

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

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Kasturba Gandhi Marg, New Delhi

Order No: 023/2023

27.07.2023

**ORDER**

**In the matter of CA Sachin Kansal, under Section 132(4) of the Companies Act, 2013**

1. This Order disposes of the Show Cause Notice ('SCN' hereafter) No. NF-20012/5/2022 dated 23.09.2022, issued to CA Sachin Kansal (ICAI Membership No. 137191), proprietor of M/s S. Kansal & Associates (ICAI Firm Registration No. 134937W) ('Audit Firm' hereafter), Ahmedabad, who 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 M/s Anshu's Clothing Ltd (now known as Aditri Gems & Jewels Ltd), ('Anshu' or 'the company' hereafter) for the Financial Year ('FY' hereafter) 2015-16.
2. This Order is divided into the following sections:
  - A. Executive Summary
  - B. Introduction & Background
  - C. Failure to Report Non-compliance with Accounting Standards
  - D. Non-compliances with Standards of Auditing
  - E. Articles of Charges of Professional Misconduct
  - F. Penalty & Sanctions

**A. EXECUTIVE SUMMARY**

3. Pursuant to the information received from the Ministry of Corporate Affairs (MCA, hereafter), regarding irregularities observed in the financial statements of the Company by the Financial Reporting Review Board (FRRB, hereafter) of the ICAI for FY 2015-16, NFRA initiated investigation into the role of the Statutory Auditors during the audit of Anshu for FY 2015-16. During FY 2015-16, the equity shares of the company were listed on Bombay Stock Exchange and Metropolitan Stock Exchange. M/s S. Kansal and Associates were the statutory auditors of Anshu and CA Sachin Kansal was the EP for the audit during FY 2015-16.

4. Based on the investigation and proceedings under Section 132(4) of the Companies Act, 2013 ('the Act' hereafter) into the issues raised in the FRRB report and the preliminary examination of the financial statements of Anshu and the Audit File submitted by the EP, NFRA found the EP, *prima facie*, guilty of professional misconduct and issued SCN to the EP.
5. NFRA's investigation *inter alia* found that the company had not recognised accrued interest, amounting to ₹143.98 lakhs, on loans from bank and NBFCs in violation of Section 128 and Section 129 of the Act and AS 1<sup>1</sup>. With proper accounting of interest accrued the reported loss of the company would have increased by about 8 times. Such a material and pervasive misstatement in the financial statement of the company was not reported by EP in his Auditor's report. Further, deferred tax assets of ₹9.07 lakhs have been recognized by the company despite the company being in loss for several years, and lack of certainty that the company would be able to realise the deferred tax assets in future. Anshu was required to prepare its financial statement in the format given in Schedule III to the Companies Act, 2013 but various instances of non-compliance with the format of financial statements have also been noted, which have not been reported by EP in the Auditor's Report.
6. It was also noted that the EP has not assembled the Audit File within 60 days of signing of Auditor's report and has not appointed Engagement Quality Control Reviewer despite Anshu being a listed entity. The EP did not maintain the agreement on terms of Audit engagement in the Audit File, nor did the EP maintain any written communication with TCWG in the Audit File.
7. Based on investigation and proceedings under Section 132 (4) of the Companies Act, 2013 and after giving him opportunity to present his case, NFRA has found the EP guilty of professional misconduct and imposes through this Order the following monetary penalties and sanctions, which will take effect from a period of 30 days from issuance of this Order:
  - (i) Imposition of a monetary penalty of ₹ 1,00,000 (Rupees One Lakh) upon the EP, CA Sachin Kansal.
  - (ii) CA Sachin Kansal is also debarred for one year from being appointed as an auditor or internal auditor or undertaking any audit in respect of financial statements or internal audit of the functions and activities of any company or body corporate.

## **B. INTRODUCTION & BACKGROUND**

8. NFRA is a statutory authority set up under Section 132 of the Act to monitor

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<sup>1</sup> AS 1, Disclosure of Accounting Policies

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 certain powers of a civil court and is empowered under Section 132 (4) of the Act to investigate the prescribed classes of companies and impose penalty for professional or other misconduct of the individual members or firms of chartered accountants.

9. The statutory auditors, both individual and firm of chartered accountants, are appointed by the members of a company, under Section 139 of the Act. The statutory auditors, including the Engagement Partners and the Engagement Team are bound by the duties and responsibilities prescribed in the Act, the rules made thereunder, the Standards on Auditing (SAs, hereafter) including the Standards on Quality Control and the Code of Ethics, the violation of which constitutes professional misconduct, and is punishable with penalty prescribed under Section 132 (4) (c) of the Act.
10. On receipt of information vide letter dated 05.11.2019 from MCA describing irregularities observed by FRRB of ICAI in the Financial Statements of Anshu for FY 2015-16, the matter was thereafter taken up for investigation into the role of statutory auditor under Section 132(4) of the Act.
11. Anshu was engaged in the retail sale of readymade garments during FY 2015-16. Its equity shares were listed on the BSE Limited and Metropolitan Stock Exchange of India Limited during FY 2015-16 and it was required to prepare its financial statements for the FY 2015-16 in accordance with Schedule III and other applicable provisions of the Act and Accounting Standards (AS, hereafter) notified under the Companies (Accounting Standards) Rules, 2006.
12. M/s S Kansal & Associates having Firm Registration No. 134937W were the Statutory Auditors for Anshu for the FY 2015-16 and CA Sachin Kansal, was the Engagement Partner (EP) on behalf of the Audit Firm. The EP was requested on 08.12.2021, to submit the Audit File<sup>2</sup> and Quality Control Policies of the firm as per SQC1<sup>3</sup>. In response, the EP furnished Audit File along with SQC Policy followed by the firm in a series of emails (last email dated 08.03.2022).
13. The non-compliances observed by the FRRB of ICAI in the financial statements of the Company were also sent to EP for clarification/ explanation on each of the issues- 30 days were given for the responses which were received on 20.05.2022.
14. After examination of the Audit File and materials available on record, a, *prima facie*, case of professional misconduct on the part of EP was found and accordingly SCN dated

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<sup>2</sup> As defined in para 6(b) of SA 230 of Audit Documentation

<sup>3</sup> Standard on Quality Control (SQC) 1, Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements

23.09.2022 under Section 132(4)(c) of the Act and Rule 11 of the National Financial Reporting Authority Rules, 2018 ('NFRA Rules 2018', hereafter) was issued to the EP, giving him time to respond till 23.10.2022.

