NFRA

National Financial Reporting Authority
Government of India

3 CIRCULARS, FRQR, AQRR & 13 ORDERS

Aug 2023

M P Vijay Kumar

INSURANCE !!

The views expressed are those of the presenter and, therefore, readers are requested to cross check with actual orders before making any application related decision.

E&OE.

- Purpose of deck is to highlight importance of quality financial reporting
- Any communication gap while converting content of NFRA orders to short sentence bullet points in the deck is unintentional and may please be excused.

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- Financial report quality review report (FRQR)
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Accounting is accountability : Accounting is base for tax, governance, capital, sustenance :

FS & Opinion on FS is a communication: should be ONLY truthful & complete

NFRA : INTRODUCTION

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NATIONAL FINANCIAL REPORTING AUTHORITY (‘NFRA’)

Scope : Monitor and enforce compliance with accounting and auditing standards and oversee the quality of service in such manner as may be prescribed under Sec 132 of Companies Act and NFRA Rules, 2018

Coverage : Following class of companies or their auditors:

i) All **Listed** Entities

ii) Unlisted Entities having

- Paid-up-capital of 500 Cr or more (or)
- Turnover of 1000 Cr or more (or)
- Outstanding debentures, loans and deposits of 500 Cr or more in preceding FY.

iii) Insurance & Banking Companies

iv) Companies engaged in the generation or supply of electricity

v) Companies governed by any special Act for the time being in force or bodies corporates.

Companies → FR Quality Review Report

Auditors/ Audit Firms → Audit Quality Review

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NFRA CIRCULARS

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CIRCULAR 1

October 2022 : Non-Accrual of interest on borrowings in violation of Ind AS

Facts :

1. Bank borrowing classified as NPA by the lender bank
2. Company is negotiating one time settlement (OTS)
3. Banks discontinued accrual of interest income from the date, it was classified as NPA
4. Considering the OTS, company discontinued the accrual/ recognition of interest expenses on borrowing cost

Analysis :

As per Ind AS 109, Financial liability to be classified and measured at amortized cost using EIM. In applying EIM, future cash flows to be estimated without considering future lower cash flow.

The banks discontinue, the recognition of interest on loans classified as NPAs as per prudential guidelines of RBI. However, these guidelines also require the banks to maintain a Memorandum Record of Accrued Interest on the NPAs clearly reflecting the fact that the bank has not legally released the borrowers from their contractual liability to pay interest. As per Ind AS 109 derecognition of any financial liability will be allowed only when borrower is released form primary responsibility for the liability either by process of law or by the creditors.

Circular :

The discontinuation of Interest accrual on borrowings is violation of Ind AS and Companies should continue to accrue expense & liability.

CIRCULAR 2

March 2023 : Non-Compliance with Ind AS on accounting policies for measurement of Revenue from Contract with customers and Trade Receivables

- Ind AS 115, requires that the entity shall recognize as revenue the amount of the transaction price, excluding the estimates of variable consideration that is allocated to that performance obligation.

  - It has been noticed that the significant accounting policies disclosed by many companies wrongly state that revenue is recognized and measured at fair value of the consideration received or receivable.

- Trade receivables are financial assets. All financial assets are required to be initially measured at fair value plus or minus the transaction costs. However, those financial assets classified as '"FVTPL"' are required to be measured at fair value. As an exception to these principles, trade receivables, shall be initially measured at their transaction price (Ind AS 115) unless those contain a significant financing component.

  - It is noticed that many companies in their accounting policy, either stated separately for trade receivables or stated as part of the accounting policy for financial assets which include trade receivables that the trade receivables are initially recognized (or measured) at fair value, which is contrary to the requirements of Ind AS 109.

CIRCULAR 3

June 2023 : **Responsibility of Statutory Auditors in reporting fraud**

- Auditors must report instances of fraud or suspected fraud to the Central Government and the Board/Audit Committee within specified timeframes and in the prescribed manner.

- Auditors to maintain professional skepticism throughout the audit process and communicate any identified fraud or suspected fraud to management, TCWG, and regulatory and enforcement authorities.

- Resigning from an audit engagement does not absolve an Auditor from reporting obligation. A recent judgment by the Hon'ble Supreme Court of India, held that auditors who resign without reporting fraud or suspected fraud can still be subject to the consequences.

3 There is a misconception amongst some Auditors that resigning from an audit engagement absolves them of their reporting obligations relating to fraud and the consequences under CA 2013 for nonreporting of fraud. In this regard, the Hon'ble Supreme Court of India in a recent judgment dated 03.05.2023 (Union of India and Another versus Deloitte Haskins and Sells LLP & Anr CRIMINAL APPEAL NOS.2305-2307 OF 2022), has held that the consequences of section 140 (5) of CA 2013 will be applicable also on those auditors who resign from the their audit engagements without reporting fraud/suspected fraud. The Hon'ble Apex Court observed:

> *"7.... Therefore, on true interpretation, even on resignation by an auditor of a company even during the enquiry/proceedings under section 140(5) or even prior to that, there shall not be any termination of the proceedings under section 140(5) as observed and held by the High Court. At the cost of repetition, it is observed that in a given case, an auditor, who in fact has, directly or indirectly, acted in a fraudulent manner, to avoid any further consequence under the second proviso to section 140(5), resigns to avoid any consequence under the second proviso to section 140(5), it cannot be permitted.*
>
> *14... Acting in a fraudulent manner, directly or indirectly, by an auditor is a very serious misconduct and therefore the necessary consequence of indulging into such fraudulent act shall follow."*

FINANCIAL REPORT QUALITY REVIEW

FRQR completed : Annual Reports for FY 2019-20

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NON-COMPLIANCE WITH IND AS

1. **Ind AS 109: Expected Credit Loss (ECL)**
   - Impairment loss on Non-Current and Current financial Assets (Loans & Others) is to be measured for ECL even if there has been no default in past periods.
   - No allowance for credit loss is contradictory for non-current trade receivable 'More than 12 months
   - No impairment loss allowance reported against the outstanding amounts of contract assets (unbilled revenue).
   - A subsidiary company was in distress and the acquisition was made for a nominal consideration. No impairment was made on the same. In the present case, though the amount involved is not material, this shows a weakness in the internal controls in so far as ECL evaluation is concerned.

