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

Order No.:021/2023 Date: 28.06.2023

ORDER

In the matter of M/s M H Dalal & Associates, Chartered Accountants (Firm Registration No 112449W) and CA Devang Dalal (ICAI Membership No 109049) under Section 132(4) of the Companies Act 2013 read with Rule 11(6) of National Financial Reporting Authority Rules 2018.

1. This Order disposes of the Show Cause Notice ('SCN' hereafter) of even no. dated 18.10.2022, issued to M/s M H Dalal & Associates and CA Devang Dalal (collectively Auditors hereinafter). CA Devang Dalal is a Member of the Institute of Chartered Accountants of India ('ICAI' hereafter) and was the Engagement Partner ('EP' hereafter) for the Statutory Audit of MAN Industries (India) Limited, Mumbai ('MIIL' or 'the Company' hereafter) for the Financial Year ('FY' hereafter) 2020-21.

2. This Order is divided into the following sections:

   A. Executive Summary

   B. Introduction & Background

   C. Major Lapses in the Audit

   D. Other Lapses in the Audit

   E. Lapses by the Audit Firm

   F. Findings on Articles of Charges of Professional Misconduct by the Auditors

   G. Findings on Additional Articles of Charges of Professional Misconduct by the Audit Firm

   H. Penalty & Sanctions

A. EXECUTIVE SUMMARY

3. National Financial Reporting Authority (NFRA) is India's independent regulator in respect of matters relating to accounting and auditing of prescribed class[1] of entities which can be broadly described as 'Public Interest Entities' (PIEs).

[1] Rule 3 of NFRA Rules, 2018

4. NFRA initiated action under Section 132(4) of the Companies Act, 2013 **(the Act)** for investigating into professional or other misconduct of the Statutory Auditor of MIIL, a company listed on BSE and NSE, following information received from Securities and Exchange Board of India **(SEBI)** vide letter dated 23.06.2022 regarding financial irregularities committed by MIIL.

5. MIIL's shareholding pattern in FY 2020-21 reflected substantial public interest with 57-58% of its shares held by the public, of which 32 -36% were held by individuals.

6. M/s M H Dalal & Associates **(the Firm)** was the Statutory Auditor of MIIL and CA Devang Dalal was the Engagement Partner **(EP)** for this Statutory Audit for the FY 2020-21. They had been Statutory Auditors of MIIL since 2017-2018.

7. On being observed that there was prima facie case for investigation by the National Financial Reporting Authority (NFRA), the Auditors were asked to submit the audit file and SQC 1 policy of the Firm. NFRA's investigations revealed a number of significant failures on the part of the Auditors. As a result, a Show Cause Notice (**SCN**) listing their failures and negligences was issued to the Auditors on 18.10.2022 in terms of Section 132 (4) of the Act read with Rule 11 of the NFRA Rules 2018.

8. The Auditors replied to the SCN on 05.12.2022 after availing of extension of time. The Auditors did not avail of the personal hearing offered to them.

9. The lapses in audit established in this Order have been organised into major lapses and other lapses and discussed in section C and D respectively of this Order.

10. The Auditors opinion on Standalone Financial Statements (SFS) that the Financial Statements reflected 'true and fair view' in accordance with accounting principles generally accepted in India and the provisions of the Act was false as the Financial Statements were materially misstated in view of the following:

    a) Financial Statements did not contain required disclosures mandated by Ind AS 24[2] and the Act, in respect of critical and sensitive information pertaining to Related Party Transactions. These include long outstanding balances of capital advances arising from conversion of loans into capital advances in earlier years, non-disclosure of full particulars of loans etc. **(para 32 and 35).**

    b) Disclosures in respect of Credit Risk Profile of Trade Receivables were erroneous and were not in compliance with requirements of Ind AS 107[3] **(para 46).**

    c) The impairment losses in respect of Trade Receivables (Rs. 96.58 crores), Other Assets (Rs. 35.66 crores), Investment in and Loans to subsidiaries (Rs. 8.56) were not adequate; despite the existence of indicators of high risk, impairment loss of Rs. 140.8 crores were not recognised; had they been, the reported PBT would have turned into a loss of at least Rs. 4.33 crores **(para 58 and 60).**

11. The Auditors 'Qualified' opinion on Consolidated Financial Statements (CFS) that the Financial Statements reflect 'true and fair view' except for the effect of non-consolidation

[2] Indian Accounting Standard 24, Related Party Disclosures (Ind AS 24)
[3] Indian Accounting Standard 107, Financial Instruments: Disclosures (Ind AS 107)

of a subsidiary, Merino Shelters Private Limited (MSPL) is erroneous, as the impact of the grounds for qualification was both material and pervasive which, as per Para 8 of SA 705, required the Auditors to give an adverse opinion **(para 50).**

12. The Auditors did not obtain Sufficient Appropriate Audit Evidence (SAAE) in a number of material account balances and class of transactions such as the following:

    a) Trade Receivables which constituted 37% of the total assets of MIIL and depicted adverse features indicating a significant risk of material misstatement (ROMM) **(para 56).**

    b) In respect of impairment test of investment in, and loan given to a subsidiary, the Auditors did not perform any audit procedures as required by SA 540 to evaluate whether the impairment test and documents given by the Company satisfied the requirements of Ind AS 36[4] **(para 60).**

    c) In respect of the Key Audit Matter (KAM) pertaining to valuation of MIIL's subsidiary, MSPL, the Auditors mentioned that it was done using the Discounted Cash Flow (DCF) method. However, the valuer's report available in the audit file mentions that the valuation was done using the Adjusted Net Assets Value methodology. This shows negligence and lack of due diligence by the Auditors in respect of a KAM **(para 60)**.

    d) The Auditors failed to perform a fundamental duty to attend the physical count by the management of inventory and other related procedures[5](**para 64).**

    e) The Auditors failed to identify the applicable Ind AS viz. Ind AS 115[6] and the presumption of risk of fraud[7] in recognition of revenue **(para 68 and 69).**

13. The Auditors made false statement in their report on the Internal Control over Financial Reporting (ICoFR), without testing their adequacy and operating effectiveness as required by the relevant Guidance Note of the ICAI **(para 73 and 74).**

14. The Auditors failed to demonstrate sufficiency and appropriateness of audit work in virtually every critical building block of an audit of Financial Statements i.e., Audit Strategy, Planning **(para 86 to 88),** Determining Materiality **(para 104 to 108),** identification and assessment of ROMM through an understanding of the entity's environment and internal control **(para 90 to 94)**, designing and performing audit procedures responsive to the ROMM **(para 98 to 101)** and evaluating the audit results.

15. This Order establishes that in view of the potentially high ROMM in the Financial Statements, and the dismal quality of the audit evidence as reflected in the audit work papers, the Statutory Audit of MIIL, instead of being an exercise in application of professional skill and care had degenerated into simply collecting and filing reams of photocopies of documents of routine nature (e.g., 2900 pages of Purchase/Sales Invoices) in the Audit Work Paper files. The audit work lacked demonstration of professional skepticism and sound knowledge of application of Ind AS and SAs and the Audit Firm

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[4] Indian Accounting Standard 36, Impairment of Assets (Ind AS 36)
[5] Standard on Auditing 501, Audit Evidence-Specific Considerations for Selected Items (SA 501)
[6] Indian Accounting Standard 115, Revenue from Contract with Customers (Ind AS 115)
[7] Standard on Auditing 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements (SA 240)

was grossly negligent in fulfilling its responsibilities of establishing a system of quality control[8] designed to provide it with reasonable assurance that the Firm and its personnel comply with professional standards and regulatory and legal requirements, and that the reports issued by the Firm and Engagement Partner(s) are appropriate in the circumstances.

16. In view of the above mentioned findings, this Order imposes the following Sanctions:

    i. Imposition of a monetary penalty of Rs.10,00,000/- (Rupees Ten Lakhs) upon CA Devang Dalal, who is also debarred for Five years from being appointed as an auditor or internal auditor or from undertaking any audit in respect of Financial Statements or internal audit of the functions and activities of any company or body corporate;

    ii. Imposition of a monetary penalty of Rs.50,00,000/- (Rupees Fifty Lakhs) upon M/s. M H Dalal & Associates.

B. INTRODUCTION and BACKGROUND

17. NFRA is a statutory authority set up under Section 132 of the Act to monitor implementation and enforce compliance of the auditing and accounting standards and to oversee the quality of service of the professions associated with ensuring compliance with such standards. NFRA has the responsibility to protect the public interest and the interests of the investors, creditors and others associated with the companies or bodies corporate that come under its purview. Under Section 132(4) of the Act, NFRA is vested with the powers of a civil court, and power to investigate the prescribed classes[9] of companies and impose penalty for professional or other misconduct of the individual members or firms of chartered accountants.

18. The Statutory Auditors, both individual and firm of chartered accountants, are appointed under Section 139 of the Act. The Statutory Auditors, including the Engagement Partners and the Engagement Team that conducts the audit are bound by the duties and responsibilities prescribed in the Act, the rules made thereunder, the Standards on Auditing (SA hereafter), including the Standards on Quality Control and the Code of Ethics, the violation of which constitutes professional or other misconduct, and is punishable with penalties prescribed under Section 132(4) (c) of the Act.

19. NFRA took up for investigation, under Section 132(4) of the Act, possible violations of the SAs by the Statutory Auditor of M/s MAN Industries (India) Limited (MIIL), a company located at Mumbai, on receipt of information from Securities and Exchange Board of India (SEBI) vide letter dated 23.06.2022 regarding financial irregularities committed by MIIL.

20. MIIL is a manufacturer and exporter of large diameter Carbon Steel Line Pipes for various high pressure transmission applications for Gas, Crude Oil, Petrochemical Products and Potable Water. MIIL has disclosed, as required under Ind AS 24,[10] total of three subsidiaries, the accounts of one of which has not been consolidated. MIIL is a

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[8] Para 3 of Standard on Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements (SQC 1).
[9] Rule 3 of NFRA, 2018
[10] Indian Accounting Standard 24, Related Party Disclosures

company listed on BSE and NSE and is categorized as a Small Cap company by Association of Mutual Funds in India (AMFI[11]) based on its average market capitalization of Rs. 385.30 crores during six months ended 31.12.2020. Table 1 below depicts certain key features of MIIL, the shareholding pattern of MIIL (showing substantial public interest), Revenue, PBT and Borrowings from banks for the FY 2020-21, FY 2019-20, and FY 2018-19:

Table 1

			(Numbers are in Rs. crores except percentages)
Particulars	**31.03.2021**	**31.03.2020**	**31.03.2019**
Shareholding Pattern			
Public	57.43%	57.49%	58.08%
Individual	36.07%	33.99%	32.68%
Revenue from Operations	2,075.18	1, 759.09	2, 215.39
PBT	136.47	66.24	86.98
Equity			
Borrowing from Banks	279.56	240.11	193.45

21. M/s M H Dalal & Associates (Firm) was the Statutory Auditor of MIIL and CA Devang Dalal was the EP for the Statutory Audit for the FY 2020-21.

22. On perusal of the SEBI report and preliminary examination of the Financial Statements of MIIL for FY 2020-21, it was observed that MIIL had not complied with a number of requirements of Ind AS and provisions of the Act in preparation and presentation of the Financial Statements for FY 2020-21. The Auditors were asked on 03.08.2022 to submit the audit file and SQC 1 policy of the Firm, which they did on 18.08.2022. On comprehensive examination of the audit file, it was prima facie observed that the audit had been conducted in disregard of most of the SAs and the relevant provisions of the Act. The EP had, however, issued, on behalf of the Audit Firm, an unmodified opinion in the Independent Auditor's Report for the SFS and a qualified opinion for the CFS, certifying that the Financial Statements (both SFS and CFS) of MIIL reflected true and fair view in conformity with the accounting principles generally accepted in India.

