

INSPECTION REPORT 2022

Audit Firm: Deloitte Haskins & Sells LLP
Firm Registration No. 117366W / W-100018
Inspection Report No. 132.2-2022-02
December 22, 2023

राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण

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PART A

Executive Summary

Section 132 of the Companies Act 2013, inter alia, mandates the National Financial Reporting Authority (NFRA), to monitor compliance with Auditing and Accounting Standards, to oversee the quality of service of the professions associated with ensuring compliance with such standards, and to suggest measures required for improvement in the quality of their services. The relevant provisions of NFRA Rules prescribe the procedures in this regard, which include evaluation of the sufficiency of the quality control system of Auditors and the manner of documentation of their work. NFRA initiated audit quality inspection of Deloitte Haskins and Sells LLP (DHS LLP) in December 2022. The scope of the inspection included a review of firm-wide quality controls to evaluate Audit Firm's adherence to SQC 1¹ and review of selected Audit Documentation of the annual statutory audit of financial statements for the year ending 31.03.2021. Three significant audit areas were identified in respect of each audit engagement viz., Revenue, Trade Receivables and Investments, due to their inherent higher risk of material misstatement. The on-site inspection was carried out between December 2022 and January 2023.

During the inspection, the Inspection Team held discussions with the Audit Firm personnel, reviewed policies and procedures and examined documents to arrive at the prima facie observations. These observations were conveyed to the Audit Firm. After examining the replies, NFRA conveyed a draft inspection report to the Audit Firm. The replies and documents submitted by the Audit Firm have been examined, incorporated in this report, where considered appropriate. Key observations in this report are summarised as follows:

- a) It was observed that engagement level independence confirmations of some members of the Engagement Team (ET) and others in respect of four engagements were not obtained/retained in the Engagement Management System (EMS-Audit File) (Para 13-17).
- b) The Audit Firm did not reassess and recategorize audit risk in one engagement as required by SA 315² and its own policy manual (Para 18-22).

¹ Standards on Quality Control 1 (SQC 1), Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and other Assurance and Related Services Engagements

² Standard on Auditing (SA) 315, Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment

- c) It was observed that there is no Board as envisaged in the Networking Agreement (Para 23-25).
- d) In one engagement, Engagement Quality Control Review (EQCR) Docket (summary of EQCR work performed) generated through EQCR Portal was not incorporated in the EMS as evidence of the performance of EQCR (Para 26-29).
- e) It was observed in the case of one engagement, that during consultation process, the Audit Firm did not record the basis/rationale of the decision arrived at (Para 30-32).
- f) In one engagement, the Audit Firm provided non-audit services which amounted to self-review threat (Para 37-42).

Inspection Overview

1. Section 132 of the Companies Act 2013, inter alia, mandates the National Financial Reporting Authority (NFRA), to monitor compliance with Auditing and Accounting Standards, to oversee the quality of service of the professions associated with ensuring compliance with such standards, and to suggest measures required for improvement in the quality of their services. The relevant provisions of NFRA Rules prescribe the procedures in this regard, which include evaluation of the sufficiency of the quality control system of Auditors and the manner of documentation of their work. Under this mandate, NFRA initiated audit quality inspections in December 2022. The overall objective of audit quality inspections is to evaluate compliance of the Audit Firm/Auditor with auditing standards and other regulatory and professional requirements, and the sufficiency and effectiveness of the quality control systems of the Audit Firm/Auditor, including:
 - (a) adequacy of the governance framework and its functioning;
 - (b) effectiveness of the firm's internal control over audit quality; and
 - (c) system of assessment and identification of audit risks and mitigating measures
2. Inspections involve a review of the quality control policy, review of certain focus areas, test check of the quality control processes, and test check of audit engagements performed by the Audit Firm during the year.
3. Inspections are, however, not designed to review all aspects and identify all weaknesses in the governance framework or system of internal control or audit risk assessment framework and are also not designed to provide absolute assurance about the Audit Firm's quality of audit work. In respect of selected audit assignments, inspections are not designed to identify all the weaknesses in the audit work performed by the auditors in the audit of the financial statements of the selected companies.