2. **Ind AS 109: Corporate Guarantee -** The Company has not provided any clarification in the FS as to how the amounts of corporate guarantees have been disclosed and whether these are accounted as required by Ind AS 109. Para 4.2.2. of Ind AS 109 gives an option to the entity to measure a financial liability at fair value under certain conditions. Further, the company decision not to opt for the same, is incorrect as it is specifically states that a financial liability should be classified and measured in accordance with Ind AS 109.

3. **Ind AS 109 :** The company has not disclosed in its accounting policy for recognition and measurement of impairment loss on financial assets.

4. **Ind AS 19-** Non-disclosure in the notes to accounts to explain the nature of 'Employee Benefits - Pension', the absence of which results in inadequate information to users of the FS.

NON-COMPLIANCE WITH IND AS

5. **Ind AS 115 -** Non –disclosure of information related to refunds, returns and other similar obligations, types of warranties and related obligations regarding revenue generation activities
   - The accounting policies appear to have serious errors and are not in line with the prescriptions of the standard

6. **Ind AS 8 -** No details of regroupings to enable understanding of reclassifications. It is not clear whether these reclassifications and regroupings were due to correction of prior period errors.

5. **Ind AS 103 -** The company has accounted for the assets acquired and liabilities assumed at book value instead of fair value. The company did not provide the necessary disclosure and did not comply with para 18 and 45 of Ind AS 103 for the relevant year.

6. **Ind AS 12 -** The use of 'Liability Method' for accounting deferred tax assets and deferred tax liabilities is unclear, ambiguous and appears inconsistent with the Ind AS 12.

7. **Ind AS 36 -** It is not clear from the disclosures as to how the recoverable amount was measured i.e., higher of fair value less costs of disposal and value in use and lack of disclosure of information required by Ind AS 36.

Presentation of FS as per Schedule III

1. The company has treated the accumulated leave as short-term employee benefits, but reported an amount of Rs.2,144.03 lakhs under the head Long Term Provisions.

2. In AOC-1, one of the foreign subsidiaries shown as Subsidiary" for FY 2018-19 but the same is not shown in FY 2019-20 ; whereas, the date on which the subsidiary was acquired is mentioned as 27.08.2019 (FY 19-20).

3. Inadequate coverage of Risk Management Policy in Annual Report.

4. Not presented SOCIE, a component of FS.

5. Not disclosed aggregate of quoted/ unquoted Investment

6. Did not provide adequate details of the Company's going concern assessment and also whether the assessment was subjected to a review by the AC/BoD.

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AUDIT QUALITY REVIEW REPORT (AQRR)

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KEY OBSERVATIONS

1. **Compliance with Independence Requirements:**
   - During the tenure as Statutory Auditor, provided **non-audit services** directly and indirectly (through the other firms and entities in the same Network).

2. **Evaluation of Going concern Assumption:**
   - No management assessment of the entity's ability to continue as a going concern required by SA 570 (Revised). The Auditor was grossly negligent in compliance with SA 570 (Revised) in considering the evaluation of going concern assumption.

3. **Evaluation of ROMM Matters:**
   - After having identified the significant risk of Rollover of loans, the engagement team (ET) failed to design and implement any response to the identified risk, as required by SA 330.

4. **Communication with TCWG:**
   - Non-compliance with SA 260 by failing to document the communication made with TCWG except for the Engagement Letter and presentation made at the half year ended and year ended.

KEY OBSERVATIONS

5. **Engagement Quality Control Review (EQCR) Process:**
   - Complete travesty of the EQCR process by **appointing the Engagement Partner (EP) himself as its EQCR Partner**, thereby negating the very fundamental objectives of the SAs.
   - EQCR Partner has merely acted as an ordinary member of the ET and did not perform any independent and objective evaluation of significant judgments.
   - The work papers do not identify or document any discussion about significant matters between EQCR team and the EP.

6. **Basis of Qualified opinion** –
   - The impact of the transactions violative of accounting and auditing standards is such that the profit before tax of Rs. 351.71 crores, as reported in the financial statements, would have turned into a loss of at least Rs. 3,215.77 crores. This impact is **both material and pervasive**. As a result, the Firm was bound, under the SAs, to issue an adverse opinion instead of qualified opinion.

7. **Insolvency Petition on one of the Subsidiary** –
   - Did not obtain SAAE to understand the impact that the insolvency petition against one of the Subsidiary had on the Auditee. Further, the Auditor did not perform any audit procedures to understand as to why the auditee was made party to this insolvency petition.

KEY OBSERVATIONS

8. Emphasis of Matter (EOM) Paragraphs

- Provided **eight EOMs** in the financial statements of FY 2017-18. The Auditor compromised with the effectiveness of the auditor's report by widespread use of Emphasis of Matter (EOM) Paragraphs.
- Failed to obtain SAAE for providing these EOMs that was required as per SA 706.

9. Lapses in the Audit of Loans and Advances

- Failed in designing and performing **SAAE** to mitigate the risks, including risks of management override of internal controls, associated with the sanction of the loans, and disbursement of loans by the Company.

10. Lapses in the Audit of Investments

- Failed to properly verify the investments in almost 80% of the cases. The deficiencies are observed in the areas of use of valuation experts, fair valuation, and impairment loss evaluation.
- There are certain investments (₹1,637 Crore) for which **no evidence of verification** is available in the audit documentation.
- Completely neglected the possible negative impacts on the financial position of the Company and it solely relied on the Valuation Report of the Management Expert without performing any additional independent audit procedures that justify the valuation of the Company.

KEY OBSERVATIONS

11. Lapses in Preparation of Consolidated FS

- T**wo associates were excluded** while preparing CFS in violation of the Act. The Auditor failed to raise any questions to the management in this regard and also regarding the discrepancies in the total number of components.

12. Related Party Transactions

- Failed to notice non-compliance with the provision of Section 177 of the Companies Act, 2013, which requires **prior approval of the Audit Committee** for the RPT.

13. SQC 1 Compliance: Policies & Procedures –

- Firm did not have a policy document as required by SQC 1. The policies and procedures relating to independence, which are required to be an integral part of the QC Manual, are not present in the section titled “Independence”.
- Majority of the documents in SQC Policy submitted by the Audit Firm seem to be from the Global Network Entity and had not been developed with reference to Indian laws, rules and regulations. This can be seen from the policy related to communication with TCWG which is based on the IESBA Code of Ethics and PCAOB Rules and not according to the Standards of Auditing or Code of Ethics issued by ICAI.