23. On satisfaction that a sufficient cause existed to take action under sub section (4) of Section 132 of the Act, a SCN was issued to the Auditors on 18.10.2022 under Section 132 (4) of the Act read with Rule 11 of the NFRA Rules 2018 asking them to show cause why action should not be taken against the Auditors for professional or other misconduct in respect of their performance of the audit of MIIL for FY 2020-21. The Auditors were charged with professional misconduct of:

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

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[11] On half yearly basis, Association of Mutual Funds in India (AMFI) publishes a list of all listed companies in India classified into three categories Large, Mid and Small Cap as per SEBI instructions.

(b) failure to report a material misstatement known to him to appear in a financial statement with which the EP is concerned in a professional capacity;

(c) failure to exercise due diligence, and being grossly negligent in the conduct of professional duties;

(d) failure to obtain sufficient information which is necessary for expression of an opinion, or its exceptions are sufficiently material to negate the expression of an opinion; and

(e) failure to invite attention to any material departure from the generally accepted procedures of audit applicable to the circumstances.

24. The Auditors vide letter dated 15.11.2022 requested for extension of time for submission of replies, which was granted up to 05.12.2022. The Auditors submitted their reply vide email dated 05.12.2022.

25. The Auditors did not provide satisfactory response to the charges in the SCN and have not accepted their alleged lapses detailed in the SCN. They have claimed that they have a due procedure for carrying out audit assignments which are in compliance with SAs; and that they followed an exhaustive and a thorough process before forming audit opinion. Part C and D of this Order discusses the replies to the charges in detail.

26. The Auditors did not avail the opportunity of personal hearing. Thus, this Order is based on review of the audit file, written responses of the Auditors and other material available on record. Each of the charges in the SCN is analysed and discussed herein below.

C. MAJOR LAPSES IN THE AUDIT

C.1. Lapses pertaining to Related Party Transactions

Conversion of Loan into Capital Advance to Merino Shelters Pvt. Ltd. (MSPL)

27. The SCN alleged that MIIL had not disclosed outstanding capital advance of Rs. 56.41 crores receivable from a related party viz., MSPL- a wholly owned subsidiary, in the Financial Statements for the three FYs 2018-19, 2019-20 and 2020-21. This non-disclosure by the Company was in violation of Ind AS 24[12]. It was alleged that the capital advance was in fact an outstanding loan to this related party that was converted into capital advance during 2017-18, without the approval of the Audit Committee of the Company, as required under Section 177(4) of the Companies Act 2013. The Auditors were charged with failure to identify and report non-disclosure of the outstanding capital advance that resulted in non-compliance with the requirements of Para 15 and 25 of SA 550[13].

28. In reply, the Auditors simply reproduced Para 15 and 20 of SA 550 and stated that in their understanding of Para 18 of Ind AS 24, only transactions undertaken during the

[12] Indian Accounting Standard 24, Related Party Disclosures (Ind AS 24)
[13] Standard on Auditing 550, Related Parties (SA 550)

periods covered by the Financial Statements have to be disclosed; and that MIIL had disclosed the transactions in the FY 2020-21 and the outstanding balances with its subsidiaries as on March 31, 2021. The Auditors have not referred to Auditor's obligations under Para 25 of SA 550 and why they have not complied with this para, which is germane to their professional misconduct presently under consideration. Para 25 of SA 550 requires auditors to evaluate whether the identified related party relationships and transactions are appropriately accounted for and disclosed as per the applicable financial reporting framework; and to evaluate whether their effects cause the Financial Statements to be misleading or prevent the Financial Statements from achieving a true and fair presentation.

29. We find that while the Company has disclosed other outstanding amounts of related party transactions which happened in previous years, such as investments in shares of related parties (subsidiaries) and the lease deposits (Refer Note 44 of SFS for FY 2020-21), but they have avoided disclosure of long outstanding unpaid loan converted into capital advance to related party for purchase of office premises. The Auditors failed to demonstrate professional skepticism to challenge the Company and to get to the bottom of the non-disclosure of a critical and sensitive information from the users' perspective.

30. The objective of related party disclosure is to draw attention to the possibility that the financial position and profit or loss of the preparer may have been affected by the existence of related parties and by transactions and outstanding balances with related parties, including commitments with such parties (Refer Para 1 of Ind AS 24). While laying down the purpose of related party disclosure, Para 6 of Ind AS 24 states that *"a related party relationship could have an effect on the profit or loss and financial position of an entity. Related parties may enter into transactions that unrelated parties would not. For example, an entity that sells goods to its parent at cost might not sell on those terms to another customer. Also, transactions between related parties may not be made at the same amounts as between unrelated parties"*. Therefore, disclosure of related party outstanding balances in a partial manner would be incomplete and misleading and if the view of the Auditors were to be accepted, the whole objective and purpose of the Ind AS 24 would be defeated.

31. The Auditors contention that two out of three members of Audit Committee of MIIL were the members of Board of Directors (BoD) and were also present in the BoD meeting that assented to the conversion reflects their poor understanding of the statutory requirements and their auditorial responsibility. Audit Committees are prescribed as mandatory for every listed public company and companies falling in specific categories mentioned in the Rules[14]. If the related party transactions are directly routed through the BoDs without consideration and recommendation of Audit Committee, the whole purpose and objective behind the statutory requirement of Section 177 of the Act of mandating the public interest entities to have Audit Committees would get defeated. Hence, the argument that the aforesaid transactions had the approval of the BoD is unacceptable. Further, the Auditors have failed to comply with the SEBI LODR requirements under Clause 23.

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[14] Section 177 of the Companies Act,2013 read with Rule 7 of Companies (Meetings of Board and its Powers) Rules,2014

32. The Auditors failure to ensure compliance with disclosure requirements of Ind AS 24, provisions of the Act and SEBI LODR requirements is a serious violation of professional standards especially as the related party transactions have historically been known to be a source of manipulation of financial position, siphoning of funds by the unscrupulous company promoters and management. We therefore conclude that the Auditors have violated Para 15 and 25 of SA 550. We note that the PCAOB, the US Audit Regulator, in its recent order15 in the Matter of Cheryl L. Gore, CPA, imposed sanctions and monetary penalty among other things for failure to act with due professional care and professional skepticism and failure to perform sufficient procedures to determine whether related parties and relationships and transactions with related parties were properly identified, accounted for, and disclosed in the Financial Statements.

Failure to report full particulars of loan to a Related Party

33. The Auditors were charged with violating Section 186 (4) of the Companies Act, 2013 by not reporting non-disclosure by the Company of full particulars of the purpose and utilisation of the loan of Rs 8.47 Crores receivable from a Related Party viz. MSPL, outstanding as on 31.03.2021.

34. Responding to the charge, the Auditors submitted that no loan had been given by the Company during the period under audit i.e., FY 2020-21, hence disclosure as required by the Section 186(4) of the Companies Act, 2013 is not applicable.

35. The reply of the Auditors is not acceptable as they were responsible for certifying the information presented in the Financial Statements of FY 2020-21. The reply indicates that their understanding of their obligation under Section 186 (4) of the Act is flawed. We observe that the Auditors have displayed similar lack of understanding in respect of disclosure requirements of Ind AS 24, as elaborated in earlier paragraphs of this Order. Therefore, we conclude that the Auditors failed to comply with their obligation under Section 186 (4) of the Act by failing to report the non-disclosure of full particulars of related party loan of Rs. 8.47 crore to MSPL, its purpose and utilisation..

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

36. The Company in its Annual Report for 2020-21 has disclosed loan to subsidiary and its repayment on net basis, which was not in accordance with requirements of Para 18 of Ind AS 24 that requires an entity to disclose the amount of the transactions entered into with a related party. The Auditors were charged with failure to comply with Para 15 & Para 25 of SA 550 by not reporting such non-disclosure as per Ind AS 24 which rendered the Financial Statements misleading.

37. As part of reply to SCN, the Auditors submitted the breakup of related party transactions disclosed on net basis in the Financial Statements regarding disclosure of loans given/received during the period under audit. In case of one subsidiary, the only transaction was receipt of loan of Rs 0.09 Crores and in case of another subsidiary there was a change in the balance of Rs 0.27 crores on account of foreign exchange rate fluctuations. Considering the amounts involved in these transactions, we are not

[15] Release No. 05-2021-020 dated December 14, 2021

proceeding further with this charge, while maintaining that the Auditors should have been alert to non-disclosure on gross basis.

C.2 Failure to report non-disclosure of material transactions

38. The Auditors were charged with not reporting the non-disclosure by MIIL of pledging of equity shares of its subsidiary MSPL amounting to Rs. 102.30 crores for obtaining credit facilities from South Indian Bank and thus violating Para 14 of Ind AS 107, [16] which requires that the carrying amount of Financial Assets pledged as collateral needs to be disclosed.

39. The Auditors submitted that the pledged collateral was in addition to the primary security (current assets) valuing Rs.1077.32 crores, constituting 66.29% of the total assets of the Company, whereas the value of the undisclosed shares of MSPL pledged as collateral security was only 5.71% of the total value of the assets and was immaterial to the users of the Financial Statements. They also referred to Note 25 to the SFS of MIIL which says that '*Working Capital facilities by banker's are secured by first pari passu charge on entire current assets and second pari passu charges on the immovable properties of the company.*'

40. The reply of Auditors that the disclosure was not required as these were only additional security over and above the primary security is not a valid ground for non-compliance with the disclosure requirements of Para 14 of Ind AS 107. Further, their argument that the value of pledged clollateral was immaterial as it was 5.71% of the total assets, is also unaccepatable in view of it being much higher than the generally accepted quantitative benchmarks of materiality of 1% to 2% of total assets. Further, the Auditorsreference to disclosure in Note 25 of SFS regarding charge created on the Current Assets and Immovable Property is irrelevant here. Accordingly, we conclude that the Auditors failed to exercise due professional care and to disclose a material fact known to them, which is not disclosed in the Financial Statements, but the disclosure of which is necessary in making such a Financial Statement, where he is concerned with that Financial Statement in a professional capacity.

C.3 Issues related to Credit Risk Exposures (Trade Receivables)

41. The Auditors were charged with failure to question the accounting policies relating to trade receivables, improper disclosures, failing to report non-disclosure of credit risk profile of the trade receivables by the Company as required by Para 35M and 35N of the Ind AS 107. Further, the Auditors were charged with non-compliance of SA 505[17] which required them to obtain external confirmations of outstanding trade receivables to ascertain accuracy, genuineness and recoverability of these balances.

42. The Company had disclosed at Note 49 in its Financial Statements that in respect of its trade receivables "*Our historical experience & collecting receivables is supported by low level of past default and hence the credit risk is perceived to be low*". This was despite the fact that it had written off substantial amount of trade receivables (51.14% of PBT)) as bad debts

[16] Indian Accounting Standard 107, Financial Instruments: Disclosures (Ind AS 107)
[17] Standard on Auditing 505, External Confirmations (SA 505)

during FY 2020-21, the period under audit, and the trade receivables constituted 36.88% of the total assets of the Company.

43. In their replies to the SCN, the Auditors have stated that 16.2% of the trade receivables were at risk indicating low risk and have given the following information about trade receivables:

Sr. No.	**Particulars**	**Amount (In lakhs)**	**Remarks**
1	Non-current		
a)	Unsecured	2,518.32	
2	Current		
a)	Secured	37,724.87	
b)	Unsecured	25,803.56	
3	Total unsecured (1a+2b)	28,321.88	Percentage = 42.88%
4	Total Secured (2b)	37,724.87	Percentage = 57.12%
5	Total trade receivables (3+4)	66,046.75	Percentage = 100%
6	Trade receivable dues under litigation		
(a)	Total amount receivable under litigation (Refer note no 42(a) to the financial statements)	13,324.46	
(b)	Litigation related to other matters (refer APB 4 pg 49)	3666.72	
(c)	Matter under litigation relating to trade receivables (6a-6b)	9657.74	
7	% to total unsecured receivables	34.10%	
8	Balance undisputed unsecured trade receivables	18664.14	
9	Receivable belonging to the Dubai branch (audited by other auditor)	8015.14	Recovered subsequently
10	Balance receivables from Indian Branch	10649.00	a) 90% of receivables are outstanding for less than one year as On 31.03.2021 b) Outstanding amount has been received as on signing of audit report for the FY 2021-22.
11	% of trade receivables risk to the total receivables	16.12%	Hence, low risk associate with trade receivables

This information/analysis has to be construed as an afterthought as none of these details were documented in the Audit Work Papers as required by Para 6 (b) of SA 230. All that is available in the Audit Work Papers is the Auditors' reliance on the company management representation that the outstanding trade receivables were fully recoverable, and no provision was necessary except for a provision for ECL of Rs. 2.14 crores as per Ind AS 109. Nevertheless, our analysis of this information/ explanation presented by the Auditors now shows some significant points of concern regarding the credit risk and impairment loss for trade receivables.