4. Inspections are intended to identify areas and opportunities for improvement in the Audit Firm's system of quality control. Inspection reports are also not intended to be either a rating or a marketing tool for Audit Firms.

Audit Quality Inspection Approach

5. Selection of Audit Firms for the 2022 inspections was based upon the extent of public interest involved, as evidenced by the size of the firm, its composition and nature, the number of audit engagements completed in the year under review, complexity and diversity of preparer's financial statements (henceforth, Companies) audited by the Audit Firm and other such risk indicators. M/s DHS LLP was one of the Audit Firms selected as per the above parameters.
6. The selection of individual audit engagements of the Audit Firm was largely risk-based, using and based on financial and non-financial risk indicators identified by NFRA. Accordingly, the Audit Files in respect of five (5) audit engagements relating to the statutory audit of financial statements for the year ending 31.03.2021 were reviewed during the inspection.
7. The scope of the inspection was as follows:
 - a. Review of firm-wide quality controls to evaluate the Audit Firm's adherence to SQC1, Code of Ethics and the applicable Laws and Rules. Focus areas for the 2022 inspection related to critical elements of the Firm's quality control system viz. leadership responsibilities within the Firm, auditor independence, acceptance and continuation of audit clients, engagement quality control and the Audit Firm's internal quality inspection program.
 - b. Review of individual Audit Engagement Files- A sample of five (5) individual audit engagement files pertaining to the annual statutory audit of financial statements for the year ending 31.03.2021 was selected. Three significant audit areas were identified in respect of each audit engagement viz., revenue, trade receivables and investments, due to their inherent higher risk of material misstatement.

The selected sample of five individual audit engagements is not representative of the Audit Firm's total population of the audit engagements completed by the Firm for the year under review.

Inspection Methodology

8. An entry meeting was held with DHS LLP on 23.11.2022 at NFRA office. The Firm presented an overview of the Governance and Management Structure, Firm-wide system of quality control, their audit approach and methodologies, including IT Systems. The on-site inspection was carried out between December 2022 and January 2023. The inspection methodology comprised meetings, walkthroughs, presentations, and interviews with certain members of the leadership team as well as the ETs of the selected audit engagements.
9. The areas of weaknesses or deficiencies on the part of the Audit Firm, included in the inspection reports, should be understood as areas of potential improvement and not a negative assessment of the work of the Audit Firm unless specifically indicated otherwise.

Audit Firm's Profile

10. M/s. DHS LLP is one of the fifteen (15) firms in the Indian Network M/s. Deloitte Haskins & Sells & Affiliates (DHS Network) registered with ICAI (The Institute of Chartered Accountants of India). As presented by the Firm in their entry meeting, this Firm is also a part of a global network of member firms of Deloitte Touche Tohmatsu Limited (DTTL), a UK private company limited by guarantee.
11. The Firm comprises 84 audit partners and had 249 audit clients falling under NFRA's jurisdiction during the FY 2020-21. The table below presents an overview of the Audit Firm's profile:

| Networks of which the Audit Firm is a part/member of: | |
|---|--|
| <i>(i) India:</i> | M/s. Deloitte Haskins & Sells & Affiliates |
| <i>(ii) Overseas:</i> | Deloitte Touche Tohmatsu Limited (DTTL) |
| Name of other members of the network (Entities in the Indian Network): | |
| <i>Name of Entity</i> | <i>Nature of Business</i> |
| DHS (6 firms) | Professional Services |
| A F Ferguson & Co LLP | Professional Services |
| A F Ferguson Associates | Professional Services |
| C C Chokshi & Co LLP | Professional Services |
| C C Chokshi & Co | Professional Services |
| S B Billimoria & Co LLP | Professional Services |

| | |
|--------------------------|-----------------------|
| P C Hansotia & Co LLP | Professional Services |
| Fraser & Ross Associates | Professional Services |
| Fraser & Ross | Professional Services |