15. The EP was charged in the SCN with professional misconduct on the following grounds:
  - a) failure to disclose material facts known to him, which are not disclosed in a financial statement, but disclosure of which is necessary in making such a financial statement, where he is concerned with that financial statement in a professional capacity,
  - 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 the 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 procedure of audit applicable to the circumstances.
16. On 25.10.2022, the EP sought an extension of time for replying to the SCN and was permitted to submit the reply to SCN by 15.11.2022. On 15.11.2022, the EP filed written submissions in response to the SCN along with a request for personal hearing in accordance with Rule 11(5) of NFRA Rules 2018. Accordingly, the EP was given personal hearing on 01.02.2023 through video conferencing, as requested by him vide email dated 27.01.2023.
17. During the personal hearing through video conferencing, the EP conveyed that his written reply dated 15.11.2022 was the final reply. He also submitted that as he was a newly qualified Chartered Accountant at the time of signing of financial statements of the company and it was his first audit of a listed company, the charges in the SCN may be viewed leniently.
18. This Order takes cognizance of all materials on record. The major lapses found on the part of the EP in the audit of the financial statements of Anshu for FY 2015-16 are failure to report non-compliance with AS. These are discussed in Part 'C' of this Order. Non-compliances with SAs are discussed in Part 'D' of this Order.

## C. FAILURE TO REPORT NON- COMPLIANCE WITH ACCOUNTING STANDARDS

### C.1 Non-provision of Interest Costs on Borrowings from Bank and NBFCs

19. The EP was charged with failure to report that the company had not recognised interest accrued, amounting to ₹143.98 lakhs, on loans from bank and NBFCs in violation of Section 128 and Section 129 of the Act and AS 1. Had the interest accrued been properly accounted for, the reported loss of ₹ 20.28 lakhs for FY 2015-2016 would have been ₹ 164.26 lakhs , about eight times of what was reported. This resulted in a material misstatement in the financial statements of the Company for FY 2015-16. The SCN stated that the Auditors' opinion in the Independent Auditors' Report that the financial statements give a true and fair view of the state of affairs of the company as on 31.03.2016 was false and misleading since the interest had not been accounted for by the company and the auditor had failed to identify this as a qualification in his auditor's report.
20. In response to the above, the EP submitted that the management was in negotiations with the Bank for a one-time settlement of the loan and hence, in his professional judgment, no additional interest expenses were payable to clear the dues of the Bank. The business, for which the loan was taken, was not profitable and going with management's judgment and acting with objectivity and professionalism to such real-life business situations, the EP had agreed with management's judgment. The EP has referred to a no-dues certificate dated 03.04.2018 from Bank of Baroda, wherein the loan was settled through a one-time settlement; he thus claimed that the judgment exercised by him at the time of the audit to agree with the decision of the management not to recognise further interest was neither misplaced nor without a proper basis.
21. The EP further stated that "*Provisions in AS 1 are not rigid to prevent a company management from taking pragmatic decisions.*" The EP stated that "*. . .as an auditor my judgment suggested that 'contractual obligations' if are incapable of being fulfilled and are not acknowledged any longer as liabilities by a company management' they can be excluded from the concept of "all known liabilities" as stated in the principle of 'prudence', in AS 1 Para 17.*" "*If there are factors that suggest that expenses that have become "due" are unlikely to be "paid", then they would not become expenses "incurred" up on becoming "due" automatically until and unless the uncertainty over its payment is removed. These are finer principles of accounting practised to achieve the objective of true and fair state affairs in the financial statement.*" The EP has further argued that it was a case of error of judgment, which cannot become the basis to hold him guilty of professional misconduct.

22. We observe that while the EP justifies his action, he also admits that there was an error of judgment. The justifications of the EP are not acceptable for the following reasons:
- a. None of the claims of the EP are supported by the evidence in the Audit File. There are no documents in the Audit File which indicate any ongoing negotiations regarding the settlement of the loans. On the contrary, the Audit File contains a demand letter dated 02.01.2014 from Bank of Baroda for both the principal and the interest amount due and a response letter dated 03.01.2014 from the company stating that the company was working hard to arrange the funds. There is another letter dated 20.05.2014 from Bank of Baroda taking possession of the stocks because of the failure of the company to make the payment.
  - b. There was no evidence of a firm commitment from Bank of Baroda on waiver of interest at the time of the audit of FY 2015-16. The settlement with Bank of Baroda came into effect on 03.04.2018, i.e. 19 months after the signing of the balance sheet by the EP on 03.09.2016. The EP is using subsequent developments, that took place over one and a half years that followed, to justify his actions at the time of statutory audit.
  - c. The accrual concept in accounting requires a company to record revenue and expenses in the period they are earned or incurred, regardless of when the related cash transactions occur<sup>4</sup>. Liabilities, including contractual obligations, are recognized in the financial statements when they are incurred, even if payment is not due until a later period. This means that contractual obligations that are incapable of being fulfilled are still recognized as liabilities by a company, even if they are not acknowledged any longer by the management.
  - d. If a contractual obligation no longer meets the definition of liability, it may be excluded from the concept of “all known liabilities”. For example, if the company has successfully renegotiated the terms of loan agreement and the obligation has been significantly reduced, it may no longer meet the definition of liability and can be excluded from the financial statements. However, there is no such evidence in the Audit File. The Company, instead, had a present obligation, which was legally enforceable<sup>5</sup>. Thus, the interpretation of the EP regarding AS 1 and prudence are flawed and shows a poor understanding of the fundamentals of accounting. The subsequent settlement of the loan in 2018, much after the date of the audit report, had no relevance to the circumstances and facts prevailing at the time of audit.
  - e. By not providing for the interest accrued, the company has materially misstated the financial statements. The EP failed to report this material misstatement.

