason to doubt the authenticity of the minutes of the RBI meetings or the integrity of the management and TCWG in regard to those discussions.

170. He further states that: -

a. With regard to the alleged observation that the disclosure of NOF and CRAR was a material disclosure to the investors and lenders of an NBFC, it is worth noting that the only equity

investor in IFIN was IL&FS, the parent entity, which, of course, was fully apprised of the matter.

b. The Company made disclosures relating to the NOF/CRAR matter as part of the risk factors it included in its Offer Document when raising NCDs from the public starting in November 2017, promptly after learning of RBI's position. RBI itself had given the time to implement the new methodology.

c. In any event, investors, lenders, creditors, and any other users of the financial statements (as well as, of course, the Joint Auditor) all were aware of the matter given the disclosures in the Note to the financial statements and the Emphasis of Matter paragraph in the Auditors' Report.

171. Based on the above, he submits that in his professional judgement, he considered the NOF/CRAR matter appropriately in the course of the audit in a manner consistent with the SAs and ensured adequate and reasonable disclosure and reporting of the same was made in the financial statements and audit report.

C.6.2. Examination of the reply

172. On examination of various submissions of the CA, it is observed that the CA has strongly believed that there was no need to challenge the management regarding the definition of "companies in the same group" and he claims to be right in his acceptance of the management's position on this matter. He also submits that the disclosure by the company in this regard has been adequate. He cites the credibility of TCWG, previous history of the auditee, discussions he had with the auditee and joint auditor, consultations made with the audit firm, disclosures made by the auditee in the financial statements, his professional judgment etc. as the basis for such a position. However, the reply of the CA does not address/take note of the following:

a. The contention of the CA that "companies in the same group" have not been defined by the Companies Act, 1956, is clearly incorrect. Explanation to Section 45-IA (7) of the RBI Act, 1934, provides that the term shall have the same meaning as assigned to it in the Companies Act, 1956. Sections 370 and 372 of Companies Act, 1956, clearly define the said term. These sections were made inoperative by the Companies (Amendment) Act, 1999. But they were neither repealed from the Act nor were the references to those sections in other parts of Companies Act, 1956, or RBI Act, 1934, deleted. Further, section 465 (2) (c) of the Companies Act, 2013, lays down that any rule of law, inter alia, shall not be

affected by the repeal of the Companies Act, 1956, notwithstanding that such rule of law had been derived from the repealed enactment.

b. As per definition in section 2(7) of the Companies Act 1956, "body corporate" is a wider term which includes all companies as defined in section 3 of the said Act.

c. The CA himself states in the reply that "We again draw your attention to the fact that the RBI in its inspection reports for FY 2011 and FY 2013, despite recomputing the NOF of the Company and making certain adjustments, never made any adjustment related to lending to the "companies in the same group" (Refer Exhibit 6.2 for Company's response to RBI inspection report for FY 2011 and Exhibit 6.3 for copy of the inspection report for FY 2013) (to be submitted). And there is no doubt that the Company's methodology was explicitly and transparently disclosed to RBI in various RBI filings and certificates, all without objection or concerns **in the period leading up to 2016** (Emphasis added). Hence, it was reasonable to have understood and believed that RBI had accepted the Company's definition and that no further concerns existed at that point." Thus, the CA is well aware of the fact that at least from 2016 itself the RBI had clearly communicated its stand while the company continued to follow the earlier definition.

d. It is stated in the Directors Report that "During the course of its inspection, the RBI has directed the Company to follow a different method for computation of Net Owned Fund (NOF) and Capital to Risk Assets Ratio (CRAR) and has given time till March 31, 2019 to implement the same. In response to the above, the Company is in the process of formulating a detailed plan and has communicated to the RBI that the same shall be submitted to them by June 30, 2018**. The Company has already initiated the process for reduction of the exposure to companies in the same group based on the RBI Directions**." (Emphasis added).

e. The CA submits that the matter reached finality in November 2017 and the company accepted the method prescribed by the RBI. (However this was clearly wrong and NFRA had earlier concluded in the AQRR that that RBI had taken a final view even in March 2017 and not only in November 2017 as argued by the Audit Firm).

f. Thus there was no uncertainty as on the balance sheet date as on 31st March 2018, regarding the definition of companies under the same group, or the financial implications of the proposed regulatory changes, though RBI had given the Company time until March 31, 2019 to comply with the revised NOF/CRAR requirements, and there was a proven and admitted non-compliance as on the balance sheet date. Even then, the CA had

unquestioningly accepted the management's position on this matter without considering the clear stand taken by the Regulator.

g. Given the amounts involved, (negative NOF of ₹4123.76 Crore against a minimum requirement of ₹2 crore and CRAR of (-) 42.61% against a minimum requirement of 15% as on 31st March 2016 as per RBI assessment vide RBI letter dated 1st November 2017) the materiality of the violations was apparent. However, there is no such analysis of materiality seen in the audit file. Thus, NFRA after analysing the working papers, concluded in para 2.4.6 of the AQRR that "the said regulatory non-compliances to RBI norms on the part of auditee were very serious, material and deliberate/willful".

h. None of the work papers challenge the Management stand regarding NOF/CRAR or the alleged interpretive issue of "companies in the same group". There is no independent analysis carried out by the Audit Firm regarding the issues raised by RBI or the legal position in this regard.