44. Apart from the fact that 16.12% of the total trade receivables stated to be at risk is a significant number, we find that 34.10% of the total unsecured trade receivables were under dispute/litigation; bad debts written off during the year were as high as 6.59% of the total outstanding receivables; the bad debts write off during last three years had increased from Nil in FY 2018-19 to 13.48% in the FY 2019-20 and to a staggering 51.14% of PBT in FY 2020-21. These figures are sufficient to raise red flags to an auditor, who will be expected to apply his professional skepticism to rigorously test any assertion made by the preparers in this regard. However, in the present case, we find that the Auditors have simply accepted what was asserted by the management, displaying lack of professional skepticism.

44.1 The Auditors, we also find, have not obtained sufficient appropriate evidence in respect of substantial amount of bad debts written off of Rs. 26.33 crores out of total bad debts written off of Rs. 69.33 crores.

44.2 In their reply to the SCN, the Auditors have questioned the PBT being used as benchmark to compare materiality of total bad debts written off. We note that Para A6 of SA 320[18] lays down overarching principle of determining materiality i.e., at five percent of PBT from continuing operations for a profit-oriented entity in a manufacturing industry and one percent of total revenue or total expenses for a not-for-profit entity[19]. Therefore, we consider the Auditors concern regarding the PBT being used as a benchmark is misplaced.

Errors in Presentation and Disclosures - Ageing Analysis of Trade Receivables

45. Para 22 of SA 530 requires that the auditor shall perform audit procedures to evaluate whether the overall presentation of the Financial Statements, including the related disclosures, is in accordance with the applicable financial reporting framework. The Audit Work Paper 'Debtor Ageing as on 31/03/2021[20]' gives a summary of party-wise outstanding balances segregated into Current and Non-current. Apart from the fact that the document does not indicate who prepared it, management or the Auditors, the balances included in the 'current' category have outstanding balances in the ageing buckets of 1 to 2 years (Rs 8.63 crores), 2 to 3 years (Rs 6.37 crores) and 3 years and above (Rs 3.59 crores). These ageing categories are expected to be presented in the non-current category as per Paras 66 and 68 of Ind AS 1[21] . The Auditors have failed to identify this anomaly and report appropriately. Our rough calculation shows that the amount of debtors more

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[18] Standard on Auditing 320, Materiality in Planning and Performing

[19] Refer report of the Committee of European Audit Oversight Body (CEAOB) on benchmarks for determining materiality threshold in the audit of public interest audits.

[20] Page 176 of audit file 2

[21] Indian Accounting Standard 1, Presentation of Financial Statements (Ind AS 1)

than a year old but classified as current is Rs.18.59 crores (1% of total assets). This indicates a material mis-statement to that extent in terms of Para A6 of SA 320.

Inadequacy of disclosures regarding credit risk exposure of trade receivables required under Para 35M and 35N of Ind AS 107

46. Absence of sufficient and appropriate disclosures regarding credit risk exposure of trade receivable i.e., provision matrix, the loss allowance percentage used and the loss allowance against each past due bucket and other risk evaluation tools e.g., credit risk grading used for the Financial Assets has resulted in material non-compliance with the disclosure requirements of Para 35M and Para 35N of Ind AS 107[22]. Ind AS Implementation Guidance- Example 12-Provision Matrix of Illustrative Examples of IFRS 9 Financial Instruments (extract given below) provides an illustration of the manner in which the credit risk exposure should be disclosed. We find that no such disclosure has been made by the Company and the Auditors have not reported this matter.

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

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

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

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

Therefore, in light of above, we conclude that the Auditors have failed to report in their audit report the non-disclosure of the credit risk profile of trade receivables as per Para 35 M and 35 N of Ind AS 107 and have therefore not discharged their duties under SA 505.

C.4 Failure to report non-consolidation of subsidiary

47. The Auditors were charged with failure to appropriately modify their opinion as per SA 705, even though the accounts of MIIL's subsidiary (MSPL) were not consolidated in the Financial Statements of MIIL. Note 44 of SFS shows MSPL as 100% subsidiary of MIIL. Accordingly, as per Ind AS 110, MIIL was required to consolidate the Financial Statements of MSPL in the CFS of MIIL.

48. The Statutory Auditors have qualified their Audit Report for non-consolidation of MSPL in the Financial Statements of MIIL. . MSPL was the wholly owned subsidiary of MAN Infra Projects Private Limited (MIPL), which in turn was the wholly owned subsidiary of MIIL. Pursuant to the Scheme of Arrangement approved by Hon'ble High Court of Bombay vide its order dated 20.03.2015[23], which was to be made effective from

[22] Indian Accounting Standard 107, Financial Instruments: Disclosures (Ind AS 107)

[23] Company Scheme Petition No. 658 and 659

01.04.2013, the shares held by MIPL in MSPL were to be transferred to MIIL and accordingly MSPL became 100% wholly owned subsidiary of the MIIL from 01.04.2013. MIIL has given effect to this Scheme of Arrangement in its Financial Statements for the FY 2014-15. However, MIIL has not consolidated the Financial Statements of MSPL for FY 2015-16 to 2020-21.

49. The Auditors replied that they had been informed of an ongoing legal dispute between the promoters in relation to the control of MSPL pending in Hon. Bombay High Court, and the consolidation of the financials of MSPL as a subsidiary of MIIL would not only lead to an incorrect disclosure but also result in contempt of the order of the Hon. Bombay High Court dated September 25, 2020. The Auditors submitted that they had relied on a legal opinion given by M/s. Kanga & Co to MIIL on 18.12.2015 wherein they had advised MIIL not to treat MSPL as a wholly owned subsidiary of MIIL and not to consolidate the financials of MSPL with MIIL till the time the legal proceedings were disposed of. Further, the Auditors stated that non-consolidation of MSPL barely had any material impact on the Financial Statements of MIIL and would not be pervasive in nature and therefore, not meriting an adverse opinion.

50. We observe that the audit file for FY 2020-21 as also the reply to the SCN, do not provide a copy of the order dated September 25 2020 of Hon. Bombay High Court, nor was there any evaluation of the legal opinion taken way back in 2015. It appears contradictory that the Auditors have issued a qualified opinion on account of non-consolidation of MSPL in MIIL while at the same time asserting that the consolidation would amount to contempt of Court. The impact of consolidation of Financial Statements of MSPL into that of MIIL would have been material and pervasive, as the assets and liabilities of MSPL constituted about 19.63% and 32.76% respectively of the assets and liabilities of MIIL as shown at Table 2. Para 8 of SA 705 requires the auditor to express an adverse opinion when misstatements, individually or in the aggregate, are both material and pervasive to the Financial Statements.

Table 2 **(In Rs. Crores)**

Particulars	**MIIL (Published Consolidated Financials) as on 31.03.2021**	**MSPL as on 31.03.2021**	**MSPL as % of MIIL**
Total Assets	1785.91	350.65	19.63%
Total Liabilities	951.03	311.56	32.76%
Net Worth	834.88	39.09	4.68%

In light of above, we conclude that the qualified opinion by the Auditors was without due diligence and sufficient appropriate audit evidence, and the Auditors have failed to comply with Para 8 of SA 705.

C.5 Failure to obtain Sufficient Appropriate Audit Evidence (SAAE).

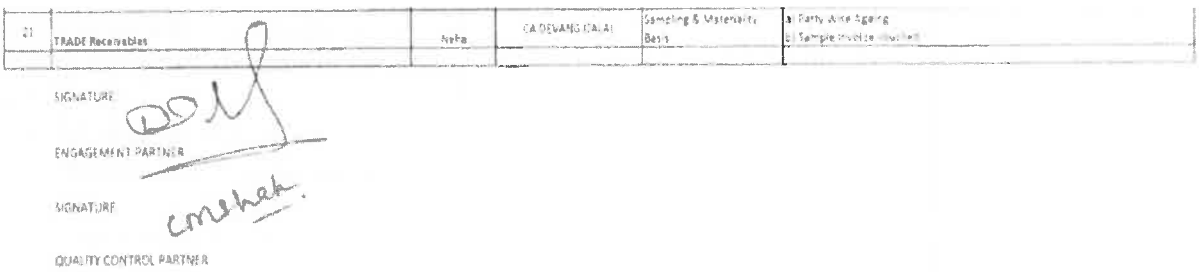
51. The Auditors were charged for failure to comply with SA 200[24] as they did not obtain reasonable assurance whether the Financial Statements were free from material misstatements and failed to obtain SAAE.

52. Responding to the charge, the Auditors submitted that they have sufficiently demonstrated that the allegations are unsustainable on account of the submissions made by them.

53. On perusal of the audit file, it is observed that the Auditors have failed to obtain SAAE in respect of a number of material account balances and transactions, some of which are explained below.

Trade Receivables

54. Trade receivables are 37%, 28% and 36% of the total assets of MIIL as of 31.03.2021, 31.03.2020 and 31.03.2019 respectively and therefore material and significant account balances that required the Auditors to obtain SAAE. However, the Auditors work documented in undated Audit Work Paper[25] shows only the signatures of the EP and Quality Control Partner. The information reproduced below has only the column headings but no work has been shown under the columns:



21	TRADE Receivables	Neha	CA DEVANG DALAL	Sampling & Materiality Basis	a) Party Wise Ageing b) Sample Invoice Vouched

SIGNATURE

ENGAGEMENT PARTNER

SIGNATURE

QUALITY CONTROL PARTNER

The Audit Work Papers also contain the following documents which are neither signed by any member of the Audit Engagement Team nor by any official of MIIL:

a) 1 Page of Debtors Ageing as on 31/03/2021[26]

b) 1 Page of Party-wise Ageing as on 31/03/2021[27]

c) Tax Invoices along with supported documents[28]

55. In the reply to the SCN, the Auditors have given incomplete details of the risk profile of the trade receivables, none of which was available in the audit files submitted. The deficiencies in the audit and weaknesses in these submissions have been discussed in Section C 3 above.

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[24] Standard on Auditing 200, Overall objectives of the Independence Auditor and the Conduct of an Audit in accordance with Standards on Auditing (SA 200).

[25] Page 21 of Audit File 1

26 WP Reference-Page 175 of Audit File 2

27 WP Reference- Page 176 of Audit File 2

28 WP Reference-Page 177-213 of Audit File 2

56. From Audit Work Papers shown at para 54, it can be noted that the audit work performed, comprises only three cryptic statements of two–three words such as Party wise, Sample Invoice Vouched and Sampling and Materiality Basis, which do not indicate the nature, extent and timing of the work performed to obtain SAAE expected from the auditor such as the following:

a) Nature of tests i.e., Test of Controls, Substantive Procedures such as Test of Details, Analytical Reviews.
b) Extent of audit work performed e.g., the sampling approach, sample sizes.
c) Timing of tests performed.
d) Audit steps performed to check the correctness of party wise ageing.
e) Identification of internal controls and its testing.
f) Results of audit steps performed, and its evaluation.