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<sup>4</sup> Para 22, Framework for the Preparation and Presentation of Financial Statements, issued by ICAI.

<sup>5</sup> Para 59 to 63 of the Framework for the Preparation and Presentation of Financial Statements.

23. Based on the above, the charges relating to failure to report non-provision of Interest Costs pertaining to Borrowings from bank and NBFCs stand proven. The omission being material in nature, the EP should have taken them into consideration before issuing his opinion in accordance with SA 705<sup>6</sup>, which he failed to do.

## **C.2 Non-provisioning for Trade Receivables- Unsecured, Considered Doubtful**

24. The SCN charged the EP for non-compliance of SA 705. During FY 2015-16, the company had not made provision for 'Trade Receivables- Unsecured, Considered Doubtful' of ₹ 709 lakhs, which constituted 22% of the total assets of the company. The SCN noted that the EP had also stated in his Auditor's Report in the section for "*Basis of Qualified Opinion*" as under:

*"In respect of balances of receivables and payables confirmation and reconciliation is unsecured and doubtful. Impact is uncertain and cannot be commented by us. For receivables considered doubtful and no provision has been created in the books of accounts."*

25. However, in the paragraph titled "*Qualified Opinion*" EP opined that the Financial Statements give a true and fair view without any qualification or reference to the "*Basis of Qualified Opinion*" section as required under Para 23<sup>7</sup> of SA 705.
26. In response to the above charge, EP replied that "*the Respondent wanted to qualify the non-provisioning of doubtful trade receivables*" and that "*it was an unintended mistake. Although the mistake is on the face of the audit report, a combined reading of the report would make clear the intention of the auditor. A reader of the report would not be misled by the audit report; however, there is room for criticism for not taking care of the draft of the document sufficiently.*"
27. Though the EP admits non-compliance with SA 705, the justifications and reasons submitted are not acceptable. SA 200 requires the auditor to comply with all SAs relevant to the audit and mandates an understanding of the entire text of an SA, including its application and other explanatory material, to understand its objectives and to apply its

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<sup>6</sup> SA 705, Modifications to the Opinion in the Independent Auditor's Report

<sup>7</sup> Para 23 of SA 705 states that "*When the auditor expresses a qualified opinion due to a material misstatement in the financial statements, the auditor shall state in the opinion paragraph that, in the auditor's opinion, except for the effects of the matter(s) described in the Basis for Qualified Opinion paragraph:*

- (a) The financial statements present fairly, in all material respects (or give a true and fair view) in accordance with the applicable financial reporting framework when reporting in accordance with a fair presentation framework; or*
- (b) The financial statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework when reporting in accordance with a compliance framework.*

*When the modification arises from an inability to obtain sufficient appropriate audit evidence, the auditor shall use the corresponding phrase "except for the possible effects of the matter(s)..." for the modified opinion."*

requirements properly. Objective of SA 705 is to express *clearly* an appropriately modified opinion on the financial statements when the conditions for modifications are met. The opinion expressed in this case is ambiguous as the basis of qualification did not have a proper description and quantification of the financial effects of the misstatement or other explanations as required by Para 17 of SA 705. Hence, the audit opinion is not meeting the objective of SA 705. Such an opinion is misleading to the users of the financial statements as well. The charges regarding non-compliance with SA 705, therefore, stand proven.

### C.3 Wrong Accounting of Deferred Tax Assets

28. The Company had recognized Deferred Tax Assets (DTA) of ₹9.07 lakhs in FY 2015-16. As per the Statement for Profit and Loss, the Company had a net loss of ₹143.96 lakhs and ₹20.28 lakhs in FY 2014-2015 and FY 2015-2016 respectively (after considering the DTA of ₹64.38 lakhs in FY 2014-2015 and ₹9.07 lakhs in FY 2015-2016). As there was no evidence in the Audit File to indicate the sufficiency of taxable income in future to realise such DTA, the recognition of DTA was, *prima facie*, misplaced as in the facts and circumstances of the case realisability of such an asset was questionable. The EP was therefore charged with not qualifying the audit report with respect to recognition of DTA in contravention of the requirements of AS 22<sup>8</sup>.
29. The EP admitted that “*there was unintended oversight in verifying the compliance of AS 22*”. He has further argued that the impact of the error did not constitute material misstatement as the DTA constituted less than 2% of the Balance Sheet and did not impact ‘profit/loss before tax’ which is generally taken as the base for assessing material misstatement. The EP submitted that “*the error that had very minimal impact on the financial statement did not make a case of professional misconduct although it was an error of judgment in the application of Accounting Standard 22, . . .*”.
30. The EP has stated that his responsibility as per Section 143(2) of the Act was to ensure that the accounts are true and fair to the best of his information and knowledge and are as per the provisions of the Act and the Accounting and Auditing Standards. He has further stated that as per SA 700, he has to give a “*reasonable assurance*” and not “*absolute assurance*”.
31. Although the EP accepts that non-verification of compliance with AS 22 was an oversight, he seeks to rely on SA 700 which refers to ‘*reasonable assurance*’ and he further points to the deferred tax assets not being material. The reference by the auditor to reasonable assurance as given in SA 700 has no relevance in this matter. It is apparent that the DTAs have been recognised in contravention of the relevant Accounting

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<sup>8</sup> As per paragraph 17 of AS 22, Accounting for Taxes on Income, “*Deferred tax assets should be recognized only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised*”.