Acknowledgement

12. NFRA acknowledges the cooperation of the Audit Firm during the inspection.

PART B

Review of Firm-Wide Audit Quality Control System

A. Independence Requirements

13. It was observed that the independence declarations of some ET members and others in respect of Issuer A, Issuer B, Issuer C and Issuer D who worked on audit engagements during FY 2020-21 were not available in the respective Engagement Management System (EMS), i.e., Audit Files.
14. The Audit Firm referred to its policy manual regarding complying with the independence policies and procedures and stated that all partners and employees submit an annual independence confirmation in an electronic tool, Global Independence Monitoring System (GIMS), in compliance with the requirements of Para 23 of SQC 1. Further, the Audit Firm stated that confirmations provided by partners/professionals encompass: (a) Annual confirmations and (b) Engagement level confirmations.
15. The Audit Firm also stated that a member of ET can access the EMS only after submitting the independence confirmation, and that the persons in the cited instances either did not work on the engagement, or the independence declarations were inadvertently not obtained/retained in the EMS. The Firm stated that the individuals mentioned in the Draft Inspection Report had given their annual independence confirmations and that engagement level independence confirmations is an additional control which is mandatory on first time access of an engagement file in the EMS.
16. Further, the Audit Firm stated that there is an automated control within the EMS system itself that requires an individual to assess and confirm his/her independence when he/she accesses the EMS for the first time by ticking/checking a box thereby confirming his/her independence prior to accessing any working papers in the EMS. Therefore, the Audit Firm stated that the integrity of an engagement is not lost under any circumstances.

17. The cited instances indicate that the EMS permitted access without obtaining the engagement level independence confirmations which is in violation of the Audit Firm's Policy Manual³ and Para 18 of SQC 1.

B. Engagement Continuance and Risk Assessment

18. It was observed that the Audit Firm accepted the audit engagement of Issuer E for the first time in the FY 2017-18, assessed the audit risk as Greater Than Normal (GTN) Risk and expressed an unmodified opinion. In the next FY i.e., 2018-19 also, the audit risk was set as GTN. During the limited review for the second quarter (FY 2018-19), the ET got to know of some suspicious transactions related to capital advances and the Inter Corporate Deposits (ICDs) provided by the company to other body corporates.
19. Para 31 of SA 315 states that where the auditor obtains audit evidence or information from performing further audit procedures, which is inconsistent with the audit evidence on which the auditor originally based the risk assessment, the auditor shall revise the assessment. Further, the Audit Firm's Policy Manual also requires the Engagement Partner (EP), in consultation with Audit Functional Leader, Audit Risk Leader, Member Firm's Professional Practice Director, and the Member Firm's Reputation and Risk Leader should assess changes in new risk factors not originally identified in engagement acceptance and changes in risk factors originally identified.
20. Therefore, the audit risk which was originally set at GTN for the FY 2018-19 was required to be reassessed and recategorized. However, the audit risk continued to be reflected as GTN.
21. The Audit Firm stated that they had discussion with the management of Issuer E on the status of the capital advances and the ICDs and the responses received from the management were not satisfactory, which aroused the suspicion of the ET. Accordingly, the ET performed additional procedures. This also led to reporting to the Central Government under Section 143(12) of the Companies Act, 2013 and the issuance of an adverse opinion on the financial statements of Issuer E for the FY 2018-19 and resignation as the Auditor.
22. However, the Audit Firm came to know of the suspicious transactions during the limited review for the second quarter of the FY 2018-19, and failed to reassess and recategorize audit risk which

³ Relevant details of the manual have been removed as per the express request of the Firm (DHS LLP) on the ground of their being proprietary.

is in violation of the Audit Firm's Policy Manual⁴ and Para 31 of SA 315.

C. Leadership of the network

23. It was observed that there is no Board to oversee the Network, its activities, and its officers as envisaged in Clause 10 and 11 of the Networking Agreement signed by DHS LLP and other member firms.
24. The Audit Firm stated that they have prepared the revised draft Networking Agreement, which is in the process of being finalized internally by the Network Firms. This will reflect the agreed networking administration and management structure. The Audit Firm confirmed that, as a part of the Deloitte Haskins & Sells & Affiliates Network, they will comply with the terms of the revised Networking Agreement.
25. DHS LLP is advised to comply with the terms of the Networking Agreement in force.