NFRA ORDERS

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NFRA ORDERS : 2023 TO DATE

1.	Coffee Day Global Limited ("CDGL")	(Dated :12th April, and 28th July 2023)
2.	Mysore Amalgamated Coffee Estate Limited ("MACEL")	(Dated :13th and 24th April 2023)
3.	Tanglin Developments Limited ("TDL")	(Dated :26th April 2023)
4.	Giri Vidhyuth (India) Limited ("GVIL")	(Dated : 30th May 2023)
5.	Bartronics India Limited ("BIL")	(Dated : 3rd July 2023)
6.	Burnpur Cement Limited for ("BCL") (On EP and EQCR)	(Dated : 1st August 2023)
7.	MAN Industries (India) Limited ("MIIL)	(Dated : 28th June 2023)
8.	Prabhu Steel Industries Limited ("PSIL")	(Dated : 21st June 2022)
9.	Vikas WSP Limited ("VWL")	(Dated : 12th September 2022)
10.	ILFS Financial Services Limited ("IFIN")	(Dated : 22nd, 23rd and 28th July 2020)
11.	Anshu Clothing Limited ("ACL")	(Dated : 27th July 2023)
12.	Women Next Loungeries Limited ("WNLL")	(Dated : 28th April 2023)
13.	Dewan Housing Finance Corporation Limited ("DHFL")	(Dated : 31st March and 12th & 13th April 2023)

CAFÉ COFFEE DAY (CCD)

- Coffee Day Global Limited (“CDGL”),
- Mysore Amalgamated Coffee Estate Limited (“MACEL”),
- Tanglin Developments Limited (“TDL”) and
- Giri Vidhyuth (India) Limited (“GVIL”)

CCD : INVESTIGATION INITIATION

April 2022:

- SEBI investigation outcome on diversion of funds worth ₹ 3,535 crores from 7 subsidiary companies of CDEL to MACEL
    - ❖ TDL is a subsidiary of CDEL and GIVL is a subsidiary of TDL
- NFRA initiated investigations into the professional conduct of the statutory auditors under Section 132(4) of the Companies Act 2013

CCD : CHARGES ON AUDITORS

- Acceptance of audit engagement disregarding Independence requirements
- Tampering of Audit File and related lapses - SA 230, Audit Documentation
- Lapses in audit relating to Advance paid to related parties of ₹ 3,769.61 Crores as against ₹ 500 Crores of Audit committee approval to related parties
- Failure to detect evergreening of loans to the extent of ₹ 222.50 crores through related party transactions
- Failure to detect diversion of ₹ 130.55 crores to family members of promoters group through fellow subsidiary. (M/s Classic Coffee Curing Works ("CCCW"))
- Failure to detect abnormal capital advance to related parties in excess of approval obtained from Audit committee (capital advance paid was ₹ 87.02 crores against approval of ₹ 50 Crores but actual purchase is only ₹ 31.46 Crores)
- Failure in understanding the nature of business of MACEL resulting in lapses in audit of diversion of funds. Instances include Company obtaining a loan of ₹ 4,112.47 Crores from 7 companies and giving loans and advances of ₹ 3858.52 Crores to family members and entities owned or controlled by them.
- MACEL has recognized movement in short term borrowings of ₹ 850.90 crores and Loans and advances (Asset) of ₹ 59.09 as Cash Flow from Operating Activities instead of recognizing as Financing and Investing Activities respectively
- Lapses in evaluation and recognition of Contingent liabilities against corporate guarantee and loan taken by Family member of promoter by creation of charge on the assets of the company (₹ 130 crores).

NFRA OBSERVATIONS

- Auditors failed to exercise professional skepticism while performing audit of internal financial control.
- Failure to identify complete absence of IFC, which was evident from evergreening of loans through structure circulation of funds and round tripping of funds, that too all with related parties.
- Lapses tantamount to turning a blind eye to the ruse that lay before them.
- The Auditors should know that transactions with related parties have high risk of fraud. The Auditors could not give any reply as to how they used the Internal Audit Reports while performing audit of CDGL.

CCD : CHARGES ON AUDITORS OF TDL & GVIL (1 / 3)

- Lapses in audit of fraudulent loan transactions provided to MACEL of ₹ 2,614.35 crores without any business relationship between the companies out of borrowed funds from financial institution (ICFI Limited) and which is more than size of TDLs balance sheet.

- Fraudulent understatement of loans of ₹ 474 crores and failure to detect evergreening of loans to the extent of ₹ 350 crores through related party transactions

- Lapses in audit of fraudulent recognition of Interest income of ₹ 75.58 crores
  - Interest income of ₹75.58 crores is recognized in the books of TDL but interest expense is not recognized in the books of MACEL which resulted in overstatement of revenue and profit of the holding company CDEL.

- Lapses in audit of fraudulent diversion of funds of ₹ 507.05 crores to GVIL
  - TDL has paid an advance of ₹ 507.05 crores to GVIL without any Board resolution to borrow or grant loans and further GVIL has invested ₹ 56.91 crores and provided loan of ₹ 150 Crores in/to SICAL and involved in conduit transaction.

CCD : CHARGES ON AUDITORS OF TDL & GVIL (2 / 3)

- Lapses in audit of fraudulent loan transactions of ₹ 1,743.42 crores with Tanglin Retail Reality Developments Pvt Ltd ('TRRDPL') which is also a promoter-controlled entity-MACEL

- Lapses in audit of suspected fraudulent diversion of ₹ 415 crores given as land advances to related parties
  - TDL has paid land advance of ₹ 140 crores to SSPL (Related party) and ₹ 275 crores to relative (Mother of Promoter). Examination of the Audit File shows that the Auditors neither obtained any audit evidence nor performed any substantive audit procedure to evaluate the genuineness of these transactions.

