NFRA Order No. NF-20012/1/2020
23rd 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: 23.07.2020

Important Note: In terms of the order passed by the Hon'ble Delhi High Court on 26th June, 2020, in C.M.No. 13478/2020 (directions) in W.P.(C)1522/2020 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 RUKSHAD DARUVALA (Membership No 111188)

A. BACKGROUND

1. A Show Cause Notice (SCN) was issued on 28th January 2020 to CA Rukshad Daruvala (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 Quality Control Reviewer **(EQCR)** in the statutory audit of ILFS Financial Services Ltd (**IFIN**) for the year 2017-18.

2. CA Rukshad Daruvala 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.1522/2020 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 letter dated 18th May.

   i. Considerable time had been already given to the CA to file his reply.

   ii. 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.

   iii. 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.

   iv. 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.

v. 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 to reply to the SCN.

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

vii. 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 in response to this letter of NFRA 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:

i. "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".

ii. "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."

iii. "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."

iv. "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."

v. "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."

vi. "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".

vii. "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. The CA submitted his reply vide Email Dated, Wednesday, 10th June 2020 11:47 PM having 8 attached documents in a compressed folder. 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, 13th June 2020 9:26 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-

i. As per the direction of the Hon'ble High Court (see para 9 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.

ii. 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.

iii. 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 complied with these directions of the court. He has not set out any specific documents that he could not produce and the effect thereof on his case. 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."

iv. However, vide email dated 20th July 2020, 5:07: 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 four issues related to para 2.0 of Annexure II to the SCN, 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".

v. 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 email, of 10 June 2020, has 8 attached documents in PDF format. Each of these documents was examined in detail. Attachment no. 1 is titled in the Index as "Preliminary / Prima

facie submissions in respect of the SCN" and contains pages numbered from 1 to 59. 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:

i. 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.

ii. 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, ("AQRR") 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 AQRR.

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

iv. 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.

v. 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.

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

vii. 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."

viii. 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 or ought to have appeared to a man of reasonable care and skill....".

ix. 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).

x. 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.

xi. 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 a 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 to by the CA very clearly says that the Audit Firm does not accept any of the findings of the AQRR. No reasoning whatsoever was given for this sweeping conclusion of theirs. Given this stand on the part of the Audit Firm, a meeting and/or discussion with DHS was not likely to have been productive of any result. Any meeting could have been 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 was 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 now 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:

    i. 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;

ii. 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;

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

iv. 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 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 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 he has presented have been carefully considered. In this connection, the Hyderabad High Court has said as follows 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.

36. 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 defence by a preponderance of the evidence".

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

    ii. 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 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.

40. A crucial para of the Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services 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."

41. The footnote to the sentence extracted in bold font above in para 40 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).

42. 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.

43. 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).

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

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

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

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

46. 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).

47. 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.

48. 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).

49. 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.

50. What has been stated above in para 49, as quotations from law lexicons, is a generalised proposition. This needs to be understood more specifically in the context of alleged professional misconduct by a CA, 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"?

51. **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.

52. **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.

53. **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 often at variance, if not in direct conflict, 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 to ensure independence 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).

54. **What is acceptable proof of the proper discharge of this duty of "due diligence"?** For the reasons explained in paras 17, and 44 to 48, 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 the logic of his own submissions.

55. 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 here 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 35 above, it is clear that the process followed by NFRA is valid in law.

56. 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".

57. 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.

58. 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.

i. All the judgments quoted and relied upon by the CA 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 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 that had happened subsequently.

ii. 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.

iii. The context of the case of Nanhelal vs Assistant Registrar, Co-operative Societies is totally different from the matters 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 by 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.

iv. 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.

v. 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

59. The CA then proceeds to provide article of charge -wise replies to the SCN. He states in para 50 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 50 and 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 order.

60. 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.

61. 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 submitted 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. The attachment to the email of 10 June, 2020, is 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 50 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

62. The attachment no.3 is titled in the index as "Detailed interim/pro tem response to paragraph 1.0 of Annexure II to the SCN" and contains pages numbered from 1 to 15. The attachment no.4 is titled in the index as "Exhibits referred to in the response to paragraph 1.0 of Annexure II to the SCN" and contains pages numbered from 16 to 33. Para 1.0 of the SCN relating to this reply is reproduced below for ease of reference.

> ***1.0*** *CA Rukshad Daruvala failed in his role as EQCR Partner to consider whether the Audit Report issued by DHS for IFIN is appropriate. He failed to review selected working papers relating to the significant judgments that the engagement team made and the conclusions they reached. He failed to perform an objective evaluation of the significant judgments made by the engagement team, and failed in evaluating the conclusions reached in formulating the Audit Report and considering whether the proposed Audit Report is appropriate. Thus he failed to comply the requirement of SQC 1 and SA 220.*

63. The reply of the CA states that since NFRA has not identified any specific matter in the AQRR based on which they have made this allegation, it is not practicable for him to provide a focused and specific response to this sweeping and unfounded allegation. It states that NFRA has applied the wrong standards and more generally has misinterpreted the role of the EQC reviewer. The standards for evaluating the EQCR team must be the actual standards that apply to EQC reviews, and not the standards that apply to audit engagement partners and audit engagement teams.

64. The reply further lists the requirements stated in SQC 1 and SA 220 for performing EQCR and maps each of the said requirements in paragraphs 64, 65 and 66 of SQC1 and paragraphs 20 and 21 of SA 220 onto the IFIN 2017-18 EQCR.. In the mapping table provided in para 1.5 of the reply,

the CA states that he had reviewed Engagement Team's (ET) assessment of Independence, the ROMMs identified by the ET, ETs judgments with respect to materiality and significant risks, matters communicated to those charged with governance (TCWG), had satisfied himself that the Audit Report issued was in compliance with the standards on auditing and Companies Act, 2013, held regular discussions with the Engagement Partner (EP) about the significant judgments which the ET had made and, as EQC Reviewer, had concluded that the documentation supported the conclusions the ET had reached.