D. Engagement Quality Control Review Procedures

26. It was observed that in case of Issuer F, the evidence relating to performance of EQCR i.e., the EQCR docket (summary of EQCR work performed) was not made part of the EMS. However, EQCR clearance was obtained prior to the issuance of the audit report.
27. The Policy Manual⁵ of the Audit Firm states that the Lead Engagement Manager should ensure that the PDF file of EQCR docket generated through EQCR Portal is incorporated in the EMS as evidence of the performance of EQCR.
28. The Audit Firm stated that the inclusion of the EQCR docket as part of the EMS is only administrative in nature and does not in any way reflect on the nature, timing or extent of the work performed by the EQCR. The Firm further stated that they have made an enhancement to the Firm's Quality Control Policy Manual and with effect from 1st December 2021, as a preventive control, a mandatory check by the archival team is implemented for determining whether the EQCR docket generated from the EQCR Portal is made part of the EMS.
29. The Audit Firm is advised to ensure that the EQCR docket is incorporated in the EMS as per timelines specified in the Firm's Quality Control Policy Manual.

⁴ Relevant details of the manual have been removed as per the express request of the Firm (DHS LLP) on the ground of their being proprietary.

⁵ Relevant details of the manual have been removed as per the express request of the Firm (DHS LLP) on the ground of their being proprietary.

E. Consultation

30. In respect of audit engagement of Issuer E, a consultation related to the capital advances took place. The Consultation Memo in the EMS mentions only about the decision but does not capture the basis/rationale on which such decision was arrived. This does not meet the requirement of Para 56 of SQC 1 which inter alia requires that ‘....*the documentation is sufficiently complete and detailed to enable an understanding ofthe results of the consultation, including any decisions taken, the basis for those decisions and how they were implemented.*’ Further, the Audit Firm’s Policy Manual sets out who is responsible for the appropriate documentation of matters subject to consultation and related conclusions: "*The Partner (or his or her designee) who initiates consultation should be responsible for appropriate documentation of such consultation, including the relevant facts, issues raised, individuals consulted, conclusions reached, and supporting rationale for the conclusions.*"
31. The Audit Firm stated that they maintain an Audit and Accounting Consultation Portal on which ETs are required to raise consultation requests. The ET is required to populate in the portal, information such as engagement details, details of the ET and subject matter of consultation. In addition, a memo discussing the matter on which consultation is sought, the preliminary conclusion of the ET and the technical literature on which the ET has relied upon, duly approved by the EP and the EQCR, is required to be uploaded. The Consultation Memo considers the views of all the parties involved and the final view/ results that is to be implemented is documented in the Memo.
32. However, it is observed that the Consultation Memo in respect of Issuer E did not contain the basis/rationale based on which the decision was arrived at. The Audit Firm is advised to comply with its Policy Manual⁶ on Consultation and Para 56 of SQC 1.

PART C

Review of Individual Audit Engagement Files

A. Audit Evidence in respect of investments not documented

33. Issuer G invested in Government of India (GOI) securities during FY 2020- 21 pursuant to the Reserve Bank of India (RBI) guidelines related to liquidity risk management for certain Non-Banking Finance Companies (NBFCs). As on 31.03.2021, the closing balance of such securities was Rs. 3,069.32 million (Face Value Rs. 3000 million).

⁶ Relevant details of the manual have been removed as per the express request of the Firm (DHS LLP) on the ground of their being proprietary.

34. It was observed that the EMS did not contain the document with respect to the existence of the investment in the securities as on 31.03.2021. The Audit Firm obtained a copy of the year-end confirmation for investment from SBI DFHI Limited (Custodian) during the inspection and provided to the inspection team.
35. The Audit Firm stated that the ET verified the confirmation obtained by the Company from SBI DFHI Limited (Custodian) as on 11 December 2020 amounting to Rs. 1,500 million for the existence of the first tranche. The ET had not identified 'existence' as a relevant assertion for this account balance since the ET had concluded that the assertion of existence for investments was not relevant (i.e., the assertion does not have a reasonable possibility of containing a misstatement(s) that would cause the financial statements to be materially misstated); and, because no risks of material misstatement were identified related to the assertion, designing further audit procedures like obtaining a confirmation at the year end to address the assertion was not considered necessary.
36. Considering the nature of the investment and the fact that the investment constituted approximately 1% of the total assets as on 31.03.2021, the Audit Firm was required to verify and document the evidence related to the existence of total investment of Rs. 3,069.32 million as on 31.03.2021. This was not in conformity with the Audit Firm's Policy Manual and Para 7 of SA 230⁷.