- Failure to understand the nature of the business of GVIL
  - GVIL is a subsidiary of TDL, engaged in power generation, not commenced its operations since 2001 and there is no physical assets, revenue and expenditure except write off ₹ 45 crores of land advance but has advanced loan to MACEL of ₹ 475 crores out of gross amount of ₹ 581 crores of loans received from related parties
  - These details from financial statement showed that GVIL was used as conduit for financial mischief to divert funds from listed entities to entities controlled by promoters of listed entities

CCD : CHARGES ON AUDITORS OF TDL & GVIL (3 / 3)

- Fraudulent diversion of funds of ₹ 520 crores and failure to detect evergreening of loans to the extent of ₹ 350 crores
  - GVIL has received a loan from TDL and TRRDPL of ₹ 581.16 crores and given loan to MACEL and SICAL of ₹ 475 crores and paid a land advance of ₹ 45 crores which has been written off in the same year.
- Lapses in audit relating to Statement of Cash Flows
  - Cash advance and loans made to other parties has been disclosed as Cash flow from operating activities instead of cash flow from investing activities
- Lapses in evaluation of Going concern assumption
  - GAIL did not commence its operations moreover it has written off ₹ 45 crores of land advance and impaired ₹ 55.06 crores of investment

NFRA OBSERVATIONS

- Engagement team should have demonstrated professional scepticism to red flag the several irregularities.

- Considering the totality of the facts shows that GVIL was not going concern but just a means for achieving diversion of funds to the promoters group entities. Thus, auditors failed to evaluate the going concern assessment of GVIL.

- The two Audit firms are related firms with the same registered address.

NFRA ACTION

Company	Responsibility	Monetary Penalty	Debarred (Duration)
CDGL	Signing Partner	Rs. 10 Lakhs	5 Years
CDGL	Engagement Partner	Rs. 5 Lakhs	5 Years
CDGL	Engagement Partner	Rs. 5 Lakhs	5 Years
MACEL	Engagement Partner	Rs. 10 Lakhs	10 Years
TDL	Engagement Partner	Rs. 5 Lakhs	5 Years
GVIL	Engagement Partner	Rs. 5 Lakhs	5 Years
GVIL	Engagement Team	Rs. 5 Lakhs	5 Years

Company	Responsibility	Monetary Penalty	Debarred (Duration)
CDGL	Audit Firm	Rs. 1 Crore	2 Years
TDL	Audit Firm	Rs. 1 Crore	2 Years
GVIL	Audit Firm	Rs. 1 Crore	2 Years after expiry of TDL duration

Order in the matter of Bartronics India Limited

making businesses work

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BIL: INVESTIGATION INITIATION

- Information from the Ministry of Corporate Affairs regarding irregularities observed by **Financial Reporting Review Board (FRRB, hereafter) of ICAI** in the Financial Statements of FY 2013-14 and 2014-15

- BIL equity shares are listed on NSE and BSE

- NFRA initiated an investigation into the role of the statutory auditors,

BIL : CHARGES ON AUDITORS

1. **Misusing the "Emphasis of Matter" for covering up misstatements in the financial statements, instead of issuing Modified/Qualified report.** EoM included :
   - *Company has not provided interest on unsecured loans as terms are not clearly available with the Company*
   - *Company has not provided provision for doubtful advances of Rs. 90.63 Crores against capital advances*
   - *A Provision (PDD) of ₹ 70.31 Crores for trade Receivables of ₹ 812.64 Crores which are more than three years,*
   - *Non-repayment of FCCB of ₹313.02 crores which has fallen due as of February 2013* ***which may require going concern assessment****,*
   - *Uncertainties relating to MCD Project, matter in arbitration -* ***which may require going concern assessment***

EoM refers to a matter appropriately presented in the financial statements that, in the Auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements.

Whereas, in the existing case since the matter is not adequately disclosed in the financial statements, the matter cannot be included in the EoM para in the Auditor's report.

BIL : CHARGES ON AUDITORS

2. Other lapses in the audit :

i. **Erroneous Application of Financial Reporting Framework by the Company -** The Company has erroneously applied the provisions of Companies Act, 2013 while the Companies Act, 1956 was applicable for the reporting period

ii. **Non-compliance with the provision of AS 5 -** The Company has received a waiver from lenders of Principal, Interest and lease rentals which should have been disclosed as Income in financial statements, whereas the principal has been credited to capital reserve by the company .

iii. **Recognition of deferred tax asset without virtual certainty for sufficient future taxable income** - The company is in losses from FY 2012-13 to FY 2014-15 and has recognized deferred tax asset of ₹ 23.55 crores. EP should have exercised professional skepticism and challenged the management's judgement to provide convincing evidence for sufficient future taxable income.

iv. **Failure to report or address errors in Cash Flow Statement -** Non-cash income relating to waiver of Principal, interest and lease rental charges by the lenders should have been adjusted to arrive at 'Cash flow from Operating Activities'. Since the same has not been done, the Cash Flow from Operating Activities has been inflated.

v. **Significant Accounting Policies not as per applicable accounting standards -** *Employee Benefit Expense note* states that the provision for gratuity fund and leave encashment is made on adhoc basis. In contrast, in Significant Accounting Policies, it is stated that the estimated liability is determined in accordance with the requirements of AS 15 and charged to Profit and Loss account based on valuation by independent actuary.

NFRA ACTION

Considering the professional misconduct, nature of the violation and principle of proportionality, NFRA issued order in the matter of statutory audit of *M/s* Bartronics India Limited for FY 2013-15 on August 03,2023 as follows on the Engagement Partner:

i. Imposition of a monetary penalty of ₹ 5 lakhs

ii. Debarred for 10 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.

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Order in the matter of Burnpur Cement Limited

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BCL: INVESTIGATION INITIATION

- Information received from Registrar of Companies vide letter dated 24.11.2020 that the Statutory Auditor of BCL for FY 2017-18, had resigned within one month after issuing a Qualified Independent Auditor's Report

- NFRA initiated action under section 132 (4) of Companies Act 2013 against Audit firm’s Engagement Partner and the Engagement Quality Control Reviewer, for professional misconduct in statutory audit.

BCL : CHARGES ON ENGAGEMENT PARTNER

1. Improper assessment of the appropriateness of the use of Going Concern basis of accounting and misusing the "Emphasis of Matter ("EoM"):

Financial statements are prepared on going concern basis despite the following facts :

- Loss of ₹ 44.49 crores for 2017-18 and accumulated loss of 102.97 crores, which resulted in erosion of its net worth to ₹ (0.42) crores,
- Negative working capital of ₹ 238.85 crores and was highly debt ridden (Debt was 80.32% of its Assets) a
- Default in payment of debts of ₹ 233.09 crore

If in the Auditor's judgment, the management's use of the going concern basis is inappropriate, then the Auditor shall express an adverse opinion, but Auditors issued Qualified opinion and drew attention in EoM.