173. The 'Framework for the Preparation and Presentation of Financial Statements' issued by the Accounting Standards Board of the Institute of Chartered Accountants of India states that:

a. "The users of financial statements include present and potential investors, employees, lenders, suppliers and other trade creditors, customers, governments and their agencies and the public.

b. "The economic decisions that are taken by users of financial statements require an evaluation of the ability of an enterprise to generate cash and cash equivalents and of the timing and certainty of their generation. This ability ultimately determines, for example, the capacity of an enterprise to pay its employees and suppliers, meet interest payments, repay loans, and make distributions to its owners. **Users are better able to evaluate this ability to generate cash and cash equivalents if they are provided with information that focuses on the financial position, performance and cash flows of an enterprise.** (Emphasis supplied).

c. "The financial position of an enterprise is affected by the economic resources it controls, its financial structure, its liquidity and solvency, and **its capacity to adapt to changes in the environment** in which it operates." (Emphasis supplied).

d. "To be useful, **information must be relevant to the decision-making needs of users.** Information has the quality of relevance when it influences the economic decisions of users by helping them evaluate past, present or future events or confirming, or correcting, their past evaluations". (Emphasis supplied).

e. "The **relevance of information is affected by its materiality**. Information is material if its misstatement (i.e., omission or erroneous statement) could influence the economic decisions of users taken on the basis of the financial information". (Emphasis supplied).

f. "To be reliable, the information contained in financial statements must be neutral, that is, free from bias. Financial statements are not neutral if, by the selection or presentation of information, they influence the making of a decision or judgement in order to achieve a predetermined result or outcome".

g. "To be reliable, the **information in financial statements must be complete within the bounds of materiality and cost**." (Emphasis supplied).

174. Thus, as pointed out by the CA in his reply, it was the responsibility of the management to disclose material information which focuses on the financial position, performance and cash flows of an enterprise, and affects the economic decisions of the users of financial statements. While doing so the management had to consider the relevance of the information, materiality and had to disclose it in an unbiased manner and the information has to be complete within the bounds of materiality and cost.

175. The CA cites Exhibit 6.7 to establish that he gained an understanding of the RBI Matter and documented his consideration of the RBI's observations. The said exhibit being an Extract of Memo on RBI Inspection Report states and notes, *inter alia*, that:

a. The RBI had observed that "The Company should run down its exposure to Group Companies by March 2019 with no fresh lending to them".

b. However, the Company in its response had stated that "Due to difficult conditions arising out of overall slowdown in economy specially in the infrastructure sector the reduction of Group exposure below 10% of Net Owned Fund (NOF) seems in all earnest most likely to be achieved by March 31, 2021".

c. The Company had represented to the Audit Firm, after discussion with the Audit Committee and the Board that "a large part of the exposure is expected to be repaid by March 31, 2019 and for the remaining exposure it is believed that RBI would favourably consider the request for further extension post review of the cogent plan to comply with RBI directions".

d. "In its inspection for FY 2016, the RBI recomputed the NOF and CRAR based on its definition and directed .....the Company should not distribute its profits until the minimum regulatory capital and CRAR is achieved."

e. The Company had further represented to the Audit Firm that "in the unlikely event the RBI does not permit extension of timeline, and based on the discussion with the parent company IL&FS, appropriate measures would be taken to comply with RBI directions as specified below:

— Induction of the investor to share up the Capital base of the Company

— Equity infusion in the parent company to enable onward capital infusion by the parent in the Company to shore up the capital base of the Company

— Divestment of group verticals by IL&FS this would change the categorisation of exposure from group to non- group

— Assignment / refinancing of group loans by external lenders under the risk participation arrangement. The company may offer its guarantee to fast track the assignment / refinancing, requisite regulatory approval for the same would be obtained.

— Purchase of outstanding receivables in the books of group companies and is due from external parties on non-recourse basis."

However, NFRA notes that the sixty third meeting of the Audit Committee of the auditee held on 28th May, 2018 (Exhibit 7.3 A), approved the action plan on achievement of RBI directives and recommended to the Board for approval. There is no mention about the situation contemplated by the words "the unlikely event the RBI does not permit extension of timeline" in the said minutes.

176. The disclosure note provided by the company states *"In respect of the definition of 'companies in the same group', the Company has adopted a policy which was approved by the Board of Directors in October 2007. This policy has been consistently followed, till date, for purpose of disclosure and computation of various ratios per RBI directions and has been used for current financial statements. The RBI in its inspection reports adopted a different method, which requires the Company to consider exposures as per section 370 (1B) of the Companies Act, 1956 for*

determining 'companies in the same group'. This impacts computation of Net Owned Funds (NOF) and Capital to Risk Assets Ratio (CRAR) of the Company. The RBI has given time up to 31st March 2019 to fulfil the minimum NOF and CRAR requirements. The Company is committed for continued compliance with the above directions of RBI". Clearly, this disclosure note, read with a similar one in the directors report, falls short of the above said requirements laid down by the ICAI, as explained in para 173 above, and the Audit Firm's own observations and conclusions as extracted in para 175 above, and is biased towards the company since it:

a. hides the material information as noted by the CA in Exhibit 6.7 (para 181),

b. The disclosure note does not disclose critical information like the expected cost implications, materiality, company's ability to adapt to the regulatory change and the extent of non-compliance even though the matter had reached finality as on the reporting date.