65. He states that the EQCR process followed was documented, along with work papers/phases reviewed, in EQCR checklists and has referred to WP 30405 'Final Annexure 1' as evidence for the claim. He denies the alleged failure to review important working papers relating to significant judgments made by the ET team by referring to the details of work papers reviewed by the EQCR team as given in Exhibit 1. He cites three examples to illustrate that he performed an objective evaluation of the significant judgments by the ET.

66. The CA adds that as he had repeatedly discussed the manner of reporting the NOF / CRAR with the ET, and as he was involved in discussions with a technical specialist, and noted that ET had also obtained concurrence through the firm's internal consultation process for the EOM, he claims that the statement by NFRA that he failed in evaluating the conclusions reached in formulating the audit report is false and incorrect. He also denies the charge that he failed in his role as EQC Reviewer to consider whether the Audit Report issued was appropriate. He denies all the charges and states that he discharged his professional duty as the EQC Reviewer in accordance with SQC 1 and SA 220.

C.1.2. Examination of the reply

67. At the outset, attention is invited to para 4 to 7 of Annexure 1 to the SCN, wherein the applicable provisions of the SAs are detailed. Attention is also drawn to para 8 of the said annexure, wherein it is stated that the details of the evidences in support of the charges are provided in the documents listed in annexure III, especially in the AQRR and work papers files submitted in non-printable electronic format by the Audit Firm. Thus the AQRR dated 12th December 2019 provides the primary details in support of the charges in the SCN, and the AQRR is an essential part of this SCN. It may be noted that there are no comments by the Auditor regarding the said paragraphs of Annexure 1 to the SCN. Attention is also drawn to para 2 and 2.1 of Annexure I to the SCN, wherein the legally binding nature of SQC 1 and SAs is stated unambiguously. The CA has not raised any objections to this para of the SCN.

68. Para 1.0 of Annexure II to the SCN describes failure to follow the requirements of SQC 1 and SA 220. The failures are identified in the areas of :

    i. review of selected working papers relating to the significant judgments that the ET made;

    ii. performing an objective evaluation of the significant judgments made by the ET and evaluating the conclusions reached in formulating the Audit Report;

    iii. considering whether the Audit Report issued by DHS for IFIN is appropriate.

69. As mentioned in para 8 of annexure 1 to SCN, the CA must refer to the AQRR for details of evidences in support of these charges. Para 2.10 of the AQRR details instances of non-compliance of SAs and SQC1 with respect to the EQCR. Hence the contention of the CA in para 1.1 of attachment no.3 that NFRA has not identified any specific matter in the AQRR based on which the charges have been made, is incorrect.

70. Para 1.0 of Annexure II to the SCN refers to SQC 1 (Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements) and SA 220 (Quality Control for an Audit of Financial Statements). As the names indicate, and as specifically quoted by the CA in subsequent paragraphs of his reply, these standards apply to the work of an EQCR. Hence the contention of the CA in para 1.2 of attachment no.3 that NFRA has applied wrong standards, is incorrect.

71. In para 1.3 and 1.4 of attachment no.3 the CA states that the alleged failure to review important working papers is inconsistent with factual records. In support of this claim, para 1.5 lists out certain work papers claimed to have been reviewed by the EQCR Team. Para 1.6 (a) repeats the same matters as in the previous paras. However, the work papers mentioned as reviewed are those that were prepared by the ET during the engagement. The sole evidence in support of the claim that the CA had reviewed these work papers is produced in the form of the EQCR Checklist in the Audit File. The checklist just provides a Yes/No response to list of items to be reviewed. The EQCR partner is required to document reasons and the bases for his conclusions and not merely provide check box "Yes or "No" responses because of the following reasons identified in the AQRR specifically in para 2.10.6 (a) to (c). It is unambiguously concluded in the AQRR that "the EQCR partner was required to document reasons and the bases for its conclusions and not merely provide check box "Yes or "No" responses". The AQRR also concluded that "the review of multiple audit work papers and signatures on the same date without any kind of independent analysis and work papers show that the evidence of EQCR involvement is false and has been created subsequently". Therefore, the contention of the Audit Firm that "Para 25" of SA 220 requires only an affirmation from the EQCR on compliance with the statements is completely invalid" As there is no

documented evidence of reasons and bases of his conclusions on the review of work papers, the contentions in para1.3 to 1.6 (a) of attachment 3 are not acceptable.

72. In para 1.6 (b) the CA states that he had performed an objective evaluation of the significant judgments by the ET. In para 1.6 (c) he states that there was no failure on his part in evaluating the conclusions reached in formulating the audit report. However, there is no supporting evidence for the claims. The AQRR clearly points out the absence of objective evaluation in para 2.10.6 (b), which states " Even though the EQCR team has claimed to have reviewed multiple audit work papers, there is not a single paper in the Audit File where the EQCR has carried out independent analysis or review. Para 6 of SQC 1 defines "engagement quality control review" as a process designed to provide an objective evaluation, before the report is issued, of the significant judgments the ET made and the conclusions they reached in formulating the report. Thus, the process required objective evaluation and separate working needs to be done for the purpose of evaluation of significant judgments and to verify the results. The same was not done by the reviewer. It has been shown clearly above that SA 230 is applicable to the EQCR. Therefore, EQCR should have documented his working properly and separately from the working of the Audit team. Further, in the last submission given by the Audit Firm, they have admitted that EQCR has reviewed multiple audit work papers and signed the same as an evidence of review, which means that the EQCR did not perform any separate working to check the results of the ET". As the CA has not produced any evidence to prove his claims, the contentions are rejected.