2. Inconsistency in audit documentation :

- The working paper recording the overall opinion and conclusions were reviewed and signed on 16th May 2018, while the Management Representation Letter (MRL), which was one of the supporting documents was signed on 28th May 2018.
- The MRL was obtained only to complete the documentary evidence and to fulfil the requirements of the SA 580.

BCL : CHARGES ON ENGAGEMENT QUALITY CONTROL PARTNER

1. Acceptance of appointment as EQCR without ensuring eligibility criteria

- EQCR has accepted the role without any prior experience in audit of listed entity

2. Failure to Perform the role of EQCR Objectively

- Only one working paper of EQCR was found, which was a yes / no type checklist. No other working papers are found showing any evaluation done by EQCR partner of the conclusions reached by the EP or any areas of disagreement with the EP.

- Failure to review the work of EP in a timely manner

- Failure to review work papers related to significant areas of audit such as, “The Independent Audit report” contained Qualified Opinion in respect of recognition of Deferred Tax Asset (DTA) and an Emphasis of Matter (EOM) in respect of the Going Concern, but audit file shows that the working papers were not reviewed by the EQCR partner.

NFRA ACTION

Considering the professional misconduct, nature of the violation and principle of proportionality, NFRA issued order in the matter of statutory audit of BCL on August 01, 2023 as follows:

i. Imposition of a monetary penalty of ₹ 1 lakh on the **Engagement Partner**

ii. Imposition of a monetary penalty of ₹ 1 lakh on the **EQCR Partner**

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Order in the matter of
MAN Industries (India) Limited

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MIL: INVESTIGATION INITIATION

- Information received from SEBI vide letter dated 23.06.2022.

- NFRA initiated action under section 132 (4) of Companies Act 2013 against Audit firm the Engagement Partner for professional misconduct in statutory audit.

MIL : CHARGES ON AUDITORS

1. **Conversion of loan to subsidiary into Capital Advance without Audit Committee approval and nondisclosure of the same**
   - Company has not disclosed loan to subsidiary in FY 2018-19 and FY 2019-20 and converted the loan outstanding loan into capital advance without prior approval of audit committee and haven't disclosed the purpose and utilization of loan.

2. **Failure to report non - disclosure of material transaction**
   - MIL pledged equity shares of its subsidiary MSPL amounting to ₹ 102.30 Crores for obtaining credit facility from Bank and it has not disclosed carrying amount of financial assets pledged as collateral which is required by Ind AS 107

3. **Improper disclosure of accounting policy related to Trade receivable and insufficient Provision for doubtful advances**
   - The company has disclosed in financial statements as *"Our historical experience & collecting receivables is supported by low level of past default and hence the credit risk is perceived to be low"* , where as company has written off debtors (51.14% of PBT) as bad debts during the year and provided only provision for ECL of ₹ 2.14 Crores considering 16.12% of debtors at risk, whereas during the investigation it found that 34.15% is at risk.

MIL : CHARGES ON AUDITORS

4. Error in presentation of ageing of trade receivable

5. Failure to report non- consolidation of subsidiary

- The Company has not consolidated it's wholly owned subsidiary MSPL but during investigation Auditors were not able to provide sufficient evidence to substantiate reason for not consolidating and issued Qualified audit report instead of issuing an adverse report.

6. Failure to obtain Sufficient Appropriate Audit Evidence (SAAE) with respect to Trade receivable, Investments, Inventories, Trade payables and Revenue

7. Audit documentation

- No dates are mentioned on signed documents such as Engagement letter, audit program and CARO

NFRA OBSERVATIONS

1. Failure to plan the audit

2. Failure to perform risk assessment procedures and response to such assessed risks
   - SA 315 : The auditors are required to perform risk assessment procedures to provide a basis for identification and assessment of the ROMM at the FS and assertion levels ; are also required to obtain an understanding of an entity and environment.

3. Failure to determine materiality

4. Failure to perform analytical procedures

5. Failure to prepare documentation regarding Auditor's responsibilities related to fraud

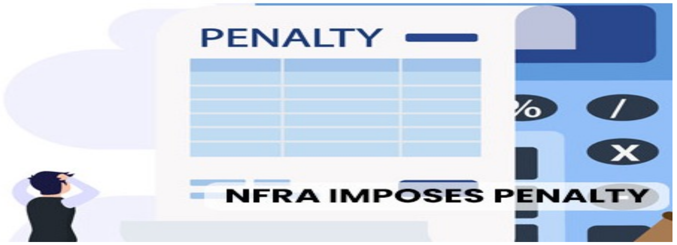
6. Failure to communicate with Those Charged With Governance (TCWG), regarding Audit plan, scope of work , timing of audit and deficiencies in Inter controls.

NFRA ACTION

Considering the professional misconduct, nature of the violation and principle of proportionality, NFRA **issued order in the matter of statutory audit of MIL on June 28th 2023 as follows:**

i. Imposition of a monetary penalty of ₹ 50 lakhs on the **Audit Firm**

ii. Imposition of a monetary penalty of ₹ 10 lakhs on the **Engagement Partner** and debarred him for a period of 5 years from being appointed as an auditor or internal auditor or from undertaking any audit in respect of financial statements or internal audit



M P Vijay Kumar

Order in the matter of
Prabhu Steel Industries Limited (“PSIL”)



PSIL: INVESTIGATION INITIATION

NFRA took up the Financial Reporting Quality Review (FRQR) of the Financial Statements of the Prabhu Steel Industries Limited(PSIL) for FY 2019-20.

NFRA OBSERVATIONS

1. **Non-Verification of ECL with respect to debtors, loans and advances which comprises more than 50% of total assets, thereby leading to inflated profits to the users of the financial statements.**
   - The total amount of trade receivables, loans and advances of the company are unsecured and bank balances are with non-scheduled & lesser known banks . The company failed to do a proper evaluation of impairment loss allowance for the financial assets.

2. **Non verification of SOCIE and information pertaining to changes in equity which form part of financial statements**
   - Despite the failure to present SOCIE, the Auditor in his audit report stated that "we have audited financial statements of PSL which comprises of Balance Sheet, Statement of Profit and Loss, Statement of Cash Flow and SOCIE"

3. **PSIL did not prepare consolidated financial statements despite having a material subsidiary viz., Haryana Metals Limited.**
   - The Auditor has failed to report this in audit report pertaining to PSIL.