Standards and the same has not been denied. Recognition of DTA in a company, which is continuously incurring losses and not having reasonable certainty of sufficient future taxable income, was erroneous and misleading for the users of the financial statements. It is the duty of the Auditor to exhibit due diligence and question the management on the same and point it out in the Independent Auditor's Report.

32. Further, the auditor's explanation that the DTA constitutes only 2% of the total balance Sheet size and hence is not material, cannot be accepted as the losses of the company in FY 2015-16 have been significantly understated by 33% on account of recognition of DTA . Regarding the issue of DTA not being material we find that there is no document regarding determination of materiality thresholds in the Audit File as required by SA 320<sup>9</sup>. In view of this, his plea cannot be accepted. It reflects the management's intention to depict a better financial position of the company than what existed and the auditor's failure to point this out.
33. As DTA is an accounting estimate, as per para 8 of SA 540<sup>10</sup>, the auditor needs to obtain an understanding of the requirements of the applicable financial reporting framework relevant to accounting estimates, including related disclosures. The EP, in this case, has not obtained a clear understanding of the provisions of AS 22 about the recognition of DTA in the financial statements of the company and failed to report non-compliance with AS 22 by the company.
34. It is noted that there is no documentation of evaluation of misstatement identified during the audit as required under SA 450<sup>11</sup>. It is important to note that SA 450 requires the auditor to accumulate misstatements identified during the audit, determine whether overall audit strategy and audit plan needs revision, communicate all misstatements accumulated to the appropriate level of management, evaluate the effect of uncorrected misstatements after reassessing materiality in the context of entity's actual financial result and determine whether uncorrected misstatements are material individually or in the aggregate taking into account the financial statements as a whole and also communicate the same to TCWG. However, none of these steps were performed by the EP. As per para 5 of SA 200, '*reasonable assurance*<sup>12</sup>' is a high level of assurance and is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce audit risk to an acceptably low level. In the absence of such an evaluation in the Audit File, there is no evidence of how the EP assured himself of "*reasonable assurance*". Hence the arguments regarding DTA not being material and being 2% of total balance

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<sup>9</sup> SA320, Materiality in Planning and Performing an Audit

<sup>10</sup> SA 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures

<sup>11</sup> SA 450, Evaluation of Misstatements identified during the Audit.

<sup>12</sup> Reasonable assurance means high, but not absolute, level of assurance as per Glossary of Term issued by ICAI

sheet are afterthoughts and the charges regarding non-reporting the wrong accounting of DTA stand proven.

#### **C.4 Non-disclosure of Cost Formula for the Measurement of Inventories**

35. The EP was charged for not reporting that the cost formula for the measurement of inventory was not disclosed by the company in its Financial Statements.
36. The disclosure in the Accounting Policy for cost of inventories stated that *“The Finished goods are valued at lower of cost or net realizable value. Consumable Stores & Spares and packing material are written off at the time of purchase itself.”* The cost formula for calculation of the cost of the inventory (say, First In First Out, weighted average cost, specific cost etc.) is not given in the financial statements. The Audit File also does not contain any work paper regarding the cost formula used by the company. This is in contravention of Para 26(a) of AS 2<sup>13</sup> which mandates the disclosure of accounting policies regarding inventories including the cost formula.
37. In response to the above charge, the EP clarified that the company was in the trading of apparel and each item of apparel has a unique cost and therefore, Para 14 and 15 of AS 2 assigning specific cost to the identified items of inventory was applicable to the firm. He further submitted that these are matters of general information to the auditor and do not require any specific mention in audit working papers and requested not to take any adverse view in this regard.
38. The replies of the EP are not acceptable as disclosure of cost formula for inventory is a mandatory requirement under the AS 2 and the financial statements of the company do not indicate the same. Use of specific cost for measurement is also a type of cost formula and should have been included in the Accounting Policies of the company. Use of different formulae permitted under para 14-17 of AS 2 can have material impact on the carrying amount of inventories in the Balance Sheet & cost of sales in the Profit or Loss. Therefore, disclosure of cost formula in the Financial Statements has relevance & significance to the users. As a diligent auditor, it was necessary for him to take up with the TCWG/Management to ensure that there is proper disclosure of accounting policy. In the absence of such action taken by the EP or any work paper in the Audit File pointing to same, the charge regarding not reporting the non-disclosure of cost formula for valuation of inventories in the financial statements stands proven.

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<sup>13</sup> Para 26 of AS 2, Valuation of Inventories, states as under:

*“26. The financial statements should disclose:*

*(a) the accounting policies adopted in measuring inventories, including the cost formula used; and  
(b) the total carrying amount of inventories and its classification appropriate to the enterprise.”*

## C.5 Wrong amortization of Expenses

39. The EP was charged with non-reporting of violations of AS 26<sup>14</sup> regarding amortization of expenses. The disclosures in the annual financial statements show unamortized expenses (to the extent not written off) as given in the table below:

(₹ in lakhs)		
<b>Other non-current assets</b>	<b>31.03. 2016</b>	<b>31.03.2015</b>
(a) Unamortised expenses (to the extent not w/off)		
(i) Deferred Revenue Brand Development Expenditure	5.21	5.21
(ii) Preliminary Expenses	1.97	1.97
(iii) Listing Expenses	30.33	29.62
(iv) Interest due but not Paid	10.37	10.37
(v) MAT Credit Entitlement	0.44	0.44
<b>Total</b>	<b>48.32</b>	<b>47.61</b>
Source: Page 60 of Annual Report under Note 14: Other non-current assets of the annual financial statements		

40. It was charged in the SCN that:

- a. Preliminary Expenses and Listing Expenses do not meet the definition of non-current assets<sup>15</sup> as no future economic benefits are expected to flow to the company through these expenses.
- b. Audit File does not clearly indicate whether ‘*Deferred Revenue Brand Development Expenditure*’ satisfies the conditions of para 44<sup>16</sup> of AS 26 which provides the conditions for recognition of intangible assets arising from development (or from development phase of an internal project). Only when these conditions are satisfied this

<sup>14</sup> AS 26, Intangible Assets

<sup>15</sup> Para 6.2 of AS 26 reads as under:

“6.2 An asset is a resource:

(a) controlled by an enterprise as a result of past events; and (b) from which future economic benefits are expected to flow to the enterprise.”