B. Providing tax advisory and other legal advisory services to Issuer H

37. It was observed that the Audit Firm was the Statutory Auditor of Issuer H for the FY 2020-21 and also provided Non-Audit Services (NAS) viz. assistance in preparation, filing and representation before Dispute Redressal Panel (DRP).
38. Section 144 of the Companies Act, 2013 lists out the prohibited NAS. Para 14 and A14 of SA 200⁸ states that the auditor shall comply with relevant ethical requirements, including those pertaining to independence and adhere to ethical requirements as established by the Code of Ethics (2019). The Code of Ethics describes independence as comprising both independence of mind and independence in appearance. Further, the Code of Ethics vide Para 600.2 and 604.1 describes the self-review threat arising from different kinds of management services.
39. Regarding providing assistance to the management in the representation before DRP, the Audit

⁷ Standard on Auditing (SA) 230, Audit Documentation

⁸ Standard on Auditing (SA) 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing

Firm stated that it entailed preparation of draft objections/appeal in the prescribed form for issues pertaining to Assessment Year 2016-17 (FY 2015-16) and 2017-18 (FY 2016-17), based on the information provided by the management of Issuer H for review, finalisation and approval; and that the services pertained to earlier years when DHS LLP was not the Statutory Auditor of Issuer H.

40. DHS LLP was appointed as Statutory Auditor from FY 2017-18 on 9 August 2017 for a period of 5 years. The Audit Firm was the Statutory Auditor of Issuer H when such services were provided in FY 2020-21, though the issues related to previous years, when DHS LLP was not the Statutory Auditor. The Audit Firm stated that certain safeguards were implemented for the said engagements to mitigate any threats to independence viz., the ET which rendered the tax services was different from the audit ET and there was a separate Engagement Quality Control Reviewer who reviewed the audit work as laid down in para 604.10 A4 of the Code.
41. The Audit Firm further stated that they have, voluntarily, issued the NAS Guidelines effective from 1st April 2020, for not providing non-audit services to Public Interest Entities (PIE) as per the guidelines. The NAS Guidelines also provided for certain transitional provisions. The services referred to by NFRA were provided during FY 2020-21 as a part of transitional provisions of the NAS Guidelines. The Audit Firm has not provided any tax services to this client in subsequent FYs other than certain continuing services (as permissible under the transitional provisions of the Audit Firm's NAS Guidelines) relating only to these past assessment years.
42. NFRA appreciates the initiative of DHS LLP for coming out with NAS Guidelines and advises the Audit Firm to comply with the same. NFRA expects the Audit Firm to note that providing NAS to audit clients by the same Audit Firm creates self- review threat even with safeguards and runs contrary to the spirit of professional skepticism which the auditor is expected to display in audit.

PART D

Chronology of Events

| S. No. | Date | Event/Correspondence |
|--------|---|--|
| 1. | 11.11.2022 | Intimation of On-site Inspection from NFRA to the Audit Firm |
| 2. | 23.11.2022 | Pre-Inspection Meeting with DHS LLP held at NFRA office |
| 3. | 01.12.2022 to 23.12.2022 and 09.01.2023 to 13.01.2023 | On-Site Inspection |
| 4. | 12.04.2023 & 11.05.2023 | Communication of Inspection Team's Observations to Firm |
| 5. | 31.05.2023 | Response received from the Audit Firm |
| 6. | 04.10.2023 | Draft Inspection Report from NFRA to the Audit Firm |
| 7. | 05.10.2023 & 30.10.2023 | Extension sought by Firm for submission of reply to Draft Inspection Report |
| 8. | 06.11.2023 | Submission of reply by DHS LLP to Draft Inspection Report |
| 9. | 04.12.2023 | Communication of final Inspection Report to DHS LLP |
| 10. | 08.12.2023 | Comments on the final inspection report by DHS LLP |
| 11. | 22.12.2023 | Publication of Inspection Report on the website of NFRA as per Rule 8 of NFRA Rules 2018 |

APPENDIX-A: Audit Firm's Response to the Inspection Report

Pursuant to Section 132(2) of the Companies Act, 2013 and Rule 8 of NFRA Rules, 2018, the Authority is publishing its findings relating to non-compliances with SAs and sufficiency of the Audit Firm's quality control systems. As part of this process, the Audit Firm provided a written response to the draft Inspection Report, which is attached hereto. NFRA, based on the request of the Audit Firm has excluded the information from this report which was considered proprietary.