NFRA OBSERVATIONS

4. **Auditor has falsely certified that FS comply with Ind AS specified u/s 133 of Companies Act and provide the true and fair value in conformity with the GAAP in India.**
    - Company did not make the disclosures under the IND AS 7, IND AS 107, IND AS 113.
    - Company failed to comply with statutory disclosure requirements specified in Division II of Schedule III with respect to Financial Assets

5. **No documentary evidence with respect to communication with TCWG or management leading to failure to comply the SA 260 & SA265**

5. **No documentary proof with respect to audit plan or audit strategy is available in audit file which leads to non-compliance of SA-300**

6. **No audit evidence of carrying out any risk assessment procedures as per SA 315 is found which leads to non-compliance of SA-315**

NFRA OBSERVATIONS

8. Other violations comprising Non-Compliance with :

- SA320- Materiality in planning and performing an audit
- SA330- Auditors responses to Assessed risks
- SA450- Evaluation of Mis-statements identified during the audit
- SA500-Audit evidence
- SA505- External confirmation
- SA520- Analytical Procedures
- SA530-Audit Sampling
- SA550- Related parties
- SA580-Written representations
- SA705-Modification to Opinion in Independent audit report.

NFRA ACTION

Action on **Engagement partner** :

- Monetary penalty of ₹ 1 lakh and
- debarred for one year from being appointed as an auditor or internal auditor or from undertaking any audit in respect of financial statements.

M P Vijay Kumar

<u>Order in the matter of</u>
VIKAS WSP Limited (“VWL”)

M P Vijay Kumar

VWL: INVESTIGATION INITIATION

- SEBI information in August 2021
- NFRA initiated investigations into the professional conduct of the statutory auditors

NFRA OBSERVATIONS

1. Failure to report lapses in accounting of interest cost pertaining to borrowings of NPA's

- Interest cost on borrowings classified as NPA by leading banks was not charged to Statement of Profit and loss since the leading banks have not recognized the interest on loans / export credit facilities.
- The company was offered One Time Settlement (OTS). IND AS 109, requires calculation of the amortised cost with reference to Effective Interest Method(EIM) by estimating the expected cash flows, without considering the possible future lower cash outflows but company had included this future possibility into its cash flows and auditor did not highlight
- This Interest Cost has potential impact of Rs.16.91 crores(which is 88% of reported PBT) resulting in understatement of expenses and overstatement of Profit.

2. Other lapses in conduct of the audit

- Absence of audit documentation for non-recognition of Interest Costs on the Borrowings classified as NPAs by the lending banks. Absence of documentation challenging the Management for such erroneous accounting treatment.
- Absence of audit evidence in the form of direct confirmations, loan agreements and correspondences with banks, etc
- Absence of determination of TCWG and the communications made with them
- Non-engagement of EQCR for VWL

NFRA ACTION

Action on **Engagement Partner**:

- Monetary penalty of ₹ 3 Lakhs

- Debarred for three years from being appointed as an auditor or internal auditor or from undertaking any audit in respect of financial statements.

M P Vijay Kumar

<u>Order in the matter of</u>
ILFS Financial Services Limited (“IFIN”)

M P Vijay Kumar

IFIN (IL&FS): INVESTIGATION INITIATION

- NFRA initiated investigation with a Show Cause Notice (SCN) on 17th January 2020 to Engagement Partner in terms of the powers vested in the u/s132(4) of the Companies Act, 2013, asking him to show cause as to why action should not be taken against him for professional misconduct in respect of his performance as Engagement Partner (EP) in the statutory audit of ILFS Financial Services Ltd (IFIN) for the year 2017-18

NFRA OBSERVATIONS

1. Loss of independence of the statutory auditor

- The Audit Firm was found to have, either directly or indirectly, provided prohibited services to the Auditee, or its holding company, thus violating the provisions as per section 144 of the Companies Act 2013 ; also, there was no prior approval of Audit committee for the non-audit services.

2. Misconduct in relation to the role of the Engagement Partner

- The list of work papers reviewed by EP, showed that almost all the important work of audit was not directed/supervised/reviewed by him.
- The EP denied the charges stating that audit were appropriately supervised and reviewed , both through his own review, and the review by another Partner to whom he delegated certain responsibilities and who ultimately reported to him ; the EP failed to provided sufficient evidence.

3. Misconduct in relation to communication with TCWG

- RBI had pointed out in various reports and letters that IFIN was in serious violation of Net Owned Funds (NOF) requirement and CRAR requirement.

Particulars	NOF	CRAR
As per RBI guidelines	₹ 2 Crore	15%
Actual as per financials	-₹ 4,123.76 Crores	-42.61%

- Regulatory non-compliances identified by RBI on the part of IFIN were very serious and material. None of the irregularities has been discussed with TCWG by EP.

NFRA OBSERVATIONS

4. Misconduct in relation to the evaluation of ROMM matters

- The Audit Firm had made references to certain other International Standards instead of compliance to Auditing Standards prescribed under section 143(9); hence there is a clear non-compliance as the Companies Act refers only to Standards of Audit issued by ICAI. Reference to International Standards is not appropriate.

5. Misconduct in relation to the RBI Inspection Matters

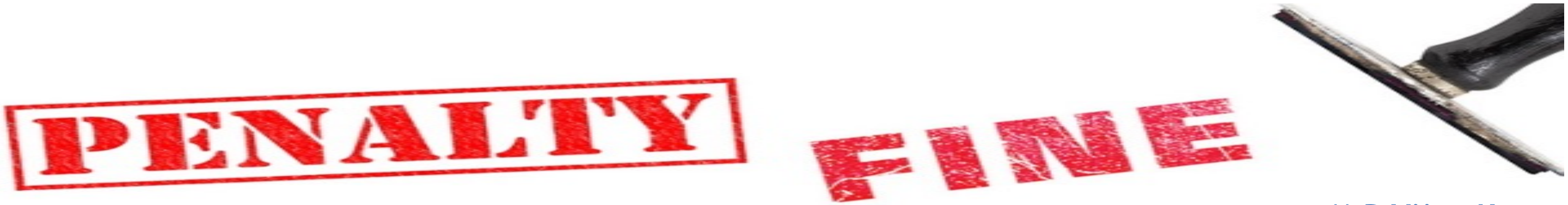
- The Company invoked pledge of shares of Tata Tele Services Limited (TTSL) upon certain loan defaults. The said shares were taken to the balance sheet at ₹ 253.55 crore.
- RBI, in its inspection reports had observed that the break-up value of the investment worked out as Nil, due to negative net worth. RBI suggested a provision of Rs.253.55 crore on March 31, 2015. However, in order to offset the impact of provisioning, the engagement partner went along with the management in including in the balance sheet a derivative asset (put option on TTSL Shares) of zero value, at ₹ 184.31 crore and taking credit for the same in the P&L A/c.