<sup>16</sup> Para 44 of AS 26 reads as under:

“44. An intangible asset arising from development (or from the development phase of an internal project) should be recognised if, and only if, an enterprise can demonstrate all of the following:

(a) the technical feasibility of completing the intangible asset so that it will be available for use or sale;

(b) its intention to complete the intangible asset and use or sell it;

(c) its ability to use or sell the intangible asset;

(d) how the intangible asset will generate probable future economic benefits. Among other things, the enterprise should demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset;

(e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and

(f) its ability to measure the expenditure attributable to the intangible asset during its development reliably.”

expenditure can be recognized as an intangible asset and amortized over a period. The Audit File did not have any work paper in this regard.

- c. Recognition of MAT Credit Entitlement presented as Unamortized Expenses is not in compliance with AS 22 <sup>17</sup>.
41. In response to the above charges, EP has admitted his mistake and was of the view that these were presentation errors and not material and sought pardon for the same.
42. In light of the auditor's acceptance of his errors, it is clear that the provisions of AS 26 and AS 22 have not been adhered to and the charge regarding non-reporting of the wrong amortization of expenses stands proven.

### **C.6 Non-compliance with the format of Financial Statements**

43. The Company was required under Section 129(1) of the Act to prepare financial statements in the format provided in Division I of Schedule III to the Act. Multiple non-compliances with the format were observed in the financial statements of the company and the EP was charged with not reporting the same. Non-compliances observed in the format of financial statements are given below:
  - a. Period from which the company had been continuously defaulting on loans and interest is not indicated<sup>18</sup>. In the annual report, it is only stated that the company has discontinued the payment of interest to the bank, or the payment of secured and unsecured loans.
  - b. Only the names of the partnership firms are given in Note 12 (Non-Current Investments) of the financial statements, other details like names of all their partners, total capital and the shares of each partner are not given. These details are required as per Para 6K of '*General Instructions for preparation of Balance Sheet*' under Division I of Schedule III to the Act.
  - c. As per Division I of Schedule III to the Act, securities deposit should be disclosed under long-term loans and advances and Fixed Deposit Receipts against bank guarantees under Cash and Cash Equivalents. However, the company has included both under other current assets.

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<sup>17</sup> Para 30 of AS 22, Accounting for Taxes on Income, reads as "30. Deferred tax assets and liabilities should be distinguished from assets and liabilities representing current tax for the period. Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities."

<sup>18</sup> As per Division I of Schedule III to the Act, the period and amount of continuing default as on the Balance Sheet date in the repayment of loans and interest needs to be specified separately.

- d. In Note no 13: Long term loans and advances, the nature of other loans and advances is given as '*advances recoverable in cash or in kind*' which is very generic and does not give any information about the nature of the other loans and advances.
44. In his response to the SCN, the EP has admitted the presentation errors in the financial statements as listed above. The EP has further submitted that presentation errors do not have any significant adverse effect on a reader's ability to understand the contents in the financial statements and that the presentation errors made by the management of the company may not be considered as omission on the part of the Auditor.
45. We observe that Section 129(1) of the Act very clearly states that the financial statements shall be in the format as may be provided for different class or classes of companies in Schedule III. Therefore, any deviation from the prescribed format is a non-compliance with the statutory provisions and therefore the auditor's submission in this regard is unacceptable as it is auditors' responsibility to report such non-compliances with the prescribed format.

#### **D. NON-COMPLIANCES WITH STANDARDS OF AUDITING**

##### **D.1 Non-compliance with requirements of SA 230 regarding Audit Documentation**

46. The EP was charged with false reporting that the Audit was conducted in accordance with SAs despite non-compliance with a large number of SAs. Para 8 and 9 of SA 230<sup>19</sup> requires an Auditor to "*prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand*". The EP had failed to comply with para 8 and 9 of SA 230<sup>20</sup>, as the nature, timing and extent of audit procedure performed, results thereof, audit evidence obtained, and conclusions reached are not documented in the Audit File.
47. Para 14 and A21 of SA 230<sup>21</sup> mandates the assembly of the final Audit File within 60 days after the date of the auditor's report. The EP was charged for not assembling the Audit File within 60 days of signing of audit report as he did not send the Audit File to

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<sup>19</sup> SA 230 , Audit Documentation

<sup>20</sup> Para 8 of SA 230 states that "*The auditor shall 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.*"

<sup>21</sup> Para 14 of SA 230 states that "*the auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report*". Para A21 of SA 230 states that "*SQC 1 requires firms to establish policies and procedures for the timely completion of the assembly of audit files. An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report*".

NFRA by 07.01.2022 as advised by NFRA vide letter dated 08.12.2021.