177. Para 25 of SA 250 states that "If the auditor concludes that the non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall, in accordance with SA 705(Revised), express a qualified or adverse opinion on the financial statements." However, there is no attempt on the part of the CA to evaluate the financial implications and materiality. The adequacy of the of the disclosure is grossly misjudged by the auditor by totally ignoring the fundamental requirements as detailed in the Framework for the Preparation and Presentation of Financial Statements. Thus, based on a conclusion arrived at after performing audit procedures that are grossly inadequate, the CA chose to have an EOM in his report about the said disclosure. There was no adequate basis for this conclusion of the CA.

178. NFRA also observes that:

a. Para 4 of SA 450 defines Misstatement as "A difference between the amounts, classification, presentation, or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework."

b. Para 7 of SA 700 states the term "fair presentation framework" is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework.

c. The Financial statements of IFIN was prepared based on a "fair presentation framework", thus implying disclosures beyond those specifically required by the Accounting Standards.

d. Para 11 of SA 700 states that in order to form an opinion, the auditor shall conclude as to whether the auditor has obtained reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error. That conclusion shall take into account: (a) The auditor's conclusion, in accordance with SA 330, whether sufficient appropriate audit evidence has been obtained; (b) The auditor's conclusion, in accordance with SA 450, whether uncorrected misstatements are material, individually or in aggregate.

e. Para 12 of SA 700 stipulates that the auditor shall evaluate whether the financial statements are prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework. This evaluation shall include consideration of the qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments.

f. Para 13 of SA 700 stipulates that in particular, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework, the information presented in the financial statements is relevant, reliable, comparable and understandable; the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements.

g. As detailed in the preceding paragraphs, the CA has performed his audit in total disregard of the above stipulations and ignoring the glaring evidences. He did not check:

   i. whether there is a material misstatement in the light of the clear violation of regulatory norms,

   ii. whether the disclosure is adequate for a financial statement prepared on a fair presentation framework,

   iii. whether there are any indicators of possible bias in management's judgments and,

   iv. whether the information presented in the disclosure notes are reliable, comparable and enable the intended users to understand the effect of material

events on the information conveyed in the disclosure note forming part of the financial statements.

179. Having regard to the legal, accounting and regulatory framework noted above, which the CA (who is one of the senior most in the Audit Firm) was expected to be aware of, NFRA specifically notes the following statements made by the CA that indicate his inadequate understanding of the users of financial statements, the economic decisions that are taken by such users of the financial statements of public interest entities, and the cavalier attitude displayed by him in the discharge of his very onerous responsibilities.

a. "with regard to the alleged observation that the disclosure of NOF and CRAR was a material disclosure to the investors and lenders of an NBFC, it is worth noting that the only equity investor in IFIN was IL&FS, the parent entity, which, of course, was fully apprised of the matter".

b. "In addition, the Company made disclosures relating to the NOF/CRAR matter as part of the risk factors it included in its Offer Document when raising NCDs from the public starting in November 2017, promptly after learning of RBI's position ..... the arrangers to these issues were well known financial institutions, who would have been aware of the NOF/CRAR matter in light of the Company's disclosures".

180. The following exhibits have been submitted in the supplemental reply dated 20 July, 2020. The CA states that "these documents and submissions disprove the allegation of the Authority that I failed to obtain sufficient information regarding management's assessment of and response to RBI inspection matters".

a. Exhibit 6.2 - Company's response to RBI inspection report for FY 2011

b. Exhibit 6.3 for copy of the RBI inspection report for FY 2013

c. Exhibit 6.8.B - containing the extract of the minutes of the audit committee and board of directors, respectively, noting the discussion of the management with the RBI officials.

d. Exhibit 6.11- Letter written by the Company to RBI dated April 17, 2018 (Referenced in WP 29203 RBI matters)

e. Exhibit 6.12 - Letter written by the Company to RBI dated May 16, 2018 (Referenced in WP 29203 RBI matters)

f. Exhibit 6.20 - Company's letter to RBI dated May 24, 2016 (Referenced in WP 29203 RBI matters)

181. NFRA has examined the above exhibits. Exhibit 6.2 and 6.3 is proposed by the CA to support his submission that "there is no doubt that the Company's methodology was explicitly and transparently disclosed to RBI in various RBI filings and certificates, all without objection or concerns in the period leading up to 2016". He also claims, on the basis of these documents, that they "demonstrate that the RBI raised the matter of computing NOF / CRAR in 2016 and 2017 based on a new definition of that term". NFRA has considered this matter as such and there is no requirement of further evidence to support the claim. Other Exhibits are either already available in the audit file or are referenced in working papers forming part of the audit file. The matters submitted from these references have already been considered by NFRA.

C.6.3. Conclusion

182. As explained above, as well as in examination of replies to para 4 of Annexure II to the SCN, in the absence of any new factual or documentary evidences, that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 6.0 of Annexure II to the SCN are held as having been proved.

C.7. Examination of the reply to para 7.0 of Annexure II to the SCN

C.7.1. Summary of the Reply

183. The submission by the CA titled in the Index of Contents as "Detailed interim / pro tem response to paragraph 7.0 of Annexure II to the SCN" having pages numbered from 114 to 135 and the submission titled in the Index of Contents as "Exhibits referred to in the response to paragraph 7.0 of Annexure II to the SCN" having pages numbered from 805 to 830 relate to the para no. 7.0 of Annexure II to the SCN have been read with his supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

7.0 Actions/Omissions leading to misconduct in relation to evaluation of the Going Concern assumption (Reference: para 2.9 of the AQR Report).