Recognition and measurement of Expected Credit Loss Allowance

57. Allowance for doubtful accounts is an example of accounting estimate other than fair value accounting estimates[29]. SA 540 lays down the audit requirements in respect of risk assessment procedures and related activities, identifying and assessing the risks of material misstatement, responses to the assessed risks of material misstatement, substantive procedures to respond to significant risks, recognition and measurement criteria, evaluating the reasonableness of the accounting estimates, disclosures related to accounting estimates and documentation etc. Certain critical requirements for audit of accounting estimates are as follows:

a) the auditor shall obtain an understanding of the following as per Para 8 of SA 540:

    i) The requirements of the applicable financial reporting framework relevant to accounting estimates, including related disclosures.

    ii) How the management makes accounting estimates, and an understanding of the data on which they are based, including the method or the model, used in making the accounting estimate, relevant controls, the assumptions underlying the accounting estimates. Whether there has been or ought to have been a change from the prior period in the methods for making the accounting estimates, and if so, why etc.

b) the auditor shall obtain SAAE whether management's decision to recognise, or to not recognise, the accounting estimates in the Financial Statements is in accordance with the applicable financial reporting framework? (Para 17 of SA 540).

c) whether the accounting estimates in the Financial Statements are either reasonable in the context of the applicable financial reporting framework, or are misstated? (Para 18 of SA 540).

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[29] (Para A6 of SA 540) Standard on Auditing 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures

d) the basis for the auditor's conclusions about the reasonableness of accounting estimates and their disclosure that give rise to significant risks and indicators of possible management bias, if any (Para 23 of SA 540).

58. In respect of understanding the recognition and measurement requirements of applicable financial reporting framework to trade receivables, there is no Audit Work Paper except a list of 37 Ind ASs[30], which is also incomplete as it misses out two critical Ind ASs viz. Ind AS 115[31] and Ind AS 116[32]. It is relevant to note that the trade receivables are Financial Assets within the scope of measurement requirements of Ind AS 109[33], which prescribes important requirements relating to impairment loss recognition and measurement based on Expected Credit Loss (ECL) approach. A key feature of ECL approach is to measure the ECL allowance after considering the information about past events, current conditions, and forecasts of future economic conditions[34] During the year under audit, the Company had recognized only a small amount of Rs. 2.14 crores as ECL allowance on trade receivables despite the fact that a substantial amount (Rs. 69.79 crores, constituting 51.14% of PBT), was written off as bad debts. As mentioned in para 41 to 43 above, trade receivables depicted high credit risk. Further, Note 42(b) of the SFS states that Rs. 133.24 crores of the outstanding dues are under dispute. Of these, Rs. 96.58 crores, constituting 37.42% of the unsecured trade receivables relate to trade receivables and Rs. 35.66 relate to other assets. Also, the Internal Audit Report for the year ending 31.03.2021[35] reported a large chunk of receivable of Rs. 85.19 crores being held up by the clients on account of delay in supply of pipes as per contractual delivery time. These facts and circumstances ought to have alerted the Auditors to apply professional skepticism about the potential material misstatement of accounting estimates in the context of the applicable financial reporting framework either due to possible management bias or flaws in the management methodology of accounting estimates. We observe that the same is lacking in the Auditors' work.

Had the Company recognized ECL allowance of Rs. 133.24 crores for these trade receivables/other assets under dispute, the PBT for FY 2020-21 would have been significantly lower than the reported PBT of Rs. 136.47 crores. Therefore, the failure of the Auditors to challenge the management decision of recognizing only a small amount of impairment loss allowance in respect of trade receivables was an act of gross negligence and displayed lack of due diligence.

Investments

59. The total Investments of Rs. 132.79 crores constitute 7.41% of the Total Assets of the Company. A significant part (99.52%) of these investments were classified as non-current investments and constitute 22% of the total non-current assets of MIIL as of 31.03.2021. Further, these non-current investments are primarily investments in equity shares of two subsidiaries viz. MSPL and Man Overseas Metal, DMCC.

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[30] WP Reference Ind AS Checklist page 37-38 of Audit File 1
[31] Indian Accounting Standard 115, Revenue from Contracts with Customers (Ind AS 115)
[32] Indian Accounting Standard 116, Leases (Ind AS 116)
[33] Indian Accounting Standard 109, Financial Instruments (Ind AS 109)
[34] Refer Para 5.5.17(c) of Ind AS 109
[35] WP Reference – Page #39 of Audit File 4

We observe from the audit file that the audit program document depicts the following work performed by the Auditor:

a) Valuation Report Checked[36]

b) Impairment testing done[37]

The screenshot of the same is reproduced below:

1	INVESTMENTS	Bhavesh	CA DEVANG DALAL	100%	a) Valuation report checked b) Impairment testing

In addition, the Audit Work Paper file contains the following documents:

(a) Investments in Subsidiary Ledgers[38]

(b) Category 1 Merchant Banker Valuation Report for MSPL[39]

(c) Credit Monetary Appraisal of Man Overseas Metal, DMCC[40]

Audit Work Paper titled 'Final Audit Points'[41] describes the discussion between the EP and the EQCR and their decisions to seek information for impairment test under Ind AS 36[42] for investments in two subsidiaries due to existence of impairment indicators and to include these as Key Audit Matters (KAM) in their Auditors Report. The Work Papers further state that the management has provided them with valuation report in case of MSPL and discounted cash flow statement in case of Man Overseas Metal, DMCC.

60. We observe from the Audit Work Papers the following major inadequacies and deficiencies in the audit work performed in respect of these material account balances:

60.1 There is no audit work performed to verify the existence of these investments.

60.2 In respect of the audit of impairment test of investments in MSPL, the Auditors have stated in the KAM part of the Auditor's report that the management has assessed the impairment by reviewing the business forecasts using the 'Discounted Cash Flow'(DCF) valuation method whereas the external valuer's report available in the audit file states that this impairment assessment was based on 'Adjusted Net Assets Value' method. This shows negligence and lack of due diligence on a matter that was raised by the Auditors as a KAM.

60.3 The Auditors did not perform any work to check whether the management applied the requirements of applicable financial reporting framework viz. Ind AS 36 and Ind AS 113[43].

60.3.1. Ind AS 36 requires the comparison of carrying amount of the assets with the recoverable amount; the recoverable amount is higher of its 'fair value less cost of its

36 WP Reference- Item #7, Page 21 of Audit File 1
37 WP Reference- Item #7, Page 21 of Audit File 1
38 WP Reference- Page 153-158 of Audit File 2
39 WP Reference- Page 159- of Audit File 2
40 WP Reference- Pages 170-173 of Audit File 2
41 WP Reference- Item #7, Page 21 of audit file 1
42 Indian Accounting Standard 36, Impairment of Assets (Ind AS 36)
43 Indian Accounting Standard 113, Fair Value Measurement (Ind AS 113)

disposal' and its 'value in use'. However, the valuation report only talks about determination of the fair value of the equity shares.

60.3.2. The Audit Work Paper titled 'Final Audit Points'[44] states the aggregate amount of exposure as Rs. 110.76 crores as against the fair value of equity investments of Rs. 102.20 crores. This is a clear case of impairment loss of Rs. 8.56 crores, which is 6.27% of PBT.

60.3.3 The Auditors did not check the suitability of the valuation report for Ind AS 36 purposes when the valuation report stated that it was meant for sale and income tax purposes.

60.3.4 As part of the Net Adjusted Value method for estimating fair value, the external valuer has used DCF method for one asset category in the form of real estate inventories. In these estimates, discount rates, cash flow forecasts, terminal value and industry/economic growth projections are critical determinants, but the Auditors have not checked whether these were in accordance with the prescription of Ind AS 36 and the source of data/information used was reliable or not.

60.3.5 The External Valuer has not used 'Comparable Companies Multiple Method' giving reasons as lack of exact comparable companies. However, he has used data of similar firms to determine the cost of equity to estimate the Weighted Average Cost of Capital to arrive at discount rates. This anomaly has not been questioned by the Auditors.

60.3.6 The Auditors were aware of the dispute among the promoters of MIIL regarding the value of assets and liabilities of MIPL, MSPL and claims on MIIL. These disputes have been claimed as the reason for not consolidating the Financial Statements of MSPL, which is subject to impairment test, into that of MIIL since 2015. However, the Auditors did not check and evaluate how these valuation disputes among promoters were factored in estimating fair value of MSPL.

60.3.7 In respect of impairment test of overseas subsidiary viz. Man Overseas Metal, DMCC, the Audit Work Papers contain a few pages with initials of an unknown person with the title 'Credit Monetary Appraisal' and give details of valuation based on DCF. There is no evidence of any audit work done to check the accuracy and validity of these amounts keeping in mind the requirements of Ind AS 36.

61. In view of the above deficiencies in the audit work performed i.e., simple collection and filing of the documents without any application of an enquiring mind of the auditor, in respect of material account balances, the Auditors have been grossly negligent in performing their professional duties and failed to identify and report material misstatements in the SFS of the Company. Thus, the impairment loss of Rs. 8.56 crores has not been recognized resulting in overstatement of PBT of the Company and the carrying amount of investments.

Inventories

62. The closing balance of Inventories is 27.92% of Total Current Assets of MIIL as of 31.03.2021 and therefore is a material significant account balance. The Audit Work Papers and the work performed by the Auditors are as follows:

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[44] WP Reference- Item #7, Page 21 of Audit File 1

(a) Anjar Plant - Stock summary with supporting[45]

(b) Pithampur Plant - Stock Summary with supporting[46]

(c) Valuation provided by management Checked[47]

(d) Scanned bill of Inventories verified[48]

63. According to SA 501[49], Inventories is one of three items that require special consideration by the auditor and this SA requires certain specific audit procedures highlighted below:

63.1 The Auditor's attendance at physical inventory count, unless impracticable, to evaluate of management's instructions and procedures for recording and controlling the results of the entity's physical inventory counting; inspect the inventory and perform test counts.

63.2 Perform alternative audit procedures in case the attendance at physical inventory count is impracticable.

63.3 In case of inventory under the custody and control of third party, obtain confirmation from third party and perform inspection or other procedures.

64. We observe from the extract of Audit Work Paper, exhibited below, that the document containing the Valuation of Stock is not authenticated raising doubts about its authenticity and reliability.

Man Industries (India) Limited, Anjar

Valuation of Stock as on 31ST MAR 2021

PARTICULARS	ANJAR			TOTAL		
	Qty (MT)	Avg	Value	Qty (MT)	Avg	Value
INVENTORIES (As certified by the Management)						
i) Raw Materials						
INVENTORIES RAW MATERIAL	26,960	44,793	1,207,643,830	26,960	44,793	1,207,643,830
INVENTORY OTHER RM - COATING MATERIAL			395,295,459			395,295,459
INVENTORY CONSUMABLES (BARE PIPE ORM)			179,479,656			179,479,656
INVENTORY STORE & CONSUMABLES			189,721,981			189,721,981
	26,960		1,972,140,925	26,960		1,972,140,926
ii) Work In Progress						
INVENTORY WORK IN PROGRESS	9,047	45,303	409,864,314	9,047	45,303	409,864,314
			-			-
	9,047		409,864,314	9,047		409,864,314
iii) Finished Goods						
INVENTORY FINISHED GOODS	6,763	66,847	452,089,988	6,763	66,847	452,089,988
INVENTORY SCRAP	211	16,000	3,383,254	211	16,000	3,383,254
	6,975		455,473,243	6,975		455,473,242
TOTAL	42,982		2,837,478,481	42,982		2,837,478,482

[45] WP Reference 214 to 336 Audit File 2
[46] WP Reference 337 to 347Audit File 2
[47] WP Reference- Item #6, Page 21 of Audit File 1
[48] WP Reference- Item #6, Page 21 of Audit File 1
[49] Standards on Auditing 501, Audit Evidence-Specific Considerations for Selected Items (SA 501)

We note that there is no evidence of the Auditors presence at the inventory count by the management, as required under the Standards. Also, the Audit Work Papers like the one reproduced above, are evidence of the gross negligence of the Auditors in performing their professional duties to obtain SAAE in respect of inventories. We note that the inventories have historically been a source of misstatement and manipulation of the Financial Statements and therefore we find that the Auditors have been grossly negligent in performing their duties in respect of the audit of inventories.

Trade Payables

65. Trade Payables constitute 54.12% of Total Liabilities of MIIL as of 31.03.2021 and therefore are a material account balance. The Audit Work Papers consist of 1 Page of Vendor Ageing[50] , a list of outstanding vendors as on 31.03.2021[51], and 2800 pages of Purchase Invoices[52] .