48. The auditor in his reply dated 15.11.2023 has agreed to the lapses in Audit documentation. He has admitted that *“the Audit File was not compiled in accordance with the provisions of SA 230 within the timeframe of six months since the audit, it is submitted that the audit working papers were scattered in different files....”*
49. As per para A21 of SA 230, *Audit Documentation*, the Audit File needs to be compiled within a period of 60 days from the date of signing of the Audit Report, not six months as mentioned by EP. This time period of sixty days is given in the Standards on Auditing taking into consideration the constraints faced by the chartered accountants. As the auditor has stated that the documents were scattered in various files and have been compiled only for the submission of Audit File to NFRA, it is evident that the Audit File had not been compiled by the Auditor even after 5 years of signing of Audit Report. The charges against the EP are, therefore, proved.
50. We observe in this regard that the lack of sufficient documentation in an audit is not a mere technical and procedural formality but is a serious issue which strikes at the very root of the audit and may defeat the very purpose of the audit itself. 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 on the lack of sufficient documentation and imposed penalties and sanctions for violations including insufficient documentation. The PCAOB Order dated 19.03.2019 in the aforesaid matter stated *“Audit documentation must contain sufficient information to enable an experienced auditor, having no previous connection with the engagement to (a) understand the nature, timing, extent, and results of the procedures performed, evidence obtained, and conclusions reached, and (b) determine who performed the work and the date such work was completed as well as the person who reviewed the work and the date of such review .....the documentation for each of those audits was insufficient to demonstrate the nature, timing, extent, and results of the procedures performed, evidence obtained, and conclusions reached, including in those areas of the audits involving significant risks. For the FY 2016 and 2017 Issuer A audits, the documentation also failed to demonstrate who performed the work and the date such work was completed. Additionally, in each of the Issuer A and Issuer B audits, the audit documentation was insufficient to demonstrate which aspects of the audit and which audit documentation Bharat Parikh reviewed”*.
51. In another case of delayed Audit Documentation viz., Alvarez and Associates Inc, an audit firm registered with PCAOB, where Vincente Alvares was a partner, PCAOB<sup>22</sup> noted *“.... also violated AS 1215, Audit Documentation (“AS 1215”) by repeatedly*

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<sup>22</sup> PCAOB Release No. 105-2022-039 dated December 21, 2022

*failing to timely assemble a complete and final set of audit documentation assembled for retention (“archived”) by the documentation completion date (i.e., within 45 days after the report release date) for 43 broker-dealer Audits for FY 2018 and FY 2019. The Firm and Alvarez further violated AS 1215 by repeatedly failing to document the information required by AS 1215 when audit documentation was changed after the documentation completion date for 25 broker-dealer Audits for FY 2018 and FY 2019.”* In this matter, Alvarez & Associates, Inc., and Vicente Alvarez, were censured and registration of Alvarez & Associates, Inc. was suspended for two years. Vicente Alvarez, CPA was debarred for two years and was required to complete 40 hours of professional education and training relating to PCAOB auditing standards and covering, among other topics, audit documentation and the performance of engagement quality reviews.

## **D.2 Non-compliance Regarding Agreement on Terms of Audit Engagements**

52. The EP was charged for not complying with para 9 read with para A20 and para 10 read with para A21-A24 of SA 210<sup>23</sup>, as the Audit File did not contain the agreement on the terms of audit engagements with management or Those Charged with Governance (TCWG).
53. In response, the EP has stated that the Audit Engagement Letter issued to the company was in response to the appointment made in the previous year, and hence it was not amongst the documents in the audit records of FY 2015-16. The EP asked to be pardoned for this omission.
54. The contention of the EP is not acceptable as in case of recurring audits, Para 12<sup>24</sup> of SA 220 requires an assessment from the auditor of whether circumstances require the terms of the audit engagement to be revised and whether there is a need to remind the entity of the existing terms. There is no document evidencing such an assessment and there is no such procedure documented in the Audit File. Moreover, there was no audit engagement

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<sup>23</sup> SA 210, *Agreeing the Terms of Audit Engagements*

Para 9 of SA 210 reads as under:

*“The auditor shall agree the terms of the audit engagement with management or those charged with governance, as appropriate. (Ref: Para. A20)*

Para 10 of SA 210 reads as under:

*“Subject to paragraph 11, the agreed terms of the audit engagement shall be recorded in an audit engagement letter or other suitable form of written agreement and shall include: (Ref: Para. A21-A24)*

*(a) The objective and scope of the audit of the financial statements;*

*(b) The responsibilities of the auditor;*

*(c) The responsibilities of management;*

*(d) Identification of the applicable financial reporting framework for the preparation of the financial statements; and*

*(e) Reference to the expected form and content of any reports to be issued by the auditor and a statement that there may be circumstances in which a report may differ from its expected form and content.”*

<sup>24</sup> Para 12 of SA 220 reads as under:

*“12. The engagement partner shall be satisfied that appropriate procedures regarding the acceptance and continuance of client relationships and audit engagements have been followed, and shall determine that conclusions reached in this regard are appropriate. (Ref: Para. A8-A9)”*

letter (as prescribed by SA 210) in the Audit File. Hence the charges against EP stand proven.

### **D.3 Non-compliance Regarding Appointment of Engagement Quality Control Reviewer**

55. The EP was charged for not complying with para 19(a) of SA 220<sup>25</sup> and para 60<sup>26</sup> of SQC-1 as there was no evidence that he had determined that Engagement Quality Control Reviewer (EQCR, hereafter) had been appointed, which is required for audits of listed entities.
56. Replying to the above charge, the EP submitted that he is the proprietor of the audit firm. There are no other persons accountable for this assignment. Therefore, there was no requirement for the appointment of any other person on quality control.
57. The reply of the EP cannot be accepted in view of the following:
- (i) The audit firm needs to ensure that the engagements are undertaken only when it is competent to perform the engagement and has the capabilities, time and resources to do so.<sup>27</sup> In considering whether the firm has capabilities, competence, time and resources to undertake a new engagement the firm needs to ensure, *inter alia*, that the individuals meeting the criteria and eligibility requirements to perform engagement quality control review are available, where applicable.<sup>28</sup>
  - (ii) As Anshu is a listed entity, it was mandatory for the auditor to determine that an EQCR had been appointed for review of the audit work.<sup>29</sup> Accordingly, while accepting the said engagement, the Audit Firm should have assessed whether the individuals meeting the criteria and eligibility requirements to perform EQC Review were available.
  - (iii) As per para 6 of SQC1, EQCR may be '*a partner, other person in the firm, suitably qualified external person, or a team made up of such individuals, with sufficient and appropriate experience and authority to objectively evaluate, before the report is issued, the significant judgments the engagement team made and the conclusions they*