73. In para 1.6 (d) the CA states that "I had concurred with the issuance of the audit report in the form it was issued by my firm based on discussions and communications with the Engagement Team, as well as work papers prepared by the Engagement Team that were reviewed by me and taking into account the concurrence received, as discussed in paragraph (c) above, through the firm's consultation process on the disclosure of the NOF / CRAR matter and the manner of reporting the same in the audit report. I deny that I failed in my role as EQC Reviewer to consider whether the Audit Report issued was appropriate." As summarized in para 3 of the SCN the AQRR identifies several areas of non-compliance by the Audit Firm with respect to the SAs, SQC1, Companies Act, 2013, Code of Ethics and RBI Regulations. By turning a blind eye to such large-scale non-compliances, the CA failed in his duty as EQC Reviewer. Thus, the charges in the SCN stand, as there are no evidences to the contrary.

74. The remaining para 1.7 in attachment no. 3 summarises the other paras and repeats the same matters as already detailed.

C.1.3. Conclusion

75. As explained above, in the absence of any 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

76. The attachment no.5 is titled in the index as "Detailed interim/pro tem response to paragraph 2.0 to 2.4 of Annexure II to the SCN" and contains pages numbered from 34 to 71. The attachment no.6 is titled in the index as "Exhibits referred to in the response to paragraph 2.0 to 2.4 of Annexure II to the SCN and contains pages numbered from 72 to 131. These relate to the para no. 2.0 of Annexure II to the SCN and have been read with the CA's supplemental reply dated 20th July 2020. The said para of the SCN is reproduced below for ease of reference.

> **2.0** The instances of violations of SAs, SQC 1, Code of Ethics and provisions of the Companies Act 2013, as brought out in the AQR Report are serious, in some cases deliberate, and shows absence of due diligence, gross negligence and dereliction of duty, among other misconducts, on the part of the Auditor. The EQCR Partner was grossly negligent in his duties and did not exercise due diligence in reviewing the work of the Engagement Team during the course of the Audit in which the Engagement Team had involved in several actions/omissions in the areas of compliance with independence requirements, communication with Those Charged With Governance (TCWG), evaluation of Risk of Material Misstatement (ROMM), the RBI Inspection Matters , presentation and valuation of Tata Tele Services Limited (TTSL) Shares and Derivative Asset, disclosure of Net Owned Funds (NOF) and Capital to Risk (Weighted) Assets Ratio (CRAR) and evaluation of the Going Concern assumption.

77. The CA denies the charges of gross negligence in his duties and not exercising due diligence in reviewing the work of the Engagement Team. He has detailed the specific procedures performed by him along with his EQCR team members in respect of the matters stated in the SCN para 2.0. As a result of his review and based on his professional judgment he states that he concluded that the ET's conclusions on independence were reasonable and supported by proper audit procedures. The reply goes on to say that the NFRA interpretation in the AQRR regarding independence is incorrect due to the reasons mentioned in his reply.

78. Regarding evaluation of independence he states that "overall evaluation of independence is the engagement team's responsibility. My responsibility as the EQC Reviewer was to consider the Engagement Team's evaluation of the firm's independence. While performing the engagement, the Engagement Team and engagement partner were not notified of any independence breaches through the Audit firm's systems of quality control nor were there in fact any independence breaches communicated to me while I served on the IFIN engagement as EQCR".

79. The CA contends that, as an EQCR Partner, he had ensured that all the significant matters identified during the course of audit had been communicated to management and TCWG, by referring to WP 30301 – "Audit Committee Presentation".

80. Regarding evaluation of ROMM, he states that "NFRA's contentions are expanding the scope, role and responsibilities of the EQC reviewer beyond what is prescribed in the professional standards. As an illustration, as per paragraph 65 of SQC 1 read with paragraphs 20 and 21 SA 220, my responsibility as an EQCR, inter alia, was to review the areas of significant risks and significant matters identified during the engagement and the responses to those risks and matters. It must be appreciated that the professional standards do not require an EQC reviewer to re-perform the audit or any of the Engagement Team's audit procedures, nor is the EQC reviewer required to review 100% of the audit risks. This is affirmed by paragraph 64 of SQC which states that "[An engagement quality control review] also involves a review of selected working papers relating to the significant judgments that the engagement team made and the conclusions they reached." The work papers claimed to be reviewed by EQCR team in this regard are listed in para 2.0.5.3. He therefore submits that he had exercised due diligence in reviewing the work performed by the ET.

81. In the matter of NOF/CRAR, he submits that he had exercised due diligence in reviewing the work performed by the ET, and that there is no question of any gross negligence in that matter. He lists Exhibit [2.0.5a and 2.0.5b], Exhibit [2.0.1], Exhibit [2.0.2] and Exhibit [2.0.1] in support of his claim.

82. The CA states that the matter of presentation and valuation of the Derivative assets were reviewed considering the significant judgment involved in valuation of such assets covered by the Guidance Note on Accounting for Derivatives issued by the ICAI. Fair value was duly recognised in the financial statements in accordance with the said Guidance Note. In this respect, he considered the ET's assessment of the Put Option, and also reviewed WP 23150.01.01A –'Memo on TTSL & Derivative Assets' and WP 23150.01.01.B 'FAS team clearance memo on derivative' and evaluated the ET's conclusions. He lists out 6 procedures performed in this regard. He has also stated that he independently concluded that the Put Option was an asset to be recognised as having value as of March 31, 2018, contrary to NFRA's assertion that the Put Option had no value. To support the claim, he refers to the FY 2017–18 balance sheet of IFIN where a value of Rs. 1,520.78 mn under "Derivative Financial Instruments" has been disclosed.

83. He has further said that he had reviewed the evaluation of the going concern assumption by reviewing WP 29502 and other relevant work papers regarding appropriateness of Going Concern assumption and considered the provisions of SA 570 (Revised) 'Going Concern' when performing his review. He further denies all charges made under para 2.0 of the SCN.

C.2.2. Examination of the reply

84. In para 2.0.1 of attachment no. 5, the CA denies all the charges in para 2.0 of Annexure II to the SCN. However no factual or documentary evidence is provided in support of the claims. In para 2.0.3 he describes the procedure followed for evaluation of independence requirements. He states that he evaluated the nature of independence threats considered by the ET. He further states that evaluation of independence is the ET's responsibility and as reviewer he did not find any independence breaches and therefore agreed with the ET's evaluation of independence. In subsequent paras he reiterates the reply provided by the Audit Firm in respect of the findings in the DAQRR regarding independence.