7.1 The Engagement Partner had not obtained the Management's assessment of the applicability of the going concern assumption; consequently, no evaluation of such assessment has been made by him. The Engagement Partner had failed to capture the significance of the RBI Inspection Report and the non-compliance with the minimum NOF and CRAR requirements to continue the NBFC business and did not obtain sufficient appropriate audit evidence as required by the SAs, especially SA 570 (Revised), to evaluate the Management's assessment of the going concern assumption. The Engagement Partner has completely failed in displaying the required professional skepticism and failed in obtaining sufficient appropriate evidence in this matter to test and evaluate and report on the Going Concern assumption as regards the Company.

7.2 The Engagement Partner had admitted that the company had not made any assessment of the going concern assumptions. Also that the company had not forecast any future cash flows nor was any future action plan drafted. However, the Engagement Partner had concluded that considering the Indian bullish market and past trend of the performance of the company he was of the view that the going concern assumption was appropriate. As provided by SA 570 (Revised), the auditor was duty bound to discuss with the management the basis for the intended use of the going .concern assumption in a situation where the management had itself not performed such an assessment.

7.3 Further, SA 570 (Revised) also provides that when the management has not yet performed an assessment of the entity's ability to continue as a going concern, the Audit Firm shall request the management to make the assessment. No such request has been made by CA Udayan Sen.

7.4 Consequently, CA Udayan Sen completely failed to check applicability of going concern assumption and did not obtain sufficient and appropriate audit evidences as required by SAs, especially SA 570, (Revised). However, he went ahead with issuing an unqualified audit report confirming the management assessment ·of going concern in gross negligence of his professional duties.

7.5 Thus the above actions/omissions on the part of, CA Udayan Sen amount to professional misconduct of:

i. failure to obtain sufficient information regarding the going concern assumption, which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion (clause 8 of the Part 1 of the second schedule to the Chartered Accountants Act 1949); and

ii. failure to exercise due diligence in evaluation of going concern and being grossly negligent in the conduct of his professional duties by not complying with SA 570 (Revised) (clause 7 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

184. The CA denies all allegations as baseless. The observations by NFRA appear to have been made based on an incomplete reading or understanding of SA 570 (Revised) and completely ignore the relevant audit evidence available in the Audit files and therefore are untenable and/or erroneous.

185. He refers to paras 9, 10 and 11 of SA 570 (Revised) for a three steps procedure for assessing the appropriateness of the going concern assumption and reporting. He further states that the Engagement Team considered the entity's ability to continue as a going concern from the outset of the engagement both as part of the engagement acceptance and in the planning stages of the audit. IFIN's management itself had supported its going concern assumption in the Asset – Liability Maturity disclosure included in the financial statements.

186. He also states that IFIN's management itself had support for its going concern assumption in the Asset – Liability Maturity (ALM) disclosure included in the financial statements in Note 2.5 of Annexure II, and referred in Note 27 to the financial statements that the Engagement Team and he, along with the Joint Auditors, reviewed and analysed, as well". He states that the management's ALM Statement reflected the available assets and liabilities and expected positive cash flows in the following 12-month period. The Engagement Team similarly obtained the backups for the disclosure and evaluated the basis for preparation of such backups. The Engagement Team also checked that the policies for preparation and disclosure of ALM confirmed with the requirements of Prudential Norms.

187. He states that "as part of the audit, the Engagement Team, under my guidance and supervision, also considered and addressed the requirements of SA 570 relating to the evaluation of the appropriateness of IFIN's going concern assumption, and documented the performance of audit procedures to evaluate the appropriateness of the going concern assumption in WPs 29501 and 29502."

188. He further states that:-

a. During the audit, the Engagement Team, had obtained copies of the Minutes of both the Asset Liability Management Committee and Risk Management Committee and had not noted any matter which indicated an event or condition that would have cast a significant doubt on the ability of the entity to continue as a going concern. Directors Responsibility Statement also clearly asserted that IFIN's directors had prepared the annual accounts on a going concern basis.

b. Based on the Engagement Team's procedures, the Engagement Team reached the conclusion that it did not have reason to believe any material uncertainty existed related to events or conditions that cast significant doubt on IFIN's ability to exist as a going concern for the next twelve months and, therefore, management's going concern assumption was appropriate. The Engagement Team further noted that "the net worth is ~6 times the share capital of the company, which shows that the company is sufficiently covered."

c. Finally, as part of the Engagement Team's closing and subsequent events procedures, the Engagement Team again considered whether there were any conditions that may cast doubt on the entity's ability to continue as a going concern, and no such conditions were identified. The Company regularly had received the highest credit rating, it had access to credit facilities that it had not utilized, and it had not defaulted on any debt.

189. He further states that the Company had cash profit after taxes for the year ended 31st March 2017 and 2018. The Company's cash flow statement reflected positive cash flows. The Company had made provisions for NPAs and standard assets as per RBI norms. No circumstances existed that indicated a likelihood of any credit facilities being withdrawn by the bankers/financial institutions of the Company as on May 28, 2018.

190. He also states that the Company had not defaulted in repayment of any principal amounts and interest payable to lenders and had not defaulted in payment to other creditors.

191. He concluded that, in his professional judgement, he did not have reason to believe that any material uncertainty existed related to any events or conditions that may cast a significant doubt on the Company's ability to continue as a going concern for the next twelve months and therefore the Company's going concern assumption was appropriate.