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<sup>25</sup> SA 220, Quality Control for an Audit of Financial Statements

<sup>26</sup> Para 60 of SQC1 reads as under:

*"The firm should establish policies and procedures requiring, for appropriate engagements, an engagement quality control review that provides an objective evaluation of the significant judgments made by the engagement team and the conclusions reached in formulating the report.*

*Such policies and procedures should:*

*(a) Require an engagement quality control review for all audits of financial statements of listed entities;*

*(b) . . . "*

<sup>27</sup> Para 28 of SQC1

<sup>28</sup> Para 31 of SQC1

<sup>29</sup> Para 19 of SA 220



reached in formulating the report'. Further, as per para 72 of SQC1, '*suitably qualified external persons may be contracted where sole practitioners or small firms identify engagements requiring engagement quality control reviews. Alternatively, some sole practitioners or small firms may wish to use other firms to facilitate engagement quality control reviews.*' Hence, being a proprietary firm cannot be accepted as an excuse not to have engagement quality control review when there is a mandatory requirement.

- (iv) The firm's policies and procedures should require the completion of the engagement quality control review before the report is issued.<sup>30</sup> The Independent Auditors Report of Anshu Clothing Limited was issued on 03.09.2016. It should have been ensured by the Audit Firm that the engagement quality control review had been completed before the report was issued. In this case since the Audit Firm was a proprietary firm and CA Sachin Kansal was the EP and the proprietor of the firm, he should have ensured that the said requirement was met.

Hence, the charge that the EP did not comply with the requirements regarding appointment of EQCR stands proven.

58. In a case wherein Engagement Quality Review has not been done by the auditors, PCAOB<sup>31</sup> has observed that "*For audits of financial statements for fiscal years beginning on or after December 15, 2009, AS 7 requires that an engagement quality review be performed on audits, interim reviews, and certain attestation engagements conducted pursuant to PCAOB standards.6 AS 7 also provides that a firm may grant permission to a client to use the engagement report only after an engagement quality reviewer provides concurring approval of issuance of the report. . . . the Firm failed to obtain an engagement quality review for each of the audits described below even though an engagement quality review was required to be performed and Donahue directly and substantially contributed to those violations.. . .In connection with an October 2012 inspection of the Firm, the PCAOB's Inspections staff reminded the Firm that it needed to comply with AS 7 for all audits and interim reviews performed by the Firm for fiscal years beginning on or after December 15, 2009. Despite being on notice, the Firm failed to comply with AS 7 regarding the performance of engagement quality reviews in connection with the audits described below.*" In this case as well, Donahue Associates LLC, and Brian D. Donahue, CPA was censored; registration of Donahue Associates LLC was revoked for one year; Brian D. Donahue, CPA was debarred for being an Associated person with any Public Accounting Firm for one year and a monetary penalty was imposed on the firm by PCAOB.

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<sup>30</sup> Para 61 of SQC1

<sup>31</sup> PCAOB Release No. 105-2016-020 dated June 14, 2016

#### D.4 Non-compliance Regarding Communication with TCWG

59. The EP was charged for not complying with para 7, 10, 11, 12, 13 & 19 of SA 260<sup>32</sup> & SA 265<sup>33</sup> as he did not determine TCWG and did not communicate with TCWG about the responsibilities of auditor, overview of planned scope and timing of the audit etc. and did not make required documentations. The Audit File did not have any documentation regarding communication with TCWG.

60. In reply to the charge, the EP has explained that communications with management were face to face during audit and by sharing draft audit report physically and hence no written communications existed. This explanation by EP cannot be accepted.

61. In the above context, it is important to reiterate Para 19 of SA 260 as under:

*“Where matters required by this SA to be communicated are communicated orally, the auditor shall document them, 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.”*

It is clear that in case the communication is done orally, it is the duty of Auditor to document the same. In the Audit File, there is no documentation of communication with TCWG. The charges regarding non-compliance for communication with TCWG therefore stand proven.

62. The EP has further submitted in his written reply *“that natural justice demands a lenient view of the Hon Authority in the case of the Respondent because the assessment of audit risk in the audit of Anshu’s by the Respondent was in the context that the total audit fees of the assignment was ₹30,000 Unintended omissions as a result of errors in judgment of audit risk may be pardoned in view of the provisions in Paras A45, A46 and A 52 of SA 200. The respondent being a small proprietorship firm, the hon Authority may prescribe the sanctions based on the principles of proportionally”*.

63. We note that the fee, which is agreed and accepted by the EP, cannot be an excuse for rationalizing the poor audit quality at a subsequent stage. The EP was at liberty not to accept an engagement if it was financially not viable. In the matter of *The Fairdeal Corporation Ltd. Bombay vs. K.Gopalakrishna Rao (quoted in ICAI Code of Ethics, 2009, Page 361 of Vol. III of the Disciplinary Cases)*, where a Chartered Accountant, appointed as auditor of the Madras branch of a limited Company at Bombay (now Mumbai), was charged with failure to report to the Bombay Office that some entries in the bank pass book had not been passed through the cash book of the branch, was held

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<sup>32</sup> SA 260, Communication with those Charged with Governance

<sup>33</sup> SA 265, Communicating Deficiencies in Internal Control to Those Charged with Governance and Management

guilty of gross negligence. The High Court observed that a small fee paid to the Respondent should not come in the way of his doing his duty without fear or favour, although it involved unpleasant consequences, namely, he might not be appointed again.