85. In para 2.2 of the AQRR, it was concluded, after considering the contentions of the audit firm that there were serious violations of independence requirements, since the Audit Firm had provided non audit services to either IFIN or its holding company. The AQR concluded that:

    i. the Audit Firm had grossly violated the provisions of Section 144 of the Companies Act, 2013;

    ii. The Audit Firm had been in serious breach of the Code of Ethics;

    iii. There had been a violation of the RBI Master Directions pertaining to mandatory rotation of the EP;

    iv. The above violations had undoubtedly fatally compromised the independence in mind required of the Audit Firm. The total fee for the 15 engagements listed in Annexure I of the AQRR 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 were from ILFS Ltd, the holding company of the group, or directly from IFIN, and did not include any of the several Engagements given by other Associates and Group Companies of IL&FS Group.

    v. Independence in appearance stood completely destroyed since no unbiased person could conclude, on an objective assessment of the circumstances, that there had been no abridgement of the auditor's independence; and

    vi. The Audit Firm's QC Polices and Practice relating to independence had been shown to be severely inadequate and not fit for purpose.

86. As there is no factual or documentary evidences provided to contradict the conclusions in the AQRR, the contentions of the CA in para 2.0.3 is not acceptable.

87. Similarly, in subsequent paras 2.0.4 to 2.0.9 of attachment no. 5, the CA denies all the charges in para 2.0 of Annexure II to the SCN. The para 2.0 points out that the instances of violations of SAs, SQC1, Code of Ethics and provisions of the Companies Act 2013, as brought out in the AQRR were serious, in some cases deliberate, and showed absence of due diligence, gross negligence and dereliction of duty, among other misconducts, on the part of the Auditor. The actions/omissions of the ET in the areas of compliance with independence requirements, communication with TCWG, evaluation of Risk of Material Misstatement (ROMM), the RBI Inspection Matters, presentation and valuation of Tata Tele Services Limited (TTSL) Shares and Derivative Asset, disclosure of Net Owned Funds (NOF) and Capital to Risk (Weighted) Assets Ratio (CRAR) and evaluation of the Going Concern assumption have been pointed out in the AQRR. However, in his reply the CA has reiterated that he was in full agreement with actions and the conclusions of the engagement team. He is unable to provide any evidence to prove that he in fact had challenged the decisions of the ET in the above areas and had done an objective analysis of these decisions. In the absence of such proofs, the contentions of the CA are not acceptable.

C.2.3. Conclusion

88. As explained above, in the absence of any factual or documentary evidences 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 to have been proved..

C.3. Examination of the reply to para 2.1 of Annexure II to the SCN.

C.3.1. Summary of the Reply

89. Para no. 2.1 of the SCN relating to this reply is reproduced below for ease of reference.

> **2.1** In particular, CA Rukshad Daruvala in his capacity as EQCR Partner has completely failed in documenting his work properly and separately from the work of the Audit team as required by SQC 1 and SA 230. He failed to do any independent analysis nor questioned the engagement team regarding issues arising out of RBI inspection and directions, failed to carry out review work on timely manner at appropriate stages of engagement, failed in appraising the quality of the work performed and failed to document various requirements as required by SA 220 (para 21).

90. The CA states that NFRA has not pointed to any specific matter in the AQRR based on which it has made this allegation. He further proceeds to state that SA 230 is not in the context of the EQCR and hence does not apply to his work. Only the documentation requirements in paragraph 25 of SA 220 need to be considered by the EQC reviewer. By referring to

Exhibit [2.1.1] he further states that his review is fully in accordance with the above requirement and it is carried out as per paragraph 70 of SQC1.

91. It is stated that the EQCR Team had spent 136 hours on engagement review (which constitute around 2.7% of total engagement hours which were more than 5000 hours) throughout the year from the planning phase until conclusion and reporting, as evidenced from the audit work papers the EQCR Team reviewed and other materials that demonstrate the EQCR Team's work.

92. It is stated that NFRA had failed to specifically identify and state the areas of work where the EQC Reviewer "failed to evaluate the documentation by the Engagement Team as required by para 21 of SA 220. However the reply states that he has complied with the requirements of paragraph 21 of SA 220 and in exercise of his professional judgment supported the conclusions reached by the ET with respect to the Significant Findings, including Significant Risks.

C.3.2. Examination of the reply

93. Para 2.10 of the AQRR details specific instances of non-compliance of SAs and SQC1 with respect to the EQCR. Hence the contentions of the CA in para 2.1.2 of attachment no.5 that NFRA has not identified any specific matter in the AQRR based on which the charges have been made, is incorrect.

94. In para 2.1.1 to 2.1.7 the CA reiterates the Audit Firm's argument at the DAQRR stage that the documentation requirements of SA 230 are not applicable to the EQCR. However, the AQRR has established beyond doubt that these arguments are not tenable. The AQRR concluded that:

> The line of argument taken by the Audit Firm is that SA 230 is applicable only to the auditor and not to the EQCR. However, Para 3 of SA 230 clearly states that Audit documentation serves a number of additional purposes including "enabling the conduct of quality control reviews and inspections in accordance with SQC1". The footnote to Para 3 gives references to Paragraphs 60, 63 and 65 of SQC1. Paragraph 60 of SQC1 relates to policies and procedures regarding EQCR. Para 63 is about the criteria for eligibility of EQCR. Para 65 brings out matter to be included in the EQCR including evaluation of firm's independence, significant risk identified during the engagement, judgements made particularly with respect to materiality and significant risk etc. Hence the argument of the Audit Firm that SA 230 is not applicable to EQCR is completely misplaced. Further, the definition of "Auditor" as given in SA 200 states that the term is used to refer to the person or persons conducting the audit, usually the EP or other members of the ET or, as applicable, of the firm. Thus, the term 'auditor' includes other persons which are conducting the audit and

are members of the firm. EQCR team members also carry out the audit of the client and are members of the firm. The definition gives EP as an example but does not restrict the scope to only to the ET. Further, the definition specifically intends that if a requirement or responsibility is to be fulfilled by the EP, the word "EP" is used. Hence, the SAs use the term "EP" or "EQCR" if it intends that as a requirement. Otherwise, the term "Auditor" is used. Even the Audit Firm in its presentation to management on 19th January, 2018 (WP 13902) has shown EQCR as Audit Support Team and part of ET.