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December 8, 2023

The Secretary,
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Kasturba Gandhi Marg,
New Delhi -110 001

Subject: Response to Inspection Report 2022

Dear Madam,

We respectfully submit our response to the Inspection Report 2022 of Deloitte Haskins & Sells LLP ("the Report").

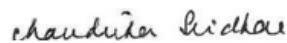
We believe that National Financial Reporting Authority's (NFRA) inspection process serves an important role in the achievement of our shared objectives of enhancing audit quality, and serving investors and public interest. We are committed to continuous enhancement in audit quality and will be unwavering in our efforts towards this objective.

Executing high-quality audits is our number one priority. In order to drive continuous enhancements in quality, we have been digitizing the audit, transforming the way we work, and fostering the development of our people, to fulfill our role to perform high-quality audits. Our quality is underpinned by a strong system of quality control. We are confident that our ongoing transformation, inclusive of the investments we are making in our audit processes, our people, and our technology, are resulting in significant, sustainable enhancements to our audit quality.

We have evaluated the matters identified in the Report and in Appendix A, have set out certain matters relating to the facts included in the Report for your consideration to incorporate any amendments in the final report.

Please contact me should you need any further information or clarification.

Yours sincerely,



Chandrika Sridhar
Partner

Matters relating to facts

Engagement Management System (EMS)

1. In paragraph 19, the Report states "...that the EMS permitted access without obtaining the engagement level independence confirmations ...". We would like to bring to your attention that although the right to access the EMS file is granted, an individual can neither access the working papers or perform any audit work or procedures in the EMS file prior to confirming their independence on the EMS system and as a result EMS system does not permit access to the work papers in the file without obtaining engagement level independence confirmations. Therefore, any member of an engagement team will not be able to perform any audit procedures and document the work performed in the EMS system without confirming their engagement level independence. This is an automated control for confirmation of independence.

We would also like to bring to your attention that the Engagement Declaration System (EDS) declaration is only for accessing project code in the time recording system to record time on an engagement and is not a substitute for independence confirmation in the EMS system.

Audit Methodology

2. We acknowledge that the risk assessment documentation was not revised to reflect the change in the assessed risks as stated in Paragraph 24. However, the audit procedures performed were similar to those required for a "much greater than normal" engagement as per the Firm's policies and consequently the Firm issued an adverse opinion for the year ended March 31, 2019.
3. In accordance with the Firm's methodology, SA 300 *Planning an Audit of Financial Statements*, SA 315 *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment* and SA 320 *Materiality in Planning and Performing an Audit*, classes of transactions, account balances or disclosures are identified based on the materiality, for e.g., benchmark determined as a percentage of profit before tax, determined for an engagement in accordance with our methodology. Fact based risk assessment is performed and is required to be documented on these classes of transactions, account balances or disclosures, to identify any risk of material misstatement and for design of appropriate audit procedures. (Refer Paragraph 38 in respect of Issuer G)



Independence

4. In Paragraph 39, we request you to include the fee received from Issuer H for assistance in preparation, filing and representation before Dispute Redressal Panel, of Rs. 2.63 lakhs and the total fee received for audit and related services of approximately Rs. 56 lakhs.

System of Quality Control

5. In Part A, point 2(e), we request you to add "one engagement" in order for the sentence to read as follows:

"In the case of one engagement, it was observed that during consultation process, the Audit Firm did not record the basis/rationale of the decision arrived at."

Others

6. In paragraph 12 - Instead of " ... this Firm is also a member of a global network of member firms ...", to state "... this Firm is also a part of a global network of member firms ..."
7. In paragraph 13, in the table, instead of "Networks of which the Audit Firm is a member", to state "Networks of which the Audit Firm is a part of"