66. The deficiencies in the audit work are similar to those mentioned in respect of Trade Receivables (refer para 56). The audit work is merely collection and filing of reams of photocopies of purchase invoices without any analysis and application of mind. The Auditors were so negligent that they have not even bothered to ensure that the audit document they obtained and relied upon were authenticated by the Company Management as can be seen from the following reproduced work paper:

Vendor Agieng FY 20-21				
Perticulars	MSME	Non Current	OTHER THAN MSME	Grand Total
less than 180days	70,537,527	-	3,486,964,536	3,557,502,063
6 months - 1year	4,641,310	1,636,918	1,574,729,005	1,581,007,233
1 year to 2 years	1,030,303	1,146,660	5,921,830	8,098,793
2 years - 3 years	5,948,865	1,408,131	7,741,424	15,098,421
3 years and above	1	4,252,653	17,730,528	21,983,182
Grand Total	82,158,005	8,444,362	5,093,087,323	5,183,689,690

Revenue

67. Revenue from operations is a material class of account in the audit of any company. The audit work performed by the Auditors, reproduced below, shows hardly any audit work done.

9	Sales	Bhavesh	CA DEVANG DALAL	High Value & Random	a) Sample Scanned invoices vouched b) Reconciliation of Sales with GST Returns provided by management checked

Most of the audit deficiencies are similar to those mentioned in respect of Trade Receivables at **para** 56 of this Order.

68. The Auditors work paper exhibited below regarding compliance with the applicable financial reporting framework has no mention of the standard applicable to Revenue i.e., Ind AS 115.

[50] Page 748 Audit File 2
[51] Page 749 to 763 Audit File 2
[52] Page 764 to 3558 Audit File 2

CHECKLIST FOR ACCOUNTING STANDARDS

CLIENT: Man Industries (India) Limited
Audit Period : F.Y 2020-21
INDIAN ACCOUNTING STANDARDS CHECKLIST CONTROL SHEET

IND AS	COMPLIANCE WITH ACCOUNTING STANDARDS	Y/N/NA
Ind AS 101	First time adoption of IND AS	No
Ind AS 102	Share Based Payment	No
Ind AS 103	Business Combination	No
Ind AS 104	Insurance Contracts	No
Ind AS 105	Non Current Asset held for Sale and Discontinued Operations	No
Ind AS 106	Exploration for and Evaluation of Mineral Resources	No
Ind AS 107	Financial Instruments : Disclosures	Yes
Ind AS 108	Operating Segments	No
Ind AS 109	Financial Instruments	Yes
Ind AS 110	Consolidated Financial Statements	Yes
Ind AS 111	Joint Arrangements	No
Ind AS 112	Disclosure of Interest in Other Entities	No
Ind AS 113	Fair Value Measurement	Yes
Ind As 114	Regulatory Deferral Accounts	No
Ind AS 1	Presentation of Financial Statements	Yes
Ind AS 2	Inventories	Yes
Ind AS 7	Statement of Cash Flows	Yes
Ind AS 8	Accounting Policies, Changes in Accounting Estimates and Errors	No
Ind AS 10	Events occurring after Reporting Period	No
Ind AS 11	Construction Contracts	NA
Ind AS 12	Income Taxes	Yes
Ind AS 16	Property Plant & Equipment	Yes
Ind AS 19	Employee Benefits	Yes
Ind AS 20	Accounting for Government Grants and Disclosure of Government Assistance	No
Ind AS 21	The Effects of Changes in Foreign Exchange Rates	No
Ind AS 23	Borrowing Costs	Yes
Ind AS 24	Related Party Disclosures	Yes
Ind AS 27	Separate Financial Statements	Yes
Ind AS 28	Investments in Associates & Joint Ventures	No
Ind AS 29	Financial Reporting in Hyper inflationary Economies	No
Ind AS 32	Financial Instruments : Presentation	Yes

69. Para 26 of SA 240[53] states that when identifying and assessing the risks of material misstatement due to fraud, the auditor shall presume that there is risk of fraud in revenue recognition. Para 47 of SA 240 further states that when the auditor has concluded that the presumption is not applicable in the circumstances of the engagement, he shall rebut the presumption and shall document the reasons for the conclusion. However, no such documentation exists in Audit Work Papers.

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

70. The Auditors have expressed unmodified opinion on the adequacy and operating effectiveness of Internal Financial Controls Over Financial Reporting (ICoFR) as at March 31, 2021. The Auditorss opinion further states that they have conducted audit in accordance with the Guidance Note on Audit of ICoFR (the "Guidance Note") and the Standards on Auditing deemed to be prescribed under Section 143(10) of the Act to the extent applicable to an audit of internal financial controls.

71. Para 16 of Section II of the Guidance Note states that a benchmark system of internal control, based on suitable criteria, is essential to enable the management and auditors to assess and state adequacy and compliance of the system of internal control. Para 17 of the Guidance Note mentions that the requirements in Appendix 1 of SA 315 provide necessary criteria for ICoFR.

72. Section IV of the Guidance Note prescribes technical guidance on audit of ICoFR. Some of the critical prescriptions are:

[53] Standards on Auditing 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements (SA 240)

72.1 While the auditor should combine the audit of ICoFR and the audit of Financial Statments, the objectives of the audits are not identical. However the auditor must plan and perform the work to achieve the objectives of both audits.

72.2 The auditor should design his or her testing of controls to accomplish the objectives of both audits simultaneously:

72.2.1 To obtain sufficient evidence to support the auditor's opinion on ICoFR as of year-end, and

72.2.2 To obtain SAAE to support the auditor's control risk assessments for the purposes of the audit of Financial Statements.

72.3 Planning the audit, role of risk assessment, addressing the risk of fraud, materiality, identifying entity-level controls, identifying significant accounts and disclosures and their relevant assertions., testing controls-testing operating effectiveness, forming an opinion.

72.4 Audit Documentation: It requires that the auditor should comply with the requirements of SA 230, Audit Documentation to the extent applicable.

73. In repect of the audit work relating to ICoFR, there is no evidence at all except for a copy of the unsigned and unauthenticated copy of a document titled "Policies & Procedures on Internal Financial Control'[54]. Further, as elaborated in para 90 to 94, the Auditors have not performed any work relating to SA 315 which is the benchmark to be used by the management and auditors to assess and state adequacy and compliance of the system of internal control. Further, as elaborated in para 77 and 98, the audit programmes used in the audit of Financial Statements are significantly deficient and do not provide any information about nature of tests performed i.e., test of controls and the timing of those tests etc. Also, there is no documenation of the results of the test of controls performed, based upon which the adequacy and operating effectiveness of the ICoFR has been concluded.

74. In the absence of any evidence of the audit work performed by the Auditors in respect of ICoFR, the unmodified audit opinion issued by them is without any basis. As can be seen from preceding paras, the Auditors are found to have been grossly negligent in their professional duties and have failed to obtain SAAE, thereby violating SA 200 and the Guidance Note.

C.6 Audit Documentation

75. The Auditors were charged with non-compliance with Para 8, 9 and 10 of SA 230.

76. The Auditors in their reply referred to certain work papers in the audit file which according to them demonstrate the audit procedure performed, audit evidence obtained, persons who performed and reviewed the same. They further stated that the audit documentation prepared by them is sufficient to enable them to understand the nature, timing and extent of audit procedures performed.

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[54] WP reference Page 42-48 of Audit File 4

77. We find that the audit file of MIIL for the FY 2020-21 consists of 4,294 pages out of which, approximately 2900 pages relate to Purchase/Sales invoices. A few pages consisting of engagement letters, audit planning, audit checklist etc. also have deficiencies as shown in the table below:

Table 3

S.NO.	Audit Paper	Reference in Audit File	Deficiency in Working Paper
i.	Engagement Letter	Page 11 to 16 (Audit File-1)	There is no date mentioned on the acknowledgement of the Engagement Letter by the Company.
ii.	Audit requirement list	Page 17 to 19 (Audit File-1)	The preliminary requirement list for Statutory Audit has three columns, (a) status (b) company remark and (c) auditor remark All of which are blank with no remarks, and no date is evidenced on the work paper as to when it was shared with the Company. (Refer para 87 below)
iii.	Audit Programme	Page 20 to 21 (Audit File-1)	Signed by the EP and EQCR Partner, but no date is mentioned.
iv.	CARO Checklist	Page 22 to 36 (Audit File-1)	Checklist on Companies (Auditor's Report) Order, 2016 only has sign of EP and EQCR Partner but no date is mentioned on the work paper. Also, there is no signature of the preparer and Audit Manager.
v.	Audit points discussed between EP and EQCR	Page 39 to 41 (Audit File-1)	Signed by the EP and EQCR Partner, but no date is mentioned on the work paper.

In the absence of dates on the work papers, the timing of preparation of these work papers i.e., whether before signing of audit report or as an afterthought in response to SCN is questionable.

78. In view of the analysis of working paper referred by the Auditors it is evident that they have not prepared audit documentation as per Para 8 of SA 230 which requires the auditor to prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit to understand:

(a) The nature, timing, and extent of the audit procedures performed to comply with the SAs and applicable legal and regulatory requirements;

(b) The results of the audit procedures performed, and the audit evidence obtained; and

(c) Significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

79. The averment made by the Auditors that the audit documentation is sufficient to enable them to understand the nature, timing and extent of audit procedures performed, is unconvincing because it fails one of the objectives of the audit documentation, that is, to enable other external parties to carry out inspections in accordance with laws and regulations.

80. Further, there was no audit evidence as to who performed the audit work, who reviewed the audit work performed, and the date and extent of such review, reflecting violation of Para 9 of SA 230.

81. The Auditors have also failed to document discussions of significant matters with TCWG, including the nature of significant matters discussed, and when and with whom discussions took place as per Para 10 of SA 230.

82. From the above, it is established that the Auditors have merely collected invoices from the company and placed in the audit file. They failed to meet the objectives of SA 230 to prepare documentation that provides sufficient and appropriate record for the basis of auditor's report and evidence that the audit was planned and performed in accordance with SAs. From the above, it is also evident that the audit file primarily contains invoices/bills and information taken from the Company and does not record professional judgements and significant conclusions/decisions made by the Auditors and the basis for that. Non-documentation of the work performed is a clear evidence that the work has not been performed. It is apposite to note the observations of the Australian Audit Regulator ASIC, mentioned below:

> *"Firms often assert that our findings relate to documentation deficiencies in their audit file. An audit file should contain sufficient detail for an experienced auditor to understand the work performed and relied on in forming conclusions.* ***Where this detail has not been documented, our presumption is that the work has not been performed. We have used this approach for several years and it is consistent with the approach applied globally by other audit regulators and in most firm internal quality review programs.****"*[55] (Emphasis supplied)

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

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[55] Refer Page 7 of ASIC Audit Inspection Report – Report 743 October 2022

performed the work and the date such work was completed. Additionally, in each of the Issuer A and Issuer B audits, the audit documentation was insufficient to demonstrate which aspects of the audit and which audit documentation Bharat Parikh reviewed."

84. We also note that the Executive Counsel to the Financial Reporting Council (FRC), the UK Audit Regulator, reprimanded Deloitte LLP and John Charlton for breach of ISA 230[56] where the auditors failed to adequately document the audit work papers in the audit of Mitie Group plc. for the year ended 31 March 2016, and imposed a financial sanction of two million pounds on Deloitte and 65,000 pounds against Charlton.

85. In the present case, we note that instead of being an exercise in application of professional skill and care to ensure quality of the audit evidence, the Auditors work had degenerated into simply collecting and filing reams of photocopies of documents of routine nature (e.g., 2900 pages of Purchase/Sales Invoices) in the Audit Work Paper file. We therefore conclude that the Auditors have failed to comply with provisions of SA 230 in respect of audit documentation thereby showing lack of due diligence and gross negligence.