95. As there is no new factual or documentary evidence to contradict the findings in the AQRR, the contentions of the CA in para 2.1.1 to 2.1.7 are not acceptable. For the same reasons para 2.1.8, which refer back to para 2.0.6 of the reply, is also not acceptable.

96. In para 2.1.9 the CA states that "The EQCR Team had spent 136 hours on engagement review (which constitute around 2.7% of total engagement hours which were more than 5000 hours) throughout the year from the planning phase until conclusion and reporting, as evidenced from the audit work papers the EQCR Team reviewed and other materials that demonstrate the EQCR Team's work". As evidence to prove the claim, he refers again to the list of work papers claimed to be reviewed by him. However, there are no log sheets provided by the CA to support the claim.

97. In para 2.1.11. the CA states that he has complied with the requirements of para 21 of SA 220 in all respects. Here again, he goes along with and support the conclusions reached by the ET. As mentioned in the previous sections, this claim is not accepted in the absence of objective evidences to prove objective analysis of the findings of the ET.

C.3.3. Conclusion

98. As explained above, in the absence of any factual or document evidences 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 2.1 of Annexure II to the SCN are held to have been proved.

C.4. Examination of the reply to para 2.2 of Annexure II to the SCN.

C.4.1. Summary of the Reply

99. Para no. 2.2 of the SCN relating to this reply is reproduced below for ease of reference.

> **2.2** CA Rukshad Daruvala in his capacity as EQCR Partner failed to prepare proper documentation related to discussion between EQCR Team and the Engagement Partner, in violation of SA 230 as detailed in Para 2.10.6 (a) of the AQR Report.

100. It is stated by the CA that "with regard to the contention in para 2.10.6 (a) of AQR Report, NFRA has provided its own definition for the term "auditor" which is not in accordance with SA 200, which very clearly states that individual persons would be considered to be an auditor if he/she is an engagement partner or a member of the engagement team. It does not refer to an EQC reviewer".

101. Further it is sated that the required documentation as per Paragraph 25 of SA 220 has been complied with by him in his review. Even ISA 220, which formed the basis of SA 220 does not require specific documentation of minutes of the discussion between the EQCR team and the engagement team.

102. He further concludes that NFRA's interpretation of the term 'auditor' and applying the same to the engagement quality control reviewer clearly violates, and is inconsistent with, the requirements in SQC1 regarding the engagement quality control reviewer and therefore is incorrect.

C.4.2. Examination of the reply

103. In para 2.2.1 to 2.2.6 of attachment no. 5, the CA repeats the claim that SA 230 is not applicable to EQCR and hence the documentation requirements are not applicable to him. However, this argument is not tenable in view of the reasons stated in para 94 above. Therefore, EQCR should have documented its working properly and separately from the working of the Audit team. The reply of the CA is hence not acceptable.

C.4.3. Conclusion

104. As explained above, in the absence of any factual or document evidences 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 2.2 of Annexure II to the SCN are held to have been proved.

C.5. Examination of the reply to para 2.3 of Annexure II to the SCN

C.5.1. Summary of the Reply

105. The para no. 2.3 of the SCN relating to this reply is reproduced below for ease of reference.

> **2.3** CA Rukshad Daruvala in his capacity as EQCR Partner 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.

106. It is stated by the CA that "I deny NFRA's allegations that I failed to review audit work papers. As discussed in more detail below, I personally reviewed audit work papers, as is expressly documented in work papers 30403, 30405, and 30406. Thus, NFRA's allegation that "there is not a single paper in the Audit File" that I reviewed is demonstrably false".

107. He further details that the term independent analysis has no legal or regulatory meaning for an EQCR and is not even mentioned in SQC1 or SA 220 in the context of EQCR. He was not required to carry out an independent analysis of the work papers, and NFRA is attempting to expand the responsibilities of an EQCR beyond the standard. He further states that he had performed the EQCR procedures as per the requirements of professional standards. Further, while performing such procedures he had reviewed/evaluated the respective section/work papers and documented his conclusion based on such review/evaluation in WP 30406 'EQCR closed Indent'.

C.5.2. Examination of the reply

108. It is stated by the CA in para 2.3.1 to 2.3.8 that he has reviewed multiple work papers. The supporting evidence is said to be the checklist designed by the firm and used by him in work papers 30403 'Planning EQCR', 30405 'Final Annexure 1' and 30406 'EQCR closed Indent'. However, as explained earlier, these work papers only provide Yes/No check boxes and is not an evidence for performing objective evaluation/review. Hence the claims of the CA are not acceptable.

109. It is also mentioned by the CA in the said paras that there is no requirement of independent analysis, since such a term has no legal or regulatory meaning for an EQCR and is not even

mentioned in SQC1 or SA 220 in the context of EQCR. In this regard the para 2.10.6 (b) of the AQRR mentioned in the SCN is reproduced below.

> Even though the EQCR team has claimed to have reviewed multiple audit work papers, there is not a single paper in the Audit File where the EQCR has carried out independent analysis or review. Para 6 of SQC1 defines "engagement quality control review" as a process designed to provide an objective evaluation, before the report is issued, of the significant judgments the ET made and the conclusions they reached in formulating the report. Thus, the process required objective evaluation and separate working needs to be done for the purpose of evaluation of significant judgments and to verify the results. The same was not done by the reviewer. It has been shown clearly above that SA 230 is applicable to the EQCR. Therefore, EQCR should have documented its working properly and separately from the working of the Audit team. Further, in the last submission given by the Audit Firm, they have admitted that EQCR has reviewed multiple audit work papers and signed the same as an evidence of review, which means that the EQCR did not perform any separate working to check the results of the ET.