64. During the personal hearing conducted on 01.02.2023, the EP conveyed that his written submissions dated 15.11.2022 were his final replies. He further added that neither he nor the company had any intention of misappropriating funds. The mistakes made in the audit were unintended and happened due to lack of knowledge of accounting standards and standards on auditing. He further added that he was a budding Chartered Accountant and had only four years of experience at the time of this audit. It was his first audit of a listed company and that he is not doing audits of any listed companies anymore. In addition, the EP showed his inclination for further studying the Accounting Standards and Standards on Auditing and the Act and submitted that the sanctions be imposed lightly lest they adversely impact his career.

#### **E. ARTICLES OF CHARGES OF PROFESSIONAL MISCONDUCT**

65. Given the above-mentioned actions and omissions, it is established that CA Sachin Kansal did not comply with the stipulations in the Act and the Chartered Accountants Act, 1949 (CAs Act, hereafter) and showed gross negligence and lack of due diligence in the audit of the said engagement. CA Sachin Kansal has not ensured audit quality and was grossly negligent in professional duties by not adhering to the requirements laid down by the relevant SAs. This has led to the issuance of an audit report not backed by audit evidence. Specifically, the following failures on the part of CA Sachin Kansal as contained in the Articles of Charges in the SCN stand established:
- 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, as CA Sachin Kansal failed to disclose in his report the material non-compliances the company made regarding non-provision of interest and regarding wrong accounting of deferred tax assets(as per Section 22 and Clause 7 of Part I of the Second Schedule to the CAs Act);
  - b) Failure to report a material misstatement known to him to appear in a financial statement with which he is concerned in a professional capacity, as CA Sachin Kansal failed to disclose in his report the material misstatements made by the Company in the area of non-recognition of interest costs pertaining to Borrowings by the lender banks and wrong accounting of deferred tax assets (as per Section 22 and Clause 7 of Part I of the Second Schedule to the CAs Act);
  - c) Failure to exercise due diligence and being grossly negligent in the conduct of

professional duties, because of the lapses and omissions as explained and proved in parts C and D above (as per Section 22 and Clause 7 of Part I of the Second Schedule to the CAs Act);

- d) Failure to obtain sufficient information which is necessary for the expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion, because of the lapses and omissions as explained and proved in part C and D above (as per Section 22 and Clause 8 of Part I of the Second Schedule to the CAs Act); and
- e) Failure to invite attention to material departure from the generally accepted procedures of audit applicable to the circumstances, because he certified in his report that the audit was done as per SAs mandated under Section 143 of the Act and committed the lapses and omissions as explained and proved in part C and D above (as per Section 22 and Clause 9 of part I of the Second Schedule to the CAs Act).

Thus, we conclude that CA Sachin Kansal committed professional misconduct, as defined in the respective clauses of the CAs Act, which is also professional misconduct under Section 132 (4) of the Companies Act.

#### **F. PENALTY & SANCTIONS**

- 66. Section 132(4) of the Companies Act, 2013 provides for penalties in a case where professional misconduct is proved. The seriousness with which the Companies Act views cases of professional misconduct is evident from the fact that a minimum punishment is laid down by the law.
- 67. The primary function of the Auditor is to ensure compliance with SAs to achieve the necessary audit quality that lends credibility to financial statements and facilitates its users. A critical, questioning attitude, an unwillingness to be satisfied by superficial explanations, not concluding on material matters without rigorous verification, diligent and methodical cross verification, proper planning, and meticulous execution of the audit plan etc. are fundamental to audit quality. As detailed in this Order, it is evident that the EP during the Audit of Anshu has failed to report non-compliance with Accounting Standards and the prescribed format of Financial Statement as per the Companies Act, 2013, and has not complied with several requirements of Standards on Auditing.
- 68. We note that both in his written reply to the SCN and during personal hearing, the EP has not only agreed with the violations identified in the SCN, but has expressed regret citing lack of experience and knowledge of the accounting and auditing standards and has expressed inclination to further study Accounting Standards and Standards on Auditing to improve his knowledge. Since there are gaps in the EP's understanding of SAs that need to be addressed, CA Sachin Kansal would benefit from further training in the area of SAs to enhance his skills as an auditor capable of carrying out the audit of

public interest entities.


69. Considering the proven professional misconduct by CA Sachin Kansal, acceptance of mistakes by him, the nature of violations, size of the audit firm, and applying the principles of proportionality, we order the following sanctions under Section 132(4)(c) of the Companies Act, 2013:
- (i) Imposition of a monetary penalty of ₹ 1,00,000 (Rupees One Lakh) upon CA Sachin Kansal.
  - (ii) CA Sachin Kansal is debarred for one year from being appointed as an auditor or internal auditor or undertaking any audit in respect of financial statements or internal audit of the functions and activities of any company or body corporate.
70. This Order will be 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 National Financial Reporting Authority

  
(Vidhu Sood)  
Secretary

Date: 27.07.2023  
Place: New Delhi

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

To,  
CA Sachin Kansal  
ICAI Membership No.: 137191  
M/s S. Kansal & Associates  
Firm Registration No.: 134937W  
A-11, SF, Millennium Plaza, Mansi Circle, Vastrapur  
Ahmedabad, Gujarat-380015  
Email: [sachinkansal077@gmail.com](mailto:sachinkansal077@gmail.com)

Copy to:-

- (i) Secretary, Ministry of Corporate Affairs, Government of India
- (ii) Securities and Exchange Board of India
- (iii) Institute of Chartered Accountants of India
- (iv) M/s Anshu's Clothing Ltd (now known as Aditri Gems & Jewels Ltd)
- (v) IT-Team, NFRA for uploading the order on the website of NFRA