C.7 Failure to plan the audit of Financial Statements

86. The Auditors were charged with non-compliance with Para 6, 8 and 11 of SA 300 which requires the auditor to establish an overall audit strategy that guides the development of the audit plan and documenting of the audit strategy and any changes made thereto during the engagement with reasons for the same. On examination of the audit file, we find that there is no evidence of performance of these activities.

87. Responding to the charge, the Auditors referred to their audit planning documents which included a preliminary requirement list for Statutory Audit for the year ending March 31, 2021, Engagement Letter, Audit Programme, Checklist for CARO and Ind AS Checklist, which they considered as overall audit strategy. We find that the preliminary requirement list for Statutory Audit has three columns, all of which are blank with no remarks and no date. A screenshot of the same is given below: -

MAN Industries (India) Limited
Preliminary Requirement list for Statutory Audit for March 31, 2021

Sr. No.	Requirements List	Status	Company Remarks	MHD Remark
1	Audit Engagement Letter (With Reference To SA 210)			
2	Minutes of Board meeting and EGM			
3	Audit Committee Minutes			
4	Draft Financials Standalone			
5	DPT 3			
6	Internal Audit Report			
7	List Of Various Registration Obtained In Various Laws			
8	List Of Branches & Books Maintained			

Therefore, the above clearly indicate lack of due diligence and gross negligence on the part of the Auditors.

[56] ISA 230 is the corresponding international standard to SA 230

88. The Ind AS checklist referred to by the Auditors has only the title of Ind AS. There are no detailed checkpoints of the activities to be performed by the Auditor for each of the applicable Ind AS. Further, the Auditors have mentioned 'N' against Ind AS 21 *The Effects of Changes in Foreign Exchange Rates,* whereas it has been observed from the Financial Statements of MIIL that they have applied Ind AS 21 for accounting investments in Man USA Inc. a subsidiary. The Auditors have also not considered Ind AS 115 for revenue recognition as part of their audit planning. Thus, the checklist for Ind AS prepared by the Auditors is a mere formality and shows the ignorance of the applicable Ind ASs. We, therefore, conclude the explanations given by the Auditors fail to establish compliance with SA 300.

89. Failure to make an appropriate audit plan has been viewed seriously. For example, PCAOB, the US Regulator, charged L.L. Bradford & Company, LLC (the "Firm") for its failure to develop an appropriate audit plan for the audit of Web:XU Inc.'s ("WebXU") and concluded that the *"the Firm violated PCAOB rules and auditing standards with respect to an audit and a quarterly review of one issuer audit client. Specifically, the Firm in conducting its audit of the Financial Statements of WebXU for the year ended December 31, 2011, failed to properly assess the risks of material misstatement. As a result, the Firm failed to properly identify significant risks in connection with the 2011 WebXU audit. The Firm also failed to properly establish an overall strategy for the audit and develop an audit plan that included planned risk assessment procedures and planned responses to the risks of material misstatement. In addition, the Firm failed to perform sufficient audit procedures that addressed the risks of material misstatement. "* PCAOB censured the Firm, revoked its registration permanently, and imposed a civil money penalty of $12,500 upon the firm.

C.8 Failure to perform risk assesment procedures and response to such risks

90. The Auditors were charged with failure to comply with Para 5, 6 and 11 of SA 315[57] which requires that the auditor shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement (ROMM) at the Financial Statement and Assertion levels. It also requires the auditor to obtain an understanding of the entity and its environment. Further, the Auditors were charged with failure to comply with Para 1, 5 and 6 of SA 330[58].

91. Responding to the charge, the Auditors have simply mentioned the objectives of SA 315 and SA 330 without evidence of any work having being performed. They have also stated that these charges do not hold good, since in their opinion the charges of professional misconduct relating to certain specific errors/omissions do not survive. Further, they state that they have performed necessary risk assessment procedures in identifying the ROMM due to fraud or error and there are no material mistatements in the Financial Statements.

92. Para 32 of SA 315 requires that the auditor shall, inter alia, document the following:

92.1 Sources of information which the understanding of the Entity and its Environment was obtained, risk assessment procedures performed e.g., inquiries of the

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

[58] Standard on Auditing, The Auditor's responses to Assessed Risk (SA 330)

management and other individuals, analytical procedures, and observation and inspection (Para 32 (b) of SA 315). The risks identified, and the related controls.

92.2 Entity's Internal Control including understanding the various components of Internal Control such as the organisation structure, participation by TCWG, assignment of authority and responsibility, human resource policies/practices, entity's process of determining risks to be managed, the information technology (IT) system relevant to Financial Reporting including those related to business processes and journal entries, control activities whether manual or within IT Systems, risks arising from IT Systems, monitoring of controls such as Internal Audit Function etc.

92.3 Identification and assessment of ROMM at the Financial Statement level and Assertion level for classes of transactions, account balances, and disclosures (Para 32 (c) of SA 315). Assertions used by the Auditor for different types of potential misstatements are shown in the Table below:

Table-4

Assertions used by the Auditor to consider different types of material misstatements (Refer Para A121 – A125 of SA 315 for more details)			
Assertions	**Material Misstatement Categories**		
	Class of Transactions/Events during the audit period	Account balances at the period end	Presentation and Disclosure
Occurrence	√	-	√
Completeness	√	√	√
Accuracy	√	-	-
Cut-off	√	-	-
Classification	√	-	-
Existence	-	√	-
Rights and obligations	-	√	-
Valuation and allocation	-	√	-
Classification and understandability	-	-	√
Accuracy and valuation	-	-	√

92.4 Information gathered by performing risk assessment procedures. **It is pertinent to note that the risk assessment i.e., nature and level of risk (low, medium, high, significant etc.) detemines the nature, timing, and extent of audit procedures to be performed.**

93. We find that the Audit Work Papers contain following documents only:

a) 3 pages of List of Preliminary Audit Requirements[59]

b) 7 pages of Policies & Procedures on Internal Financial Control[60]

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[59] WP Reference- Page 17-19 of Audit File 1
[60] WP Reference- Page 42-48 of Audit File 1

c) 12 pages of Internal Audit Reports for the 3 quarters of FY 2020-21[61]

93.1 The document on Policies & Procedures on Internal Financial Control has no signature or authentication by the Company. Further, there is no evidence of the Auditors having performed any audit steps such as walkthroughs, tests, observations, inspections or inquiries with the Management or other appropriate officials to understand the details of the design and operation of various controls and processes. The Audit Work Papers as well as the above referred documents lack even the basic information, the name and other details of the IT system used by the Company.

93.2 The Executive Summary of Internal Audit Reports for the three quarters during the audit period FY 2020-21 do not even have basic details like date of the internal audit report, who had perfomed these internal audits, signature of the internal auditors etc. This notwithstanding, the internal audit reports contain certain matters of serious concern on the recoverability of the trade receivables and capital advances indicating significant risk of material mistatements of revenue, ECL (or Impairnment Loss), trade receivables and other advances in the Financial Statements under audit i.e., FY 2020-21. The Internal Audit Reports reported amounts withheld by the customers for delay in supply of pipes as per contract committed of Rs. 85.19 crores[62] , Rs. 126.87 crores[63] and Rs. 120.47 crores[64] for the quarter ending 31.03.2021, 31.12.2020 and 30.09.2020 respectively. Similarly, Internal Audit Reports reported long pending advances to vendors without receipt of material of Rs. 22.5 crores[65] , Rs. 22.5 crores[66] and Rs. 22.5 crores[67] for the quarter ending 31.03.2021, 31.12.2020 and 30.09.2020, respectively.

94. However, there is no evidence in the audit file that the Auditors identified and assessed the above mentioned adverse features of pending litigation[68] of subtantial amounts as items of ROMM and the risks that required special audit consideration. Therefore, this is a serious non-compliance with the requirements of Para 25 to 29 of SA 315.

95. In light of the above facts and circumstances, we conclude that the Auditors have been grossly negligent in the conduct of their professional duties and made false declaration in the audit report of the true and fair view of the Financial Statements.

C.9 Failure to design and implement auditors' response to assessed risks

96. The Auditors were charged with failure to comply with Para 1, 5 & 6 of SA 330 which require the auditor to design and implement overall responses to the ROMM identified and assessed during audit.

97. The Auditors in their response have simply stated the objectives of SA 330 without giving any work paper reference of the work performed.

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[61] WP Reference- Page 38-49 of Audit File 4
[62] WP Reference – Page 39 of Audit File 4
[63] WP Reference – Page 41 of Audit File 4
[64] WP Reference – Page 45 of Audit File 4
[65] WP Reference – Page 45 of Audit File 4
[66] WP Reference – Page 41 of Audit File 4
[67] WP Reference – Page 45 of Audit File 4
[68] See Annexure 2 to SA 315

98. We observe that the Audit Work Papers in respect of design and implementation of the audit procedures contains only two pages of the Audit Programme[69] reproduced below and one page of Ind AS Checklist:

MAN INDUSTRIES (INDIA) LIMITED
PERIOD: 2020-2021

AUDIT INCHARGE: CA DEVANG DALAL
AUDIT STAFF / ARTICLE ASSISTANT:
Megha Kanade
Neha Singh
Bharat Jadeja
Bhavesh Shah

Audit Programme

Sr. No.	Particulars	Checked By	Approved By	SAMPLING METHOD	AUDITOR REMARKS
1	OPENING TRIAL BALANCE	Neha			Verified with the last years audited Financials
2	Bank & Cash Balance	Bharat	CA DEVANG DALAL	100%	a) Mailed Banks for direct confirmation for balance outstanding as on 31.03.2021 b) We have verified the Bank Reco., Bank Statement and major payments towards repayment of loan, payments to suppliers, etc. We found proper supporting & proper authorizations. There were no discrepancies found c) Confirmation received to Bank and Cash verified
3	LOAN		CA DEVANG DALAL		
	SECURED LOANS	Bhavesh		100%	a) Scanned Sanction Letter verified b) Terms of the loan checked for compliances c) Scanned Confirmation vouched
	UNSECURED LOANS	Bharat		100%	a) Ledger verification conducted b) Scanned Confirmation vouched
	INTER CORPORATE LOANS	Bharat		100%	a) Scanned Agreement verified b) Ledger Checked
4	FIXED ASSETS FA REGISTER Reports of Physical verification ADDITION DELETION DEPRECIATION As per companies act As per income tax act	Megha	CA DEVANG DALAL	Random / Scanning	a) Vouching and verification conducted for scanned invoices of Fixed Assets b) Ledger scrutiny done c) Depreciation as provided by management checked
5	PREPAID EXPENSES	Bhavesh	CA DEVANG DALAL	100%	Working provided by management checked
6	INVENTORIES	Neha	CA DEVANG DALAL	Random / Scanning	a) Valuation provided by management checked b) Scanned bills of inventories verified
7	INVESTMENTS	Bhavesh	CA DEVANG DALAL	100%	a) Valuation report checked b) Impairment testing
8	STATUTORY DUES TAX DEDUCTED AT SOURCE PROVIDENT FUND PROFESSIONAL TAX ESIC GST	Megha	CA DEVANG DALAL	100%	a) Scanned Returns Verified b) Scanned Challans Verified c) Reconciliation provided by management checked d) Ledger Verified e) Fixed GSTR 9 & GSTR 9C Verified
9	Sales	Bhavesh	CA DEVANG DALAL	High Value & Random	a) Sample Scanned invoices vouched b) Reconciliation of Sales with GST Returns provided by management checked
10	OTHER INCOME	Bharat	CA DEVANG DALAL	100%	a) Reconciliation of income with 26 AS provided by management checked b) FD Receipts vouched
11	PURCHASES	Bharat	CA DEVANG DALAL	Sampling basis	a) Sample scanned invoices vouched b) Reconciliation of ITC with GST Returns provided by management checked
12	EMPLOYEE BENEFIT EXPENSES	Neha	CA DEVANG DALAL		
	SALARY BONUS LEAVE ENCASHMENT			Random / Scanning On Test Check Basis Random / Scanning	a) Actuarial Report Verified b) Ledger Scrutiny Done
13	Finance Cost	Megha	CA DEVANG DALAL	100%	a) Interest provision for loan checked b) Working provided by Management checked c) Repayment schedule provided by the bank verified
14	EXCHANGE GAIN/LOSS VERIFICATION	Bhavesh	CA DEVANG DALAL		Exchange gain/ (loss) Transactions reviewed and the valuation provided by the management checked.
15	JOURNAL VOUCHING	Bhavesh	CA DEVANG DALAL	Materiality Basis	Various Scanned invoices of Expenses vouched & verified on sample basis along with ledger scrutiny and documentation done of the same
16	Deferred Tax	Bharat	CA DEVANG DALAL		Deferred Tax working provided by management checked
17	RELATED PARTY TRANSACTION	Bharat	CA DEVANG DALAL	100%	a) Agreements verified b) Ledger Scrutiny done

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99. SA 330 lays down certain fundamental requirements on the part of the auditors such as:

99.1 The auditor shall design and implement audit procedures to address the ROMM at the Financial Statements level, and at the level of transactions, account balances and presentation and disclosure levels called as Assertion Level.