110. It can be seen without any ambiguity that the terms "independent analysis" and "objective analysis" are used interchangeably in the AQR while the term objective analysis is used in SQC1. Hence the unfounded arguments around the absence of the term "independent" in SQC/SAs are not acceptable. Apart from this feeble argument the reply by the CA does not contain any evidence to prove that he has done an objective/independent analysis of the workpapers.

111. It is settled law that a professional must exercise reasonable care and must use his own judgment in making professional decisions. As it is admitted by the CA in his submissions that as EQCR partner, he only verified the working papers prepared by the ET without applying any independent or objective evaluation so as to arrive at his own judgment and not rely on those of others, it is clear that he has not exercised due diligence and is guilty of gross negligence.

C.5.3. Conclusion

112. As explained above, in the absence of any factual or document evidences 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 2.3 of Annexure II to the SCN are held to have been proved.

C.6. Examination of the reply to para 2.4 of Annexure II to the SCN

C.6.1. Summary of the Reply

113. The para no. 2.4 of the SCN relating to this reply is reproduced below for ease of reference.

> **2.4** CA Rukshad Daruvala in his capacity as EQCR Partner 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 24340). 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.

114. The CA has stated in his reply that "NFRA's improper attempt to expand the role of an EQCR beyond the professional standards is demonstrated by NFRA's use of the words "document reasons", "bases for conclusions" and "independent analysis." Again, none of these phrases is found in paragraph 25 of SA 220, or is elsewhere mentioned in SQC1 or SA 220 in the context of EQCR."

115. The CA has further said that "An experienced auditor would be able to understand the risks identified, the planned responses, procedures performed, audit evidences obtained and conclusions reached by the engagement team when conducting the EQCR. An experienced auditor would be able to review the checklist designed by the firm and used by me, to understand the procedures performed by me and my EQCR Team member. Contrary to NFRA's characterization, the checklist is detailed and descriptive. Moreover, it includes cross references to numerous other work papers that include the details of the audit work I and my EQCR Team member reviewed"

116. Regarding the work paper cited in the para 2.4 of the SCN, he states that the WP is a section of the audit program titled "Provision for General Contingencies" and the contention of NFRA is wholly misleading. He asserts that he obtained an understanding of the Company's General Contingency Provision ("GCP"), which was provided on the Company's assets over and above the provision required as per the RBI Prudential Norms. As such, in his professional judgment, he concurred with the ET's conclusions in this regard.

117. He further states that "The Standards of Auditing nowhere state or imply a requirement that an EQC reviewer attend Audit Committee Meetings. Nor would such a requirement make sense, as the engagement quality control reviewer is not even part of the engagement team and is not involved in any part of performing the audit."

C.6.2. Examination of the reply

118. In para 2.4.1 to 2.4.9 the CA reiterates the claims already made elsewhere and as summarised and already dealt with above. and denies the charges in para 2.4 of the SCN. The gist of the paras 2.10.6 (c), (d), (e), (f) and (g) of the AQRR, that forms the basis for para 2.4 of the SCN, is provided below:

i. Audit Firm's contention that SA 230 does not apply to the EQCR is violative of their own DAAM. Accordingly, the EQCR partner was required to document reasons and the bases for its conclusions and not merely provide check box "Yes or "No" responses. Therefore, the contention of the Audit Firm that Para 25 of SA 220 requires only an affirmation from the EQCR on compliance with the statements is completely invalid.

ii. The contention of the Audit Firm is that the involvement of EQCR can be proved from the signed working papers from the planning stage to the conclusion of the engagement. However, there is absolutely no record of any discussion held by the EQCR with the ET. There is no independent analysis carried out by the EQCR team. In fact, there are many papers which just show the opening and closing balances without any evaluation or analysis by the ET or the EQCR. For example, Working Paper 24340, Provision for General Contingencies, just shows an opening balance of Rs.450 crores and closing balance of Rs.275 crores. The reversal of Rs.175 crores from provision for general contingencies has not been explained in the Working Paper. The EQCR team has neither done any independent Analysis nor questioned the ET on the same. The conclusion is, therefore, inescapable that the profits for the year were inflated by Rs. 175 crores, without any basis or justification.

iii. Further, the Audit Firm has stated that communication with TCWG on all the RBI related matters were carried out through a Presentation to the Audit Committee (W.P. No. 30301) on 28th May 2018. On the same date, the audit was finalised, the accounts were approved by the Audit Committee, as well as the Board of Directors. The EQCR partner reviewed all the documents pertaining to the RBI matters and also reviewed and finalised all the closing documents including the 'EQCR close indent' and the final Auditors Report. However, the total man hours logged by the EQCR team on 28th May 2018 is just one hour. It may further be noted that the EP was in the Audit Committee meeting whereas the EQCR team was not part of the Audit Committee meeting. Hence any interaction between the EQCR team and EP was not possible on that day. This clearly shows that the exaggerated claims of Audit Firm of involvement of EQCR team is clearly farcical and an attempt to mislead NFRA.

iv. Thus, the EQCR has failed in appraising the quality of the work performed. The EQCR has also failed miserably in providing an objective evaluation of the significant judgements the ET made and the conclusions they reached in formulating the report. Thus, the Audit Firm has failed in complying with various provisions of SQC1, SA 220 and SA 230.

v. As shown above, the Audit Firm has completely failed to maintain documents as per SA 230. The EQCR has also failed to document various requirements as required by Para 25 of SA 220. The review of multiple audit work papers and signatures on the same date without any independent analysis and work papers show that the evidence of EQCR involvement is false and has been created subsequently. Hence, even though the refinement in the EQCR process that the Audit Firm intends to apply on the audits for the year ending 31st March, 2020 is appreciated, it would appear only to be an acknowledgement of the merit of the issues raised by NFRA.