C.7.2. Examination of the reply

192. The AQRR in para 2.9 had concluded unambiguously that:

a. "The Audit Firm has not attempted to rebut, and has, therefore, admitted the correctness of, the conclusion of the NFRA that there was no Management assessment of the entity's ability to continue as a going concern as required by SA 570 (Revised). Para 12 requires that the auditor shall evaluate Management's assessment of the entity's ability to continue as a going concern. Para A8 further adds that Management's assessment of the entity's ability to continue as a going concern is a key part of the auditor's consideration of Management's use of the going concern basis of accounting. As clearly provided by Para 10 (b) of SA 570 (Revised), the auditor was duty bound to discuss with the Management the basis for the intended use of the going concern assumption in a situation where the Management had itself not performed such an assessment. Even though the Audit Firm claims to have had a checklist based discussion with the Management on the entity's ability to continue as a going concern, the assessment is found to be completely insufficient."

b. "Further, Para 16 (a) of SA 570 (Revised) also provides that when Management has not yet performed an assessment of the entity's ability to continue as a going concern, the Audit Firm shall request the Management to make the assessment. No such request has been included in the Audit File"

c. "The Audit Firm has further mentioned that they have considered various factors like cash profits, positive cash flows, provisions for NPAs, positive net worth, et cetera to determine that no events or conditions existed as on that date that could cause significant doubt about the company's ability to continue as a going concern. However, none of these points have been analysed in Working paper 11102. There are no other references quoted by the Audit Firm where analyses of these factors are available in the audit file. Hence all this justification appears to be an afterthought by the Audit Firm with no backing whatsoever in the audit file."

d. "The evaluation of the going concern assumption as claimed to be done by the Audit Firm is found to be completely insufficient as a guide to future liquidity. It is not supported by any future cash flow statement or an analysis of adverse key ratios as required by Para A3 of SA 570 (Revised). The decrease in the Net worth of the company as on 31st March 2018 and the major reduction in the Profit earned during the year, were not given due importance. The Audit Firm failed to test the source of the cash generated and the company's ability to meet the immediately arising future liabilities."

e. "The "Asset Liability Management Maturity pattern of certain items of Assets and Liabilities", which has been disclosed in the financial statements by the Management is not a substitute for future cash flow analysis and is restricted to only certain items of Assets

and Liabilities. This disclosure is also in compliance of RBI directions only, and is not a substitute for what the Audit Firm needs to do as per SAs. The Audit Firm has not provided any evidence to show that they scrutinized or otherwise performed any procedures at all to review the cash flow forecasts for at least a 12-month period from the Balance Sheet date. No working papers or references in the audit file have been provided in this connection. The maturity pattern of certain assets and liabilities as disclosed in the notes to accounts of the Financial Statements has been prepared by the Management only. NFRA could not find any document at all in the Audit File to substantiate any kind of audit procedures performed by the auditor to evaluate the authenticity of any such information."

f. "The Audit Firm had failed to capture the significance of the RBI's inspection and report regarding non-compliance of minimum NOF and CRAR requirements to the continuation of IFIN in the NBFC business."

g. "The Audit Firm had claimed that the Management's plan for compliance with the NOF/CRAR requirements had been discussed with the Management. This claim had been found to be unsubstantiated. In response, the Audit Firm has been able to only point out to the minutes of the Audit Committee meeting held on 28th May 2018. This response only confirms the Draft Report's conclusion that the claim that such a compliance plan had been discussed with the Management is false for not being supported by any documentation. The significance of the compliance plan was enormous because this was the key to the continuation of the NBFC licence. NFRA is, therefore, reinforced in its conclusion that the Audit Firm was found totally wanting in complying with the requirements of SA 570 (Revised)".

h. "The Audit Firm has stated that as further evidence of discharge of their professional responsibility with regard to the going concern issue, an "Emphasis of Matter" paragraph was included in the audit opinion referring to the matter relating to companies in the same group as per RBI directions. Use of "Emphasis of Matter" paragraph to discharge responsibilities with regard to going concern basis is not supported by SAs".

i. "The Audit Firm was required to evaluate management's assessment of the going concern assumption and agree with it or disagree with it. The EOM Para does not do any such thing. No such argument was put forth by the Audit Firm at any stage in the protracted process of the AQR prior to this claim. There is no evidence adduced from the Audit File to show that the doubts, if any, about the going concern assumption were considered while deciding on the EOM Para. It is, therefore, dishonest and entirely misleading for the Audit Firm now to claim that the EOM Para is "further evidence of our discharging our professional

responsibilities" (page 300) with respect to the going concern matter. Such a claim, if anything, only betrays the Audit Firm's own doubts about the validity of the going concern assumption."

j. "The assertions in the Directors Responsibility Statement do not amount to an assessment by the Management of the going concern assumption, much less an evaluation of such an assessment by the Audit Firm".

193. Thus, it concluded that:

a. The CA has not obtained the Management's assessment of the applicability of the going concern assumption; consequently, no evaluation of such assessment has been made.

b. The CA did not obtain sufficient appropriate audit evidence as required by the SAs, especially SA 570 (Revised), to evaluate the Management's assessment of this assumption, such as it may have been.

c. The evidence indicates that there were serious doubts about the justification of the case of the Going Concern assumption in the present case. The CA has completely failed in displaying the required professional skepticism and obtaining sufficient appropriate evidence on this matter.

d. The CA, has clearly not complied with SA 570 (Revised).