99.2 The auditor shall design and perform appropriate type of audit procedures e.g.,

[69] WP Reference Page 20-21 of Audit File 1

the auditor shall perform Test of Controls to verify the operating effectiveness of relevant internal controls; the auditor shall design and perform substantive procedures for each class of material transactions, account balances, and disclosure;

99.3 The auditor shall document nature, timing and extent of the the audit procedures, linkages of these procedures to ROMM.

100. The sampling method and approach is mentioned as 100% Random/Scanning, Sampling Basis, High Value/Random, on test check basis, materiality basis and relevant compliance. However, the 'basis' for these sampling approaches, how they are responsive to the ROMM and how they are in compliance with the requirements of SA 530, Audit Sampling, have not been detailed.

101. In the light of above glaring deficiencies, we conclude that the Auditors were found wanting in compliance with Para 1, 5 & 6 of SA 330.

C.10 Failure to determine materiality

102. The Auditors were charged for failure to comply with Para 10 and 14 of SA 320, which require an auditor to determine materiality for the Financial Statements as a whole while establishing the overall audit strategy and the auditor to document the amounts and the factors considered in his determination of materiality for the Financial Statements as a whole and for performance materiality.

103. The Auditors denied the charges stating that there is no proof of alleged misstatements having significantly impacted the usability of the Financial Statements.

104. According to Para 10 of SA 320, when establishing the overall audit strategy, auditor shall determine the 'Materiality' for the Financial Statements as a whole. In addition, Para 11 of SA 320 states that the auditor shall determine 'Performance Materiality' for the purposes of assessing the ROMM and determining the nature, timing and extent of further audit procedures.

105. Para A2–A6 of SA 320 provides application material. Para A2 states that a percentage is often applied as a starting point determining materiality for the Financial Statements as a whole and gives factors that affect the appropriate benchmark such as elements of the Financial Statements (e.g., assets, liabilities, equity, revenue, expenses). Para A6 provides more specific guidance when it states that the auditor may consider five percent of PBT from continuing operations to be appropriate for a profit-oriented entity in a manufacturing industry and while the auditor may consider one percent of total revenue or total expenses to be appropriate for a not-for-profit entity. Also, a recent report[70] of the Committee of European Audit Oversight Body (CEAOB) mentions Profit Before Tax (PBT), Adjusted PBT, Average PBT, Total Revenue and Total Equity as the commonly observed benchmarks for determining materiality and reports 3 to 10% and 0.5 to 2% of the PBT, Total Revenue/Total Assets, respectively, as the commonly observed percentages used in the audit of public interest audits. Similar findings were reported in the thematic review of Financial Reporting Council, UK.[71]

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[70] Report on the CEAOB Survey, Materiality in the Context of Audit July 2022
[71] Audit Quality Thematic Review Materiality December 2013, FRC UK

106.The use of the expression 'Shall' in Paras 10 and 11 of SA 320 obligates the auditor to determine Materiality and Performance Materiality. In this regard, it is apposite to remember the contents of the announcements of the Council of Institute of Chartered Accountants of India regarding status of the documents issued by the ICAI.[72] In particular, the following statements about the new format of SAs applicable from 1st April 2008[73] are relevant:

> *"III. Members may also note that recently, the Council of the Institute of Chartered Accountants of India has approved the Preface to the Standards on Quality Control, Auditing, Review, Other Assurance and Related Services. The said Preface introduces a totally new format of writing Standards, in line with that adopted by the International Auditing and Assurance Standards Board pursuant to its Clarity Project. According to the new format the Standards on Auditing (SAs) would now contain two distinct sections, one, the Requirements section and, two, the Application Guidance section.*
>
> *IV. The fundamental principles of the Standard are contained in the Requirements section and represented by use of "shall". Hitherto, the word, "should" was used in the Standards, for this purpose. ..."*

107. However, we find that the Auditors have not determined any 'Materiality' or 'Performance Materiality' in the audit of Financial Statements of MIIL, which is a mandatory requirement. All that can be found in the Audit Work Papers is vague and general expression like 'Materiality Basis', 'High Value' and Random' in the column titled 'Sampling Method' of just two pages of the undated audit programme[74] .

108. In view of the above, we conclude that the Auditors have failed to adhere to the mandatory requirements of the fundamental audit procedure of determining Materiality in accordance with SA 320 and falsely stated in their report that they had conducted their audit in accordance with the SAs specified under Section 143(10) of the Act.

109. We also conclude that the quality and credibility of the audit work performed by the Auditors is significantly deficient vis-a-vis the requirements of the relevant SAs. Rather, it does not inspire any confidence in the audit work of the Auditors of a public interest entity, the fundamental purpose of which is to enhance the degree of confidence of intended users in the Financial Statements. Therefore, we hold that the Auditors have failed to discharge their responsibilities as auditors..

D. OTHER LAPSES IN THE AUDIT

D.1 Failure to perform Analytical Procedures

110.The Auditors were charged with failure to comply with Para 3(b) and Para 6 of SA 520 which require the auditor to design and perform analytical procedures to assist the auditor in overall conclusion of the audit as to whether the Financial Statements are consistent with the auditor's understanding of the entity. On examination of Financial Statements, it is observed that there was a 90% increase (from Rs. 153.98 crores in FY 2019-2020 to Rs. 292.45 crores in 2020-

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[72] Section I of the Handbook of the Auditing Pronouncements issued by Audit and Assurance Standards Board of the ICAI (2019).
[73] Page 5 of Handbook of the Auditing Pronouncements issued Audit and Assurance Standards Board of the ICAI (2019).
[74] WP Reference 20/21 of Audit File 1

2021) under the head selling and distribution expenses, whereas the sales increased only by 18%. Further, the contingent liabilities have reduced by Rs. 543.24 crores in 2020-21.

111. In response, the Auditors submitted that they had questioned the management regarding items that reported a significant increase over the previous FY. For e.g., commission on sales (+308.41%), bad debts (+781.31%), freight and forwarding charges (+151.51%).

112. We noted that the Auditors have simply referred to items disclosed in Note 40 of the Financial Statement as evidence of analytical review performed by them. There is no analysis, judgement/conclusion documented by the Auditors. There are no reasons recorded by the Auditors regarding substantial increase in the selling and distribution expenses. Various explanations given by them in reply to SCN are an attempt to wriggle out of complete absence of any work relating to analytical review procedures.

113. Regarding reduction in contingent liability, the Auditors have merely given balance confirmation obtained from different banks. The Auditors have not documented any conclusion nor recorded reasons of reduction of contingent liabilities by Rs. 543.24 crores in 2020-21.

114. On analysis of the Audit Working Papers referred to by the Auditors it is nowhere seen that they have raised queries to the management or have had discussions with them regarding the substantial changes in figures in FY 2020-21 from FY 2019-20. The table below shows the change in items year on year:

Table-5

Item	**2019-20 (Rs. crores)**	**2020-21 (Rs. crores)**	**% Change**
Non-Current			
Assets			
Right to Use Asset	14.27	10.30	-27.79
CWIP	3.56	1.01	-71.58
Trade Receivables	51.13	25.18	-50.75
Other Financial assets	15.56	4.56	-70.66
Liabilities			
Borrowings	15.33	2.03	-86.75
Trade payable	0.11	0.84	667.64
Lease liabilities	11.73	7.60	-35.25
Current			
Asset			
Inventories	379.60	331.56	-12.66
Investments	0.02	0.62	2922.22
Trade Receivables	427.07	635.28	48.75
Cash & Cash Equivalent	135.92	17.00	-87.49
Liabilities			
Borrowings	232.36	284.57	22.47
Dues to MSME	4.68	8.21	75.35
Other Financial Liabilities	65.52	31.82	-51.43
Other current liabilities	153.53	64.44	-58.03

115. In the light of above, the audit file lacks documentation regarding any analytical procedures performed, which proves that the Auditors failed to design and perform analytical procedures. We, therefore, conclude the Auditors have violated Para 3(b) and Para 6 of SA 520.

D.2 Failure to prepare documentation regarding Auditor's responsibilities relating to fraud

116. The Auditors were charged with failure to comply with the requirements of Para 16 and 24 of SA 240.

117. Responding to the charge, the Auditors submitted that necessary inquires with the management were made and as per the information and explanation given by the management, no fraud on or by the Company was noticed during the period of audit. The Auditors referred to clause 3(x) of CARO 2020 and reported that:

> *"Based upon the audit procedure performed for the purpose of reporting the true and fair view of the Financial Statements and as per the information and explanation given by the management, we report that no fraud by the company or on the company by the Company or on the company by its officers or employees has been noticed or reported during the period covered by our audit."*

118. We observe that it is nowhere documented in the audit file whether Auditors had identified and assessed ROMM to comply with the requirements of Para 16 of SA 240 wherein Auditor is required to perform the procedures as mentioned in Paragraphs 17 to 24 of SA 240, to obtain information for use in identifying the ROMM due to fraud. Further, as mentioned in preceding paras, the Auditors have failed to perform any audit procedure in respect of identification and assessesment of ROMM under SA 315. We also observe that it is nowhere documented in the audit file whether the Auditors made enquiries from the company's staff related to internal control processes or observed the staff performing the controls. The reply is an afterthought to hide their deficencies in the conduct of audit. In the light of above, we conclude that the Auditors have failed to comply with the requirements of Para 16 and 24 of SA 240.

D.3 Failure to Communicate with Those Charged with Governance (TCWG)

119. The Auditors were charged with failure to determine TCWG and communicate with TCWG about the responsibilities as an auditor, overview of planned scope, timing of the audit and deficiencies in Internal Control etc. The Auditors were also required to maintain audit documentation of such communication with TCWG. It was noted that the audit file had no documentation in this regard indicating that there was no communication with TCWG, which was in non-compliance with the requirements of SA 260[75] and SA 265[76].

120. Responding to the charge, the Auditors submitted that the Audit Engagement Letter[77] which confirms the acceptance of the audit besides the planned scope, statutory and professional duties, has been signed by the auditee thereby establishing communication with TCWG. In relation to impairment testing of investments of Rs. 102.3 crores in MSPL, the Auditors stated

[75] SA 260: Communication with Those Charged with Governance (Para 15,11,14,16 & 23)
[76] SA 265: Communicating Deficiencies in Internal Control to Those Charged with Governance and Management
[77] Page 11 to 16 of Audit File-1

that they have discussed with the management and obtained the valuation report. However, the Auditors admit that there is no documentation for every communication with TCWG and referred to Para 19 of SA 260, which states '......*Written communications need not include all matters that arose during the course of the audit.*'

121. We observe that the Auditors failed to understand the importance of TCWG as a body which has the responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity which includes overseeing the Financial Reporting process. It is pertinent to mention that impairment testing of investment of MSPL was also made a Key Audit Matter in the Audit Report. However, the Auditors assumed that it was not significant to record in writing whereas Para 19 of SA 260 states that the Auditor shall communicate in writing with TCWG regarding significant findings from the audit if, in the auditor's professional judgement, oral communication would not be adequate. Further, Para 23 of SA 260 states that, "*Where matters required by this SA to be communicated are communicated orally, the auditor shall include them in the audit documentation, and when and to whom they were communicated. Where matters have been communicated in writing, the auditor shall retain a copy of the communication as part of the audit documentation*", which the Auditors failed to do.