vi. The EQCR has completely failed in documenting its working properly and separately from the work of the Audit team as required by SQC1 and SA 230;

vii. The contention of the Audit Firm that Para 25 of SA 220 requires only an affirmation from the EQCR on compliance with the statements is completely invalid;

viii. The exaggerated claims of the Audit Firm about involvement of EQCR team is clearly unsupported by evidence and is an attempt to mislead NFRA;

ix. The Audit Firm has failed in complying with various provisions of SQC1, SA 220 and SA 230;

x. The conclusion, therefore is inescapable that such EQCR as was, if at all, performed, was so perfunctory as to render it a complete sham;

xi. NFRA's comment in other portions of this AQRR are substantive evidence of the inadequacy of the EQCR system;

xii. The large scale failure of the EQCR process that comes out of the above analysis is also evidence of the inadequacy and ineffectiveness of the QC policies of, and their implementation by, the Audit Firm; and

xiii. The refinement in the EQCR process that the Audit Firm intends to apply is an acknowledgement of the merit of the issues raised by NFRA.

119. It is clear that the CA was not able to provide any documentary or factual evidence to contradict the above conclusions.

C.6.3. Conclusion

120. As explained above, in the absence of any factual or document evidences 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 2.4 of Annexure II to the SCN are held to have been proved.

C.7. Examination of the reply to para 3.0 and 4.0 of Annexure II to the SCN

C.7.1. Summary of the Reply

121. The attachment no.7 is titled in the index as "Detailed interim / pro tem response to paragraph 3.0 and 4.0 of Annexure II to the SCN" containing pages numbered from 132 to 137.The para no. 3.0 and 4.0 of the SCN relating to this reply is reproduced below for ease of reference.

> **3.0** Overall, the Engagement was performed 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 Audit Firm 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 Audit Firm issued 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 Auditor stated in his unmodified report that the audit was conducted in accordance with the standards of auditing, which is not true to the facts. All such instances are detailed in the AQR Report. By being a silent spectator to the entire process, the EQCR Partner failed to perform an objective evaluation of the significant judgments made by the Engagement Team, and the conclusions reached in formulating the Audit Report of IFIN.
>
> **4.0** 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 CA Rukshad Daruvala, being the EQCR partner, 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

122. The CA states that for each significant risk and for other areas involving significant judgment, he reviewed the work performed by the ET as required under SA 220. The review consisted of understanding the areas involving significant judgment, whether such areas were comprehensively identified by the ET, and reviewing the work performed by the ET in respect of such areas

and the conclusions reached. In his professional judgment, the work papers included the details required to conclude on the matters, in addition to discussions he had with the members of the ET.

123. With respect to the matters reported by NFRA in the AQRR, he submits that all such matters were considered as significant risk or significant matters involving exercise of professional judgment, in the performance of EQCR. He also reviewed the draft financial statements, the draft management representation letters, the outcome of the consultation on NOF/CRAR matter and the draft audit report and also had discussed with the ET, the plans of the management to comply with the NOF/CRAR norms by March 31, 2019 based on the agenda papers for the audit committee meeting on May 28, 2018. He lists certain work papers to support his claims.

124. Further he denies all the charges in para 3 and 4 of the SCN and states that " I discharged my obligation as EQC Reviewer by performed an objective evaluation of the significant judgments made by the Engagement Team and the conclusions reached in formulating the Audit Report of IFIN."

125. In the supplemental reply submitted on 20th July, 2020, the CA makes the following points based on the exhibits submitted along with this supplemental reply:

i. Extracts of minutes of the Board meeting dated 29th July, 2016 and a letter from the Company to the RBI dated 26th December, 2017, demonstrate that 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;

ii. Regarding RBI Inspections and Disclosure of NOF/CRAR, he seeks to rely on six documents. Two out of the six documents are excerpts related to the RBI inspection reports for FY 2011 and 2013, respectively, in which the RBI did not raise the issue of the definition of "companies in the same group," and therefore, these documents demonstrate that the RBI raised the matter of computing NOF /CRAR in 2016 and 2017 based on a new definition of that term. One document is minutes of the Board meeting that took place on 28th May, 2018, reflecting that the Board noted, without reservation, the representations in the minutes of meetings between management and RBI officials concerning the manner of disclosing NOF /CRAR in the financial statements. Further, two documents are letters from the Company to the RBI in 2018, which demonstrate that the Company requested permission to continue to disclose the NOF / CRAR pursuant to the Company's existing methodology until the year ended 31st March, 2019, and to make a disclosure of the same

in the financial statements. The sixth document is a letter from the Company to the RBI in 2016, which demonstrates the Company's analysis of and rationale behind its historical definition of "companies in the same group," and the legislative provisions on the definition of such term, thereby clarifying the Company's position on the issue.

iii. Regarding the TTSL shares and valuation of the derivative assets he seeks to rely on two documents. These documents are title deeds for land mortgaged by Hill County Properties, which support the ET'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, and the Signed Clearance Memo from Valuation Team for Derivative Assets.

iv. Regarding the evaluation of the Going concern assumption, he seeks to rely on one additional document. This is minutes of the Company's Board meeting demonstrating that the Board considered and discussed at length management's plans to comply with NOF / CRAR requirements by 31st March, 2019 in accordance with the RBI inspection report, and that the partners on the engagement from his firm, and the Joint Auditor, inquired into and gained an understanding of management's plan to ensure compliance with RBI requirements.