194. On examination of the reply submitted by the CA, it is confirmed that his assertions and response are found not sufficient, not appropriate and not conclusive in support of having discharged his obligations to test and evaluate and report on the Going Concern assumption as regards the Company. The CA failed to provide any evidence to support his denial of charges. Rather, many of the submissions and evidences submitted by him in fact support and re-confirm the observations in the SCN and AQRR. A few such instance are detailed in the succeeding paragraphs.

195. He submits that "As part of the audit, the Engagement Team, under my guidance and supervision, also considered and addressed the requirements of SA 570 relating to the evaluation of the appropriateness of IFIN's going concern assumption, and documented the performance of audit procedures to evaluate the appropriateness of the going concern assumption in WPs 29501 and 29502. (Refer Exhibits 7.9 and 7.10)"

a. For audits of financial statements for periods beginning on or after April 1, 2017, SA 570 (Revised) is applicable. The workpaper 29501 'Going concern considerations' lists down the theoretical part of the standard procedure of the audit firm regarding assessment of going concern. It is a general document prepared based on SA 570. There is no mention about the SA 570 (Revised) in this work paper or in the reply of the CA.

b. Even though the workpaper 29501 lists down several procedures including the statement that "Management's assessment of the entity's ability to continue as a going concern is a key part of our consideration of management's use of going concern assumption [SA 570 A7]", none of these procedures are seen applied in practice as evident from workpaper 29502 'Going Concern Analysis'. The tests made specific to the audit are available in workpaper 29502. It contains only a table showing Net Worth, Profit after tax, Cash and Cash Equivalents for the period from 31st March 2014 to 31st March 2018 and the following observations:

   i. "Upon discussion with the management, DHS noted that company has not made any assessment of entity's ability to continue as going concern. Company has not forecasted any future cash flows nor any future action plan is drafted. Considering the Indian bullish market & past trend of the performance of the company, it is of the view that going concern is appropriate. Also company is not intended to liquidate the business or to cease the operation within foreseeable future."

   ii. "Company is NBFC engaged in the business of lending & syndication. Hence funding is the major requirement of company. DHS has verified the terms & conditions of borrowings & didn't observed any material breaches."

   iii. "Also company has obtained credit rating from various renowned institution, enabling company to borrow at lower rate of interest."

   iv. "DHS has reviewed minutes of the meetings of Board, Shareholders & Other Committee & didn't observed any thing which may cast doubt on going concern assumption."

   v. "From above it is observed that company is having positive Net Worth which is on increasing pace till the PY, but in the current year the networth has decreased. The company is earning profit consistently & is cash rich company. Also the networth is ~6 times the share capital of the company, which shows that the company is sufficiently covered. DHS, during the audit period, didn't came across any material

uncertainty in relation to event or condition which may cast significant doubt on entity's ability to continue as going concern. Hence going concern assumption is appropriate."

c. Thus, it is clear from these workpapers that the requirements of SA 570 (Revised), particularly, paras 12, 15 and 16 are not at all met. Without prejudice, the procedures performed do not even meet the requirements laid down in workpaper 29501 which is the theory as per SA 570.

d. There is no other audit evidence submitted by the CA in support of going concern analysis. All his other submissions are thus afterthoughts in his futile attempt to coverup the deficiencies in evaluation and reporting of Going Concern assumption.

e. There is a clear violation of para 12, and para A8 and A9 of SA 570 (Revised) in this regard. Para 12 stipulates that "the auditor shall evaluate management's assessment of the entity's ability to continue as a going concern' Para A9 explains that "it is not the auditor's responsibility to rectify the lack of analysis by management. In some circumstances, however, the lack of detailed analysis by management to support its assessment may not prevent the auditor from concluding whether management's use of the going concern basis of accounting is appropriate in the circumstances. For example, when there is a **history of profitable operations and a ready access to financial resources**, management may make its assessment without detailed analysis. In this case, the auditor's evaluation of the appropriateness of management's assessment may be made without performing detailed evaluation procedures if the auditor's other audit procedures are sufficient to enable the auditor to conclude whether management's use of the going concern basis of accounting in the preparation of the financial statements is appropriate in the circumstances" (Emphasis added). However, the CA ignored the fact that there is a consistent reduction in profitability of the auditee from the period ending 31st March 2014. The decline in profit is substantial during the reporting year and the preceding year. There was a sharp decline in cash and cash equivalents during the reporting year.

196. The CA stated that:

a. "Although the Engagement Team documented that IFIN had not made a formal assessment of its ability to continue as a going concern, the Engagement Team, considered the available information relating to its ability to continue as a going concern and again reached the conclusion that it had not "[come] across any material uncertainty in relation to event

or condition which may cast significant doubt on entity's ability to continue as going concern. Hence going concern assumption is appropriate.""

b. "Because the matter of compliance with the NOF / CRAR requirements would arise 12 months from the balance sheet date of March 31, 2018, the Engagement Team, under my guidance and supervision, considered and evaluated additional information about how the Company intended to address such matter that further supported our professional judgment that the Company's going concern assumption was appropriate."

197. Both the above statements are not supported by evidence. There is no such analysis made by the CA with respect to evaluation of going concern. Also, the statement that "the matter of compliance with the NOF / CRAR requirements would arise 12 months from the balance sheet date of March 31, 2018" is misleading. Though RBI had given time up to 31st March 2019 to comply with the NOF/CRAR requirements by reducing exposure to companies under the same group, the company had already initiated the process for reduction of the exposure to companies in the same group based on the RBI Directions. This fact is disclosed in the financial statements for FY 2018. As such, the compliance with NOF/CRAR was an ongoing process, which would culminate on 31st March 2019. The CA ignored the impact of this major obligation of the company in assessing going concern assumption.