6. Misconduct in relation to evaluation of the Going Concern assumption

NFRA ACTION

- NFRA action as below on 23rd July 2020 and 28th July 2020 respectively.

Company	Role	Monetary Penalty	Debarred for
IL&FS	Engagement Partner	Rs. 25 Lakhs	7 Years
IL&FS	Engagement Quality Control Reviewer	Rs. 5 Lakhs	5 Years
IL&FS	Additional Engagement Partner	Rs. 15 Lakhs	5 Years



Order in the matter of
Anshu Clothing Ltd

Anshu's

M P Vijay Kumar

ANSHU: INVESTIGATION INITIATION

- Information received by MCA regarding the irregularities in the Financial statements by **Financial Reporting Review Board[FRRB of ICAI]**

- NFRA initiated the investigation u/s 132(4) of Companies Act,2013, against the Engagement Partner for professional misconduct in statutory audit.

NFRA OBSERVATIONS

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

- The company hasn't recognised the Interest accrued on Loan from banks and NBFCs amounting Rs.143.98 lakhs. Had the interest accrued been accounted, the reported loss is ₹162.26 lakhs [Reported loss:₹20.28 Lakhs].
- **Non provisioning of Trade Receivable -Unsecured, Considered Doubtful**
- The company has not made provision for the "Trade Receivable- Unsecured , Considered Doubtful of ₹ 709 lakhs

2. Wrong Accounting of the Deferred Tax Assets (DTA)

- The company has recognised the DTA of ₹9.07lakhs & ₹64.38 lakhs for the losses pertaining to period FY 2015-16 and FY2014-15 respectively. However, there was no evidence indicating the sufficiency of taxable income in future to realise such DTA.

3. Non- Disclosure of the Cost Formula for measurement of the Inventories

- The cost method for the calculation of the cost of inventory is not given in the FS which is violative of AS 2 which mandates disclosure of the accounting policy regarding the inventories including the cost formula.

4. Wrong Amortisation of expenses

- The company reported "Preliminary expenses" , "Listing expenses" as Non -Current assets which do not meet the criteria of the Non-Current assets as no future economic benefits are expected to flow to company.
- The audit file doesn't clearly indicate " Deferred Revenue Brand Development Expenditure" whether it satisfies the AS 26 conditions for recognition of the intangible assets arising from development.
- Recognition of MAT credit Entitlement presented as Unamortised expenses which in not in compliance with AS22.

NFRA OBSERVATIONS

5. Non - Compliance with the format of Financial Statements

- Multiple non- compliances with the format of FS were observed.
- Period from which the company had been continuously defaulting on loans and interest is not indicated.
- Only the names of the partnership firms invested are given in FS; other details like names of 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.
- As per Division I of Schedule III to the Act, securities deposit should be disclosed under long-term loans. However, the company has included under other current assets.
- Long term loans and advances is given as “advances recoverable in cash or in kind” which is very generic and does not give any information on the nature of other loans and advances.

6. Non - Compliance with Standards on Auditing:

- SA230 : documentation
- Terms of Audit Engagements
- Non- Compliance regarding the appointment of Engagement Quality Control Reviewer(EQCR)

NFRA ACTION

Action on **Engagement partner** :

- Monetary penalty of ₹ 1 Lakh
- Debarred for three years from being appointed as an auditor or internal auditor or from undertaking any audit in respect of financial statements.

<u>Order in the matter of</u>
Women Next Loungeries Ltd (WNLL)

M P Vijay Kumar

WNLL: INVESTIGATION INITIATION

- Letter received from Office of Registrar of Companies (ROC- MUMBAI)forwarding the findings of investigation carried out by Office of Regional Director-Mumbai

- NFRA initiated the investigation u/s 132(4) of companies act,2013 , against Engagement Partners of respective years for professional misconduct in statutory audit [FY 2016-17 & FY 17-18 respectively].

NFRA OBSERVATIONS

1. Failure to obtain Audit Evidence regarding the existence and condition of the inventory

- Failure to obtain SAAE regarding the existence of inventory. The inventory worth ₹20.60 Crores & ₹24.11 Crores constituted 54% and 36% of Balance Sheet Size for FY 2016-17 and FY 2017-18 respectively.

2. Failure to identify the related party and related party transactions

- Failure to identify M/s. Shiv Apparels as related party and transaction entered into with them as Related Party Transactions. It is noted that 100% & 54% of Net sales was to M/s. Shiv Apparels for FY 2016-17 and FY 2017-18 respectively .

3. Failure to obtain External Confirmation for the Trade Receivables & Trade Payables

- The Trade receivable & Trade Payables accounts to 39.81% and 36.75% of the balance sheet size for FY 2016-17 & 60.48% and 29.24% for FY 2017-18. The Auditor is charged with Gross Negligence for not obtaining direct confirmation of balances from debtors and creditors and failure to perform the alternative procedures in absence of the confirmations. [SA505]

NFRA OBSERVATIONS

4. Failure to report non - provisioning for Doubtful debtors

- Company identified ₹ 9.17Cr of Doubtful debts during the FY207-18 and failed to make any provision for the same. Had the provision been made by WNLL ,the profit of Rs.2.56 Crores would turn to loss of ₹6.61 Crores

5. Other lapses in the Audit:

- Failure to plan the audit and failure to understand the entity and its environment
- Failure to identify the TCWG and communicate with TCWG.
- Failure to report the Non-Compliance with Laws & regulations.
- Failure to determine the materiality and perform materiality
- Failure to Document the sampling methodology adopted for substantive testing
- Failure to appoint Engagement Quality Control Reviewer(EQCR)

NFRA ACTION

Action on **Engagement partners** :

- Monetary penalty of ₹ 2 Lakhs each
- Debarred for 2 years from being appointed as an auditor or internal auditor or from undertaking any audit in respect of financial statements.

Order in the matter of
Dewan Housing Finance Corporation Ltd

M P Vijay Kumar

DHFL : INVESTIGATION INITIATION

- ₹ 31,000 Crores of DHFL scam reported in media

- NFRA issued Show Cause Notice issued to 6 branch auditors for the statutory audit of branches of DHFL, for the FY 2017-18.