122. In light of above, we conclude that the Auditors failed to exercise due diligence and were grossly negligent in not identifying and communicating with TCWG and therefore, violated the requirements of SA 260[78] and SA 265[79].

123. Failure to appropriately communicate with Audit Committee has been viewed seriously by our international counterparts too. For example, PCAOB, the US Regulator, charged the public accounting firm L.L. Bradford & Company, LLC (Audit Firm) for its failure to communicate with the audit committee during the audit of WebXU Inc.'s ("WebXU") and noted that the "*Firm also violated a PCAOB rule that requires a registered public accounting firm to communicate, in writing, to the audit committee ....* " PCAOB for this misconduct among others, censured the Firm, revoked its registration, and imposed a civil money penalty of $12500.

E. LAPSES OF THE AUDIT FIRM

124. The Audit Firm was charged with failure to comply with Para 2 of SA 220 and Para 3 of SQC 1 which stipulates that the Firm has an obligation to establish and maintain a system of quality control. The Firm was also charged with failure to establish policies and procedures designed to provide it with reasonable assurance that the Firm and its personnel comply with relevant ethical requirements in accordance with Para 14 of SQC 1.

125. As part of the audit file, the Firm submitted a two-page document titled 'Policies on Quality Control' which contains policy statements around six (6) elements of a system of quality control mentioned in Para 7 of SQC 1. Further, the Firm's responses given as part of reply to SCN are summarized below:

> *"The Firm stated that it was established in 1984 and over the period they have been involved in Statutory Audits, internal audits and tax audits of small, mid-*

[78] SA 260: Communication with Those Charged with Governance (Para 15,11,14,16 & 23)
[79] SA 265: Communicating Deficiencies in Internal Control to Those Charged with Governance and Management

scale and large corporates. The Firm states that there has been no regulatory action against them, and the Firm enjoyed a good reputation all through.

The Firm in general terms states that they carry out audit assignments which are in compliance with SAs and follow procedure as stated below:

(i) Firm crystallizes its terms of engagement with all its clients and compliance with SA 220.

(ii) Certain cases communicate with the previous Auditor.

(iii) After engagement terms are finalized and executed, a dedicated team is assigned and an overall audit strategy is developed which includes the scope, timing and direction of the audit, that guide the development of audit plan and develop overall strategy.

(iv) Determine materiality, the firm analyses a class of transactions, account balances and disclosures made by the entity, impact of such transaction and disclosure made by the entity, impact of such transactions and disclosure on the financial status of the Company etc.

(v) While identifying risk, inquiries are raised with management, those charged with governance.

(vi) Further, the accounting standards, legal and regulatory requirement keep changing and are updated every year.

(vii) If the Company has been audited before, the changes in its financial situation from the last audit is taken into consideration. Also review of note of previous year audit notes and observations are also done which assist the team to plan the audit in an effective manner.

(viii) On the above basis, timeline is decided, and responsibilities are assigned. Also, due date of completion is mentioned.

(ix) Evidence is gathered on the basis of which the audit opinion is arrived at.

(x) Audit work is reviewed by the Engagement Partner and finally by Engagement Quality Control Review Partner (EQCRP).

(xi) Once preliminary opinion is arrived at, discussion placed with TCWG.

(xii) If required, audit file review by EQCP and discussion between the EP and EQCR regarding audit observations.

(xiii) Thereafter, a conclusive audit opinion is formed based on the audit evidence gathered. This opinion is formed post discussion with TCWG and EQCP. Additionally, take Management representation.

(xiv) *Thereafter, Audit File is closed within 60 days of completion of the Audit.*

(xv) *Audit Firm stated that they have an exhaustive and thorough process before forming an audit opinion."*

126. The fundamental deficiencies noted are as follows:

126.1 Quality Control Policy (QCP) does not even mention how the firm complies with prohibition on non-audit services under Section 144 of the Act, Partner Rotation requirements and what its policies and procedures are to mitigate the various threats to compliance with the fundamental principles of the Code of Ethics issued by the ICAI.

126.2 QCP is silent in respect of certain critical aspects such as Consultation, Engagement Quality Control Review, ongoing consideration and evaluation of the Firms QCP and periodic inspection of selection of completed assignments.

126.3 QCP is not supported by any Procedure Manual.

126.4 The Firm's response to SCN states that "If required, the audit file is reviewed by the EQCP". This policy is completely against the mandatory requirement of Para 20 and 21 of SA 220.

127. Most of the averments of the Firm in respect of system of quality control are misleading as the deficiencies in the audit work and its documentation noted in previous paragraphs demonstrate that the Firm's QCP has remained only on paper. There is no evidence in the audit file to show that the Audit Firm has complied with Para 2 of SA 220 and Para 46 of SQC 1.

128. We, therefore, conclude that the Audit Firm has failed to monitor and control the quality of this audit engagement and integrity of the audit files as audit documentation by the Firm completely fails to ensure even the minimum essential to meet the requirements of SQC 1 and SA 230 as mentioned in para 75 to 123 of this Order. The fundamental aspects of integrity of audit files, accountability of the Firm and its personnel, maintaining sufficient appropriate audit evidence for the audit planning, performance, and basis for conclusions for achieving audit objectives are seriously compromised as has been detailed on pre-pages. Consequently, the Audit Work Papers maintained by the Firm are not found to meet the compliance requirements of SA 230. In not having reviewed and rectified these deficiencies, the Audit Firm is guilty of serious professional misconduct.

129. Therefore, as discussed above, the Audit Firm has made departure from the Standards and the Companies Act, 2013 in the conduct of the audit of MIIL for FY 2020-21. As is evident from the above discussion, the Audit Firm has given an unmodified opinion in SFS and a qualified opinion on the CFS without any basis. The poor quality of audit, incomplete documentation and attempt to mislead through evasive replies further compounds the professional misconduct on the part of the Audit Firm. Based on the foregoing discussion and analysis, we conclude that the Audit Firm has committed professional or other misconduct, as defined in the Act. In an audit engagement assigned to an Audit Firm, the responsibility of the Audit Firm is to ensure its systems and processes are conducive to a high-quality audit in compliance with the Law and Professional Standards. We find that the Firm has failed in this regard.

130. It is pertinent to note that PCAOB in its recent order[80] in the case of Marcum LLP mandated functional changes to the quality control supervisory structure in the firm and imposed monetary penalty of 3 Million USD for quality control violations.

F. Findings on Articles of Charges of Professional Misconduct by the Auditors

131. Based on the foregoing discussion and analysis, we conclude that the Auditors have committed professional misconduct as defined in Section 132 (4) of the Companies Act, read with Section 22 the Chartered Accountants Act 1949 (the CA Act), as amended from time to time, as detailed below:

i. The Auditors committed professional misconduct of *failure to disclose a material fact known to them which is not disclosed in a financial statement, but disclosure of which is necessary in making such financial statement where they are concerned with that financial statement in a professional capacity" (*Refer Clause 5 of Part I of the Second Schedule of the CA Act).
This charge is proved as explained in Section C and D above.

ii. The Auditors committed professional misconduct of *failure to report a material misstatement known to them to appear in a financial statement with which they are concerned in a professional capacity.*(Refer Clause 6 of Part I of the Second Schedule of the CA Act).
This charge is proved as explained in Section C and D above.

iii. The Auditors committed professional misconduct by not exercising *due diligence and being grossly negligent in the conduct of their professional duties.*(Refer Clause 7 of Part I of the Second Schedule of the CA Act).
This charge is proved as explained in Section C, D and E above.

iv. The Auditors committed professional misconduct by *failing to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion.*(Refer Clause 8 of Part I of the Second Schedule of the CA Act).,
This charge is proved as explained in Section C, D and E above.

v. The Auditors committed professional misconduct by *failing to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances.* (Refer Clause 9 of Part I of the Second Schedule of the CA Act).
This charge is proved as explained in Section C, D and E above.

G. Findings on Additional Articles of Charges of Professional Misconduct by the Audit Firm

132. In addition to above, the Audit Firm has committed Professional Misconduct as defined in Section 132(4) of the Companies Act, read with Section 22 the Chartered Accountants Act 1949, as amended from time to time, as failure to exercise due diligence and being grossly negligent and by failing to invite attention to any material departure from the generally

[80] PCAOB Release No. 105-2023-005 dated June 21, 2023

accepted procedure of audit applicable to the circumstances, in the conduct of professional duties in respect of matters as explained in Section E above and thus violated SQC 1.

H. PENALTY and SANCTIONS

133. Section 132(4) of the Companies Act, 2013 provides for penalties in a case where professional misconduct is proved. The seriousness with which proved cases of professional misconduct are viewed, is evident from the fact that a minimum punishment is laid down by the law.

134. Independent Auditors of Public Listed Companies serve a critical public function of enabling the users of Audited Financial Statements to take informed decisions.

135. Absent a robust system of auditing, investors, creditors and other users of Financial Statements would be handicapped and their interest compromised. The best of systems fails if the professionals implementing the system do not perform their job. This could lead to a serious failure of the financial system which could ultimately result in a breakdown in trust and confidence of investors and the public at large.

136. Thus, the Auditors are duty bound to examine and ascertain the integrity of Financial Statements of such entities[81] in larger public interest.

137. The Auditors in the present case were required to ensure compliance with SAs to achieve the necessary audit quality and lend credibility to Financial Statements to facilitate its users. As detailed in this Order, substantial deficiencies in the audit, abdication of responsibility and inappropriate conclusions on the part of CA Devang Dalal establish his professional misconduct. Despite being a qualified professional, CA Devang Dalal has not adhered to the Standards and has thus not discharged the duty cast upon him. On the contrary, he has tried to cover up by giving unsubstantiated and unconvincing replies to the SCN. The Firm, M/s. M H Dalal & Associates has also failed to exercise appropriate control and monitoring of the work of the EP and the Engagement Team during the audit engagement and has abdicated its responsibility to ensure audit quality as per Professional Standards. Under the circumstances, we proceed to order the following sanctions keeping in mind the deterrence, proportionality, and the signalling value of sanctions.

138. As per information provided by the Auditor, the Statutory Audit fee of MIIL for FY 2020-21 was Rs [redacted], fees towards other services (Certifications) received was Rs. [redacted] and the total professional fee received by the Auditor for FY 2020-21 was Rs. [redacted]. The total professional fee earned by the EP, CA Devang Dalal was Rs. [redacted] for FY 2020-21.

139. Considering the fact that professional misconducts have been proved and considering the nature of violations and principles of proportionality, we, in exercise of powers under Section 132(4)(c) of the Companies Act, 2013, order:

i. Imposition of a monetary penalty of Rs.10,00,000/- (Rupees Ten Lakhs) upon CA Devang Dalal who is also debarred for Five years from being appointed as an auditor or internal auditor or from undertaking any audit in respect of Financial Statements or internal audit of the functions and activities of any company or body corporate.

81 As defined in Rule 3 of NFRA Rules 2018

ii. Imposition of a monetary penalty of Rs.50,00,000/- (Rupees Fifty Lakhs) upon M/s. M H Dalal & Associates.

140. This Order will become effective after 30 days from the date of its issue.

Signed

(Dr Ajay Bhushan Prasad Pandey)
Chairperson

Signed

(Dr Praveen Kumar Tiwari)
Full-Time Member

Signed

(Smita Jhingran)
Full-Time Member

Authorised for issue by the National Financial Reporting Authority,

Vidhu Sood

(Vidhu Sood)
Secretary

सचिव / Secretary
राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण
National Financial Reporting Authority
नई दिल्ली / New Delhi

Date: 28.06.2023

Place: New Delhi

To,
1. M/s M H Dalal & Associates,
Chartered Accountants
Firm Registration No 112449W
2. CA Devang Dalal
ICAI Membership No 109049
301, Balaji Darshan,
Tilak Road, Santacruz-West,
Mumbai 400054

Copy To: -

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