198. Further, all the exhibits submitted by the CA, except Exhibit 7.9 (Going concern considerations) and Exhibit 7.10 (Going Concern Analysis) are not at all related to the audit procedure done for evaluation of Going Concern. Such exhibits are either workpapers relating to other audit procedures performed or evidence brought in now because of the afterthought to make good the serious deficiencies in evaluation of going concern assumption.

a. Exhibit 7.1 and 7.2 are extracts of ALM pattern and extracts of ALM disclosure summary – used for ALM analysis and testing disclosure of ALM in conformity with the requirements of Prudential Norms.

b. Exhibit 7.3.A Extracts of Minutes of the Audit Committee Meeting dated May 28, 2018 showing the action plan for achievement of RBI directives.

c. Exhibit 7.3.B. The minutes of the Company's Board meeting that demonstrate that the Board considered and discussed plans to comply with NOF / CRAR requirements by 31st March, 2019 in accordance with the RBI directions.

d. Exhibit 7.4 showing that IL&FS had raised equity capital in FY 2015 through rights issue, preference capital from public in FY 2015 and FY 2016. Source: Financial statement of ILFS.

e. Exhibit 7.5 - Extracts of memo for change in engagement risk to GTN.

f. Exhibit 7.6.A, 7.6 B and 7.11 are email communications not related to going concern analysis, and not forming part of audit file.

g. Exhibit 7.7.A – A January 11, 2018 corporate Announcement of ITNL - CNH 900 mn Notes offering by subsidiary of ITNL (Not a part of the audit file and not referenced in any WP).

h. Exhibit 7.7.B - A January 16, 2018 corporate Announcement of ITNL - CNH 100 mn Notes offering by subsidiary of ITNL (Not a part of the audit file and not referenced in any WP).

i. Exhibit 7.7.C - A January 18, 2018 corporate Announcement of ITNL – In principle approval of Board of ITNL for Masala Bond and USD denominated Bond (Not a part of the audit file and not referenced in any WP).

j. Exhibit 7.7.D - A November 30, 2017 corporate Announcement of ITNL - Arbitral award of claim to one subsidiary of ITNL (Not a part of the audit file and not referenced in any WP).

k. Exhibit 7.7.E - A September 18, 2018 corporate Announcement of ITNL - Settlement of claim with NHAI by one subsidiary of ITNL (Not a part of the audit file and not referenced in any WP).

l. Exhibit 7.7.F - A March 18, 2019 corporate Announcement of ITNL - Intimation of judgement on claim by High Court for one subsidiary for ITNL (Not a part of the EMS file and not referenced in any WP).

m. Exhibit 7.8 - Mandate from RIDCOR for refinance the loans of borrower group companies of Rs. 1,850 crores - Extract of Workpaper 26400.02 used for Fee Income testing.

199. Thus the statement of the CA that "Please refer to the paragraphs and table above, which demonstrate work performed and considerations made with numerous references to work papers which unambiguously and comprehensively establish that the work required to test the Going Concern assumption was performed appropriately and in compliance with professional standards" is a blatant untruth, since the references to work papers are not related to the work performed and

considerations made with respect to the evaluation of going concern assumption. Contrary to his statement, his assertions and response only go to confirm that he failed in discharging his obligations to test and evaluate and report the Going Concern assumption as regards the Company.

C.7.3. Conclusion

200. As explained above, in the absence of any new factual or documentary evidences, that have been submitted by the CA, and in the light of the discussion on the meaning and scope of "professional misconduct" as explained in the section on Legal Issues above, the charges in para 7.0 of Annexure II to the SCN are held as having been proved.

D. PENALTY

201. As discussed in detail in the above paras, the charges framed against CA U Sen in the SCN have been held to have been proved. The charges that were levelled against CA U Sen were as follows:

a. Article I: Committed professional misconduct as defined by Section 22 of the Chartered Accountants Act 1949 (no. 38 of 1949) read with clause 5 of the Part 1 of the Second Schedule to the said Act, which states that a CA is guilty of professional misconduct when he "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".

b. Article II: Committed professional misconduct as defined by Section 22 of the Chartered Accountants Act 1949 (no. 38 of 1949) read with clause 6 of the Part 1 of the Second Schedule to the said Act, which states that a CA is guilty of professional misconduct when he "fails to report a material misstatement known to him to appear in a financial statement with which he is concerned in a professional capacity".

c. Article III: Committed professional misconduct as defined by Section 22 of the Chartered Accountants Act 1949 (no. 38 of 1949) read with clause 7 of the Part 1 of the Second Schedule to the said Act, which states that a CA is guilty of professional misconduct when he "does not exercise due diligence, or is grossly negligent in the conduct of his professional duties".

d. Article IV: Committed professional misconduct as defined by Section 22 of the Chartered Accountants Act 1949 (no. 38 of 1949) read with clause 8 of the Part 1 of the Second Schedule to the said Act, which states that a CA 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".

e. Article V: Committed professional misconduct as defined by Section 22 of the Chartered Accountants Act 1949 (no. 38 of 1949) read with clause 9 of the Part 1 of the Second Schedule to the said Act, which states that a CA is guilty of professional misconduct when he "fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances".