C.7.2. Examination of the reply

126. As far as the points made, and exhibits relied upon, in the supplemental reply are concerned, all these matters form part of the Audit File in one form or the other and have been duly taken into consideration in making this order. Nevertheless, point wise conclusions of the NFRA are as under:

i. As far as communication with TCWG is concerned, if the CA can only say that the TCWG were even otherwise aware of the RBI related matters, it is nothing but an open admission that the Audit Firm, and hence the CA, as EQCR Partner, pathetically failed in discharging their duties to communicate with TCWG as required by the SAs.

ii. As far as the definition, computation, and disclosure of NOF/CRAR are concerned, the matter has been discussed at length in the AQRR, and the total failure of the Audit Firm to discharge their responsibility has already been established. The documents now produced have been already taken into consideration, and they do not throw any different light on the issues.

iii. Regarding the verification of title deeds of HCPL, the CA has, in his supplemental reply dated 20th July, 2020, submitted Exhibit 3.1 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 3.1, 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. The EQCR Partner trying to pass this off as proof of the ET's verification of the original title deeds only serves to confirm his gross negligence and failure to exercise due diligence.

iv. Regarding the Going Concern assumption, the CA seeks to rely on one additional document. This is minutes of the Board meeting to show that the Board considered and discussed at length management's plans to comply with NOF/CRAR requirements by 31st March, 2019 in accordance with the RBI inspection report, and that the partners on the engagement from his firm and the Joint Auditor, inquired into and gained an understanding of management's plan to ensure compliance with RBI requirements. As has been conclusively demonstrated in the AQRR, the evaluation of management's use of the Going Concern assumption was riddled with numerous violations of the SAs. There is also no proof in the Audit File that the Engagement Team had done any evaluation of the compliance plan. Just to show the minutes as proof of the discharge of his duties by the EQCR Partner amounts to acceptance of the gross negligence and failure of due diligence with which he has been charged.

v. In the attachment no.7, the CA again reiterates the earlier contentions and refers to work papers prepared by the ET team and the check lists created by the EQCR Team. There is no additional evidences or facts submitted to prove the claims. Though he has detailed procedures allegedly performed, the contentions of the CA are not acceptable in the absence of any proofs in the Audit File for performing these procedures.

C.7.3. Conclusion

127. As explained above, in the absence of any factual or document evidences 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 and 4.0 of Annexure II to the SCN are held to have been proved.

C.8. Examination of the reply to para 5.0 of the SCN

C.8.1. Summary of the Reply

128. The attachment no.8 is titled in the index as "Detailed interim / pro tem response to paragraph 5.0 of Annexure II to the SCN; and Glossary" containing pages numbered from 138 to 141. The para no. 5.0 of the SCN relating to this reply is reproduced below for ease of reference.

> *5.0* The above actions/omissions of CA Rukshad Daruvala, therefore amount to professional misconduct of:
>
> i. 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); and
>
> ii. failure to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances (clause 7 of the Part 1 of the second schedule to the Chartered Accountants Act 1949).

129. The CA states that:

i. "While the auditor exercises such professional judgment, it is also a matter of common sense that there may be opinions contrary to the conclusions drawn by the auditor. I would like to draw your attention to several judicial pronouncements which establish that even if there are any errors of judgment in discharging of duties, the same cannot constitute misconduct unless ill-motive in the aforesaid acts are established"

ii. "The words "due diligence" have not been defined in the Code. Refer paragraph 39 and 40 of the cover letter to these response for a more detailed discussion on judicial pronouncements on what constitutes due diligence."

iii. "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."

iv. "In summary, and as detailed above, I fully complied with all Standards on Auditing relating to EQC review. I and my EQCR Team member performed work in all phases of the audit from planning through issuance of the opinion. I considered the significant judgments of the Engagement Team and determined, in the reasonable exercise of my professional judgment, that I found the Engagement Team's conclusions reasonable. I and my EQCR Team member also discussed significant judgments with the Engagement Team. This work is documented in accordance with the Standards on Auditing applicable to EQC reviewers.

C.8.2. Examination of the reply

130. The attachment no.8 is only a summary of the whole replies. It denies the professional misconducts pointed out in para 5.0 of the SCN. In this earlier paras of this order have discussed the legal issues involved and have clearly laid out the standards by which professional misconduct has to be assessed.

131. Thus it is established beyond doubt that the CA in his capacity as EQCR partner for the engagement had violated SAs during the performance of his duties and failed to discharge the duties as laid down in the SAs that are statutorily required from him. Such violations amount to gross negligence and professional misconduct as detailed in the SCN.

C.8.3. Conclusion

132. As explained above, as all the charges in the SCN are established beyond doubt, the professional misconduct detailed in para 5.0 of Annexure II, as well as in Articles I and II to the Show Cause Notice dated 28th January, 2020 is established against CA Rukshad Daruvala.

D. PENALTY

133. As discussed in detail in the above paras, the charges framed against CA Rukshad Daruvala in the SCN have been held to have been proved.

134. The charges that have been levelled against CA Rukshad Daruvala are as follows:

i. Article I: 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."

ii. Article II: 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".

135. 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.

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

137. 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.

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

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.

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 EQCR Partner, it was the duty of CA Rukshad Daruvala to highlight this situation and raise an alarm. Instead, he had chosen to remain silent, when it was his duty not to remain so. This was a serious lapse in discharging his duty as EQCR Partner.

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

The primary function of the EQCR partner is the maintenance of audit quality and the compliance with SAs. The charges proved have shown the colossal failure of the CA 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 EQCR Partner have exhibited these qualities in the required measure, he should also have highlighted inadequacies in these qualities on the part of the Engagement Team as well. He has totally failed to do so.

iii. **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 been 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.

iv. **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.

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

Professional misconduct becomes very serious when the CA has gone along with the Engagement Team and 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 and the reversal of the General Contingency provision 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. The EQCR Partner 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
23rd July, 2020

ORDER

138. 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 Five Lakhs** is levied upon CA Rukshad Daruvala.

(ii) In addition, CA Rukshad Daruvala is debarred for a period of **five 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

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: 23.7.2020

Place: New Delhi.

To

CA RUKSHAD DARUVALA

(ICAI Membership No 111188)

Copy to:

1. Secretary, Ministry of Corporate Affairs, Government of India
2. Securities and Exchange Board of India
3. Reserve Bank of India
4. Institute of Chartered Accountants of India