NFRA OBSERVATIONS

1. **Acceptance of audit engagement without valid authorization and without complying with ethical requirements; and issuing an audit report in violation of the Act**
   - The EP was charged with acceptance of an audit engagement without complying with ethical requirements and issuing the audit report without a valid appointment as "Statutory Auditor for the branches" of DHFL by the competent authority i.e., the shareholders

2. **Non-Compliance with**
   - SA 210 : Agreeing the Terms of Audit Engagement
   - SA 230 : Non-Compliance with "Audit Documentation

NFRA OBSERVATIONS

4. **Non-Compliance with SA 700: "Forming an Opinion and Reporting on Financial Statements [SA 700]**
   - The Auditor shall conclude as to whether obtained reasonable assurance whether the FS as a whole are free from material misstatement, due to fraud or error. In the Annexures to the audit report, EP noted that for some of the loan files reviewed required documents were not obtained. Also, there is no documentation of whether any unadjusted misstatements were material or not. The EP did not document anywhere how these possible misstatements were evaluated in forming the unmodified opinion

5. **EP failed in establishing an overall audit strategy and development of audit plan**

6. **Audit file lacks any documentation regarding the performance of risk assessment procedures for material misstatements at the FS level and assertion level and response to such risks, etc.**

7. **Absence of the evaluation of identified misstatements and uncorrected misstatements**

DISCIPLINARY ACTION AND PENALTY LEVIED ON BRANCH AUDITORS OFDHFL

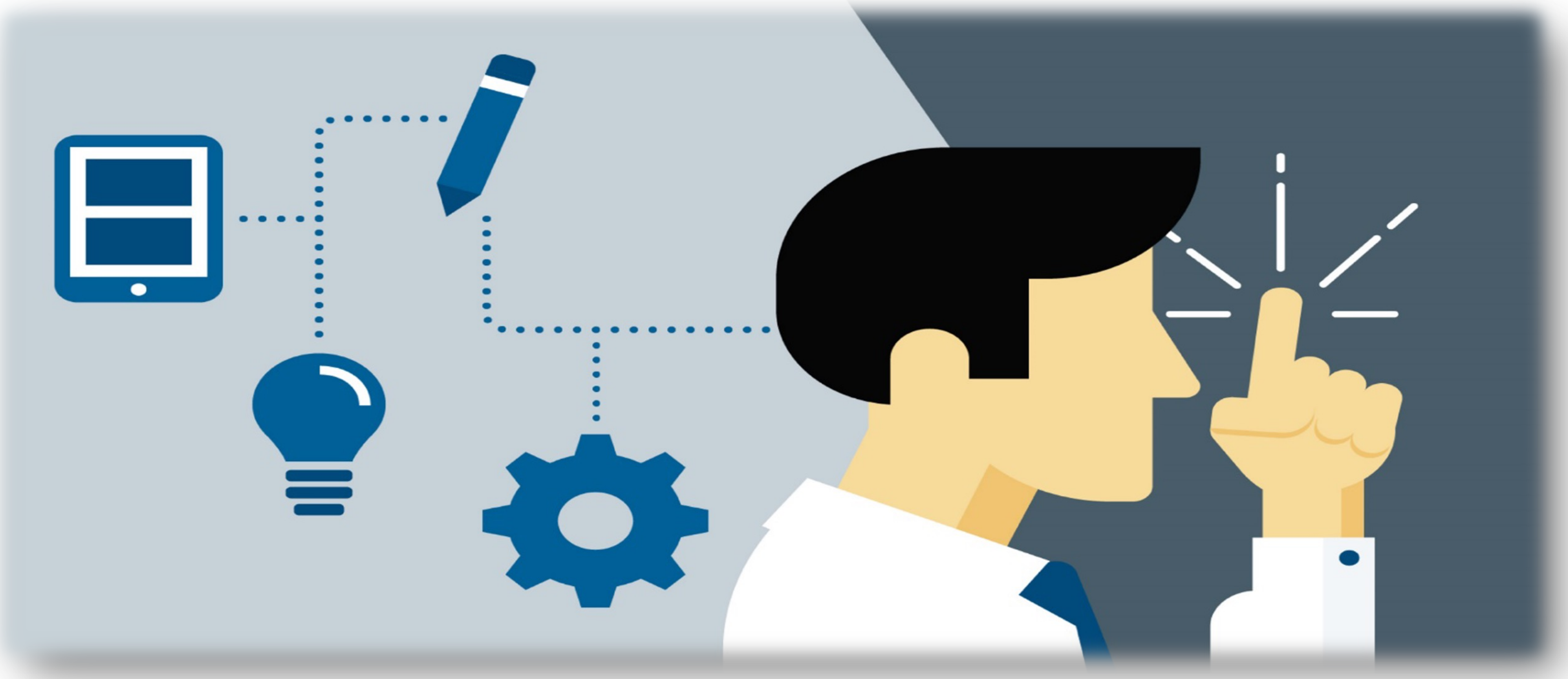
Action on **6 Branch Auditors** :

- Monetary penalty of ₹ 1 Lakh each

- Debarred for 1 year each from being appointed as an auditor or internal auditor or from undertaking any audit in respect of financial statements.

M P Vijay Kumar

LEARNING



M P Vijay Kumar

LEARNING

- NFRA is becoming more engaging and effective
- NFRA orders are explanatory
- As Ind AS and SAs/Code of Ethics are based on International standards, NFRA is conducting adequate research on how these were applied : key for Preparers (CFOs) and Auditors to track international literature/ developments/ discussion papers on how standards are being applied.
- **When in doubt, consult**
- Audit documentation is key : SA 315 is at heart of audit.

- **Recommendation :**
  - One time presentation of NFRA circulars, orders to date to AC (TCWG) and CXO
  - **Test all audits and FS of FY 22-23 wrt to NFRA observations in the FRQR, AQRR and Orders ; take steps to ensure where necessary for compliance henceforth**
  - Each year test FS for compliance with ICAI FRRB and QRB observations in addition to EAC opinions applicable.
  - Present to AC (TCWG) and CXO : update on NFRA orders during the quarter

M P Vijay Kumar

THANK YOU!

M P Vijay Kumar

STAY SAFE. STAY HEALTHY. STAY ACCOUNTABLE