202. According to Sec 132(4)(c) of the Companies Act, 2013, in a case where professional or other misconduct is proved, the NFRA shall have the power to make order for-

a. Imposing penalty of not less than one lakh rupees, but which may extend to five times the fees received, in the case of individuals; and

b. Debarring the member from 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 for a minimum period of six months or such higher period not exceeding ten years as may be determined by the NFRA.

203. The seriousness with which the Act views proven cases of professional misconduct is evident from the fact that a minimum punishment is laid down by the law.

204. There are several factors that go to what is the appropriate penalty in any case. These are discussed below with specific reference to the proved facts of this case.

a. **Loss of Independence of the Statutory Auditor**

i. The independence of the statutory auditor from the management of the company is the foundation of the institution of statutory audit. If this is compromised, there would be no case for a compulsory statutory audit at all.

ii. In this case, it has been clearly shown that the independence in mind and independence in appearance of the statutory auditor had been totally compromised. As Engagement Partner, it was the duty of CA Udayan Sen to take necessary

preventive action to ensure that his, and his Firm's, independence was not affected. He had been Managing Partner and CEO of Deloitte India for several years. His position in the Audit Firm, his standing in the profession, and his long experience, required him to be especially conscious of, and sensitive to, anything that could detract from his, and his firm's, independence. This background makes the violation of independence that has been proved even more serious than it would have been in the case of any other partner. This was a serious lapse in the discharge of his duty by CA Udayan Sen.

b. **Compliance with SAs and Maintenance of Audit Quality**

CA Udayan Sen's position, stature, and experience have been highlighted earlier. Given this, to insist that there could be more than one Engagement Partner for an engagement was to upend the SAs entirely. This certainly was one of the main reasons for the disastrous failure in audit quality that now stands proved. CA Udayan Sen has been clearly shown not to have done what was expected from him as the Engagement Partner. The primary function of the Engagement Partner is to provide the leadership and direction necessary to the engagement team to achieve the necessary audit quality, and compliance with SAs. The charges proved have shown the colossal failure of CA Udayan Sen to discharge this duty. A critical, questioning attitude, an unwillingness to be satisfied by merely superficial explanations, not concluding on material matters without rigorous verification from more than one angle, diligent and methodical cross verification, proper planning and the meticulous execution of the audit plan etc are fundamental to audit quality. Not only should the Engagement Partner have exhibited these qualities in the required measure, he should also have ensured the same in the rest of the Engagement Team as well. He has totally failed to do so.

c. **Promotion of Public and Investor confidence and Effectiveness in Deterring Auditors and Audit Firms from violating the applicable Accounting and Auditing Standards**

Audited financial statements are the basic inputs for innumerable transactions in the economy. A breakdown, or severe damage, to the trust and confidence that the public and investors have in financial statements would have ramifications that go far beyond the limited activities of an auditee company. As expert professionals, auditors are expected to judge the significance of the operations of the entity they audit for the larger financial and economic sectors and accordingly calibrate their

approach and procedures. Where the auditors have be shown to be negligent in considering these factors, appropriately severe penalties would follow. The misconduct of the type and scale that have now been proved would be severely damaging to Public and Investor Confidence. It is, therefore, essential that the penalty imposed has a suitable deterrent effect on other auditors and, at the same time, sends out a message to the Public and the Investor Community that such misconduct will not be allowed to escape lightly.

d. **Intentional Reckless Behaviour**

The evidence in the above paras shows clearly that the CA was not unaware of the Requirements of the SAs. He should have reasonably foreseen that the likely or actual consequences of his actions or inaction would amount to non-compliance with the SAs. This makes the professional misconduct very serious.

e. **Deterrence to Fraud and Collusive Behaviour**

Professional misconduct becomes very serious when the CA has gone along with the Management of the company in agreeing to misstatements/omissions so as to commit a fraud on the users of the financial statements. In this case, it is seen clearly that the company had actually incurred losses in the year 2017-18. It was only through such unacceptable/impermissible stratagems as the imputation of a value of Rs 184 crores to the Put Option on the TTSL shares that the actual incurred loss was turned into a reported profit. Besides, the fact that the company had ceased to comply with the stipulated NOF/CRAR norms was deliberately misstated. CA Udayan Sen went along with this attempt at fraudulent presentation of the financial statements. Hence, this would necessitate the imposition of a severe penalty.

NFRA Order No. NF-20012/1/2020
22nd July, 2020

ORDER

205. Considering all the above factors, NFRA makes the following order in terms of Sec 132(4)(c) of the Companies Act, 2013.

(i) A monetary penalty of **Rs Twenty Five lakhs** is levied upon CA Udayan Sen.

(ii) In addition, CA Udayan Sen is debarred for a period of **seven years** from 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.

Signed

(R. SRIDHARAN)
Chairperson

Signed

(PRASENJIT MUKHERJEE)
Member

Authorised for Issue

Vivek Narayan
Secretary NFRA

विवेक नारायण/VIVEK NARAYAN
सचिव/Secretary
राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण
National Financial Reporting Authority
भारत सरकार/Govt. of India
नई दिल्ली/New Delhi

Date: 22.7.2020
Place: New Delhi.

To,
CA UDAYAN SEN
(ICAI Membership No 31220)

Copy To

(i) Secretary, Ministry of Corporate Affairs, Government of India

(ii) Securities and Exchange Board of India

(iii) Reserve Bank of India

(iv) Institute of Chartered Accountants of India