भारत सरकार / **Government of India**

राष्ट्रीय वित्तीय रिपोर्टिंग प्राधिकरण /**National Financial Reporting Authority**

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7th Floor, Hindustan Times House,
Kasturba Gandhi Marg, New Delhi

No. 012/2024 Date: 26.04.2024

ORDER

Order under Section 132(4) of the Companies Act 2013 in respect of M/s Dhiraj & Dheeraj (Firm Registration. No. 102454W), CA Piyush Patni (ICAI Membership No. 143869) and CA Pawan Kumar Gupta (Membership No. 051713)

This Order disposes of the Show Cause Notice ('SCN') dated 25.07.2023, issued to M/s Dhiraj & Dheeraj the 'Audit Firm', CA Piyush Patni, who was the Engagement Partner (the 'EP') and CA Pawan Kumar Gupta, who was the Engagement Quality Control Review Partner (the 'EQCR Partner') for the statutory audit of Reliance Home Finance Limited, for the Financial Year (FY) 2018-19 (the Audit Firm, the EP and the EQCR Partner are collectively referred to as 'the Auditor' hereafter). This Order is divided into the following sections:

A. Executive Summary

B. Introduction and Background

C. Major Lapses and Violations

D. Findings on the Articles of Charges of Professional Misconduct

E. Penalties and Sanctions

A. EXECUTIVE SUMMARY

1) Reliance Home Finance Limited (RHFL) is a Non-Banking Finance Company (NBFC) listed on both the Bombay Stock Exchange and the National Stock Exchange. M/s Price Waterhouse & Co Chartered Accountants LLP (PW) was initially appointed as the auditor of RHFL for FY 2018-19. The Director General of Corporate Affairs (DGCoA), Ministry of Corporate Affairs (MCA), Government of India, vide its letter dated 29.05.2020 informed the National Financial Reporting Authority (NFRA) that PW had filed a report to MCA under section 143(12)[1] of the Companies Act, 2013 (the Act) on 03.06.2019. PW then resigned from the audit on 11.06.2029, without issuing an audit report for FY 2018-19. M/s Dhiraj & Dheeraj were appointed by the board of directors of RHFL on 29.06.2019 as statutory auditors of RHFL to fill the casual vacancy caused by the resignation of PW. Further, the Securities and Exchange Board of India (SEBI) vide its letter dated 21.03.2022 informed NFRA that M/s Dhiraj & Dheeraj had issued a qualified opinion for FY 2018-19

[1] Under section 143(12) of Companies Act, 2013 auditor is required to report any fraud identified in the company.

without making adequate disclosures in the audit report, including the impact of 'General-Purpose Corporate Loans' (GPCL) on financial statements.

2) On examination of the Audit file for the Statutory Audit of RHFL conducted by the Audit Firm Dhiraj& Dheeraj, which was called for under Section 132 (4) of the Act, we were of the prima facie view that the Auditor had not discharged their professional duties under the Act as well as the Standards on Auditing (SA). Consequently, the SCN was issued to the Auditor asking them to show reason why action under Section 132(4) of the Act should not be initiated against them for professional misconduct.
3) As per the financial statements, RHFL's total assets were ₹18,100 crore and total external liabilities were around ₹16,300 crore as of 31.03.2019. The external liabilities included a debt of over ₹14,800 crore, consisting of debentures, borrowings from banks, commercial papers etc. It had a total revenue of around ₹2000 crore and reported a net profit of ₹67 crore for FY 2018-19. PW reported suspected fraud regarding loans amounting to approximately ₹7900 crore as on 31.03.2019.
4) Despite the resignation of the previous auditor and a reporting of suspected fraud, the Auditor failed to conduct the audit as per standards on auditing. The material misstatements in the financial statements due to inadequate provision, unjustified valuation of loans and irrational business practices were concurred by the Auditor in disregard of their responsibilities under the Act and SAs. The deficiencies in the audit resulted in rendering the opinion unreliable since the material misstatements in the financial statement assertions remain unreported. The Auditor also demonstrated a lack of professionalism by rationalising the actions of the Company, inappropriately evaluating the work of the previous auditor, and ignoring the fundamentals of auditing.
5) After examining his detailed submissions, including written and oral, this Order concludes that the Auditor failed to meet the relevant requirements of the SAs and violated the Act, and the Code of Ethics in respect of several significant areas of audit. In the areas of the audit identified in this Order, the Auditor was grossly negligent, failed to apply professional skepticism and due diligence, and did not adequately challenge the management assertions. Major violations proved in this Order are as follows:
   a) The Auditor did not exercise professional skepticism and perform risk assessment procedures to identify, assess and respond to the Risk of Material Misstatement (ROMM) due to fraud or error in respect of (a) RHFL's loan disbursal (General Purpose Corporate Loans) to financially weak companies without appropriate business rationale, (b) Funds so disbursed being diverted/siphoned off to other group entities.
   b) The Auditor did not perform sufficient appropriate audit procedures in respect of verification of the company's assessment of (a) the going concern assumption, and (b) adequacy of the Expected Credit Loss (ECL) of ₹278 crore on loans at amortised costs of ₹16,259 crore, which included ₹7849 crore of General Purpose Corporate Loans to credit impaired entities on which ECL was only ₹173 crore.
   c) The Audit Firm accepted the audit engagement without complying with the relevant requirements of the Chartered Accountants Act, 1949. Apart from the above, the Auditor did not ensure an objective engagement quality review by the EQCR Partner, failed to adhere to quality standards, failed to evaluate the going concern basis of

accounting, and failed to comply with the requirements of SA while reporting on the work of management's experts.

d) The omissions and commissions of the Auditor had rendered the audit report unreliable. The Audit Firm issued a qualified report while it was required to issue a disclaimer or adverse opinion, had the audit been conducted as per SAs.

6) Based on the investigation and proceedings u/s 134(4) of the Companies Act, and after allowing them to present their case, we find the Audit Firm, the EP and the EQCR Partner guilty of professional misconduct and impose, through this Order, the following monetary penalties and sanctions:
   a) Imposition of a monetary penalty of Rupees One crore on the Audit Firm M/s Dhiraj & Dheeraj.
   b) Imposition of monetary penalties of ₹50,00,000/- (Rupees Fifty Lakh) and ₹10,00,000/- (Rupees Ten Lakh) respectively on CA Piyush Patni (EP) and CA Pawan Kumar Gupta (EQCR).
   c) In addition, EP and EQCR partners are debarred for five years and three years respectively 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.

B. INTRODUCTION AND BACKGROUND

7) NFRA is a statutory authority set up under Section 132 of the Act to monitor the implementation of the auditing and accounting standards and oversee the quality of service of the profession associated with ensuring compliance with such standards. The Statutory Auditor, appointed by the members of the company under section 139 of the Act is bound by the duties and responsibilities prescribed in the Act, the rules made thereunder, the Standards on Auditing (SA) and the Code of Ethics, the violation of which constitutes professional misconduct. NFRA has the powers of a civil court and is empowered under Section 132(4) of the Act to investigate the prescribed classes of companies and impose penalties for professional or other misconduct of the individual members or firms of chartered accountants.

8) RHFL was required to prepare its Financial Statements for FY 2018-19 under Schedule III and other applicable provisions of the Act and Indian Accounting Standards (Ind AS) notified under the Companies (Accounting Standards) Rules, 2006.

9) We observe that RHFL, despite being a housing finance company regulated by the National Housing Bank (NHB), had advanced loans under the category 'General-Purpose Corporate Loan' (GPCL) to group companies with significant deviations from their lending policy. The outstanding amount of GPCL as of March 31, 2019, amounted to ₹7,849.89 crore as per the financial statements. These loans were stated as secured by a charge on the current assets of borrowers. The majority of the Company's borrowers had undertaken onward lending transactions and the borrowings from the Company were used, *inter alia*, for repayment of financial obligations by some of the group companies. The previous auditor PW reported issues with the recoverability, end use and business rationale of these loans.

As per the report filed by PW under section 143(12) of the Act, they did not receive a satisfactory response from RHFL regarding queries raised on these matters.

10) Following the information from DGCoA and SEBI, as described in the executive summary of this Order, we suo motu decided to examine the audit evidence that led the Audit Firm to issue a qualified audit opinion. We called for the Audit File[2] and other information from the Audit Firm on 22.03.2022. After two extensions, the Audit Firm submitted the Audit File and other documents electronically through File Transfer Protocol (FTP) on 27.05.2022. From the Audit File, it was observed that M/s Dhiraj & Dheeraj were appointed as statutory auditors by the Board of Directors of RHFL on 28.062019 to fill the vacancy caused by the resignation of PW. The examination of the Audit File, annual reports of the Company and other communications by the Audit Firm to NFRA showed a prima facie case of professional misconduct on the part of the Auditor.

11) On satisfaction that a sufficient cause exists to initiate action under Section 132(4) of the Act, an SCN was issued to the Auditor to show cause as to why necessary action for professional misconduct against them should not be taken under Section 132(4)(c) of the Act read with Rule 11 of NFRA Rules 2018 for professional misconduct of:

a) Failure to disclose a material fact known to him which is not disclosed in a financial statement, but disclosure of which is necessary in making such financial statement where the statutory auditors are 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 expressions of an opinion; and

e) Failure to invite attention to any material departure from the generally accepted procedures to audit applicable to the circumstances, and

f) Failure to accept a position as auditor previously held by another chartered accountant after first communicating with him in writing.

12) The Auditor sought two extensions for submitting their response to the SCN which was granted. The Firm, the EP and the EQCR Partner, on 18.09.2023, submitted their replies to the SCN. The SCN also provided an opportunity for a personal hearing to the EP, EQCR Partner and the Audit Firm which was availed by them on 30.01.2024. The Auditor also made written submissions on 08.02.2024 in addition to the reply to the SCN and the oral submissions. All the written and oral submissions have been examined in detail before issuing this Order.

[2] Vide NFRA letter dated 24.11.2021.c

C. MAJOR LAPSES AND VIOLATIONS

13) The major basis for charges in the SCN included client acceptance without complying with requirements of the law, failure to examine the merits of the significant matters reported by the previous auditor, use of management's experts in violation of SA 500[3], failure in the evaluation of the Going Concern and Expected Credit Loss (ECL) on loans, and absence of objective review by the EQCR Partner.

14) Replies of the Auditor to the charges in the SCN are examined and discussed under the following broad categories. Only the violations/actions/omissions proved to result in one or more professional misconduct as per the articles of charges in the SCN are covered in this Order.

C.1. Acceptance of the Audit Engagement

C.2. Significant Matters Reported by the Previous Auditor

C.3. Evaluation of the Going Concern Assumption

C.4. Verification of Expected Credit Loss (ECL) on Financial Assets.

C.5. Modification of the Audit Opinion on the Financial Statements.

C.6. Use of the work of Management's Experts and Auditor's Expert

C.7. Engagement Quality Control Review (EQCR)

C.8. Compliance with SA 230[4]

C.1. Acceptance of Audit Engagement

15) Clause 8 of Part-1 of the First Schedule to the Chartered Accountants Act, 1949 requires that an incoming auditor shall accept a position as auditor previously held by another chartered accountant after first communicating in writing with the previous auditor. However, the Audit Firm accepted the audit engagement on 01.07.2019, before its communication with PW (initiated on 02.07.2019) and without waiting for a reasonable time for PW to respond to the communication. PW issued its no-objection letter on 05.07.2019. By that time the Audit Firm had started the engagement activities. Thus, the EP and the Audit Firm were charged with non-compliance with Clause 8 of Part-1 of the First Schedule to the Chartered Accountants Act, paragraph 12(b) read with paragraph A21 of SA 300[5], paragraphs 28 & 30 of SQC 1[6] and the Audit Firm's quality policy.

16) In their response, the Auditor denied the charges and stated that two additional letters were issued to the company, other than the engagement acceptance letter. The first letter clarified

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[3] SA 500, Audit Evidence

[4] SA 230, Audit Documentation

[5] SA 300, Planning an Audit of Financial Statements

[6] SQC 1, "Quality Control for Firms that Perform Audit and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements"

that the acceptance of the engagement was subject to getting a No-Objection Certificate (NOC) from PW. Subsequently, a second letter was also issued intimating RHFL about the receipt of NOC from PW. The Auditor also submitted that no audit work had been started before the receipt of NOC.

17) We examine the detailed submissions and observe the following.

a) The additional letters submitted along with the reply to SCN, did not form part of the Audit File submitted to us on the affidavit[7]. These letters do not contain any acknowledgement from the recipients or proof of delivery. Compounded with this is the fact that the engagement acceptance letter and the two additional letters, submitted in the course of these proceedings, were addressed to different offices, viz, the Board of Directors, Executive Director & CEO, and Chief Financial Officer (CFO) respectively. Thus, these letters lack reliability and evidentiary value. More importantly, being qualified chartered accountants bound by the Code of Ethics and SAs, the Auditor knows very well that the engagement cannot be accepted without first communicating with the previous auditor.

b) The following chronology of events makes it clear that the Audit Firm accepted the engagement before communication with the previous auditor and commenced the audit without waiting for a reasonable time for a reply from the previous auditor.

Date of Communication	Event/Correspondence
11.06.2019	PW resigned as statutory auditor of RHFL.
28.06.2019	RHFL Board resolution[8] for appointing M/s Dhiraj & Dheeraj.
29.06.2019	Letter of appointment given by the Board.
01.07.2019	Engagement Acceptance letter given by Dhiraj & Dheeraj to RHFL.
02.07.2019	Dhiraj & Dheeraj sent request for NOC to PW.
03.07.2019	Audit planning meeting between the Engagement Team (ET) and RHFL.
05.07.2019	PW sent NOC to Dhiraj & Dheeraj.

c) Further, the work papers (WP) in the Audit File[9] on audit planning evidence the start of the work before receipt of NOC from PW. For instance, WP on the audit planning meeting and WP on the understanding of the entity are dated 03.07.2019. Other planning work papers are not signed, and hence no evidence to confirm that the work was done after receiving NOC.

[7] Refer to paragraph on non-compliance with Paragraph 14 of SA 230 & SQC 1 which prescribes a maximum period of 60 days for completion of assembly of Audit File in Chapter on Audit Documentation

[8] As mentioned in the NOC letter of the Audit Firm.

[9] WPs 'J.4. K.3. Minutes of Planning Meeting with Team', "K.4. Minutes of Planning Meeting with Client Staff"

d) Clause 8 of Part-1 of the First Schedule to the Chartered Accountants Act, 1949 states that a Chartered Accountant (CA) in practice shall be deemed to be guilty of professional misconduct if he accepts a position as auditor previously held by another chartered accountant without first communicating with him in writing. Paragraph 12 of SA 300 also mandates this requirement. The above communications and WPs evidence that the audit was accepted before sending a request for NOC and the audit commenced before the completion of communication, violating the Chartered Accountants Act, 1949 and SA 300. The previous auditor resigned after reporting fraud under Section 143(12) of the Act. Despite knowing this fact, the EP and the EQCR Partner did not exercise the required professional skepticism, as required by SA 200[10], in communicating with the predecessor auditor.

e) Paragraphs 28 and 30 of SQC 1[11] require that before accepting an audit engagement, the auditor should consider the integrity of the client by collecting information from existing and previous providers of professional accountancy services to the client and from other sources. The Audit File[12] did not contain evidence of examination of the integrity of the client, particularly, any information obtained, or attempted to be obtained, from the previous auditor. The above actions of the Audit Firm violate its quality policy, contained in the Quality Control Manual prepared as per the requirements of Paragraph 3 of SQC 1. This shows the absence of operating effectiveness of firm-level controls on acceptance of the engagement.

18) Based on the above, the charges in paragraph 15 stand proved. The Audit Firm and the EP are guilty of professional misconduct in terms of Clause 8 of Part-1 of the First Schedule to the Chartered Accountants Act, 1949, paragraph 12(b) read with paragraph A21 of SA 300, paragraph 28 & 30 of SQC 1 and the Audit Firm's policy for accepting the Audit Engagement.

19) It is the admitted position[13] that the EQCR Partner participated in the planning meeting and the meeting where engagement acceptance was discussed and concluded. As explained above, both meetings were conducted before the receipt of NOC. Yet, the above violations remained unnoticed by the EQCR Partner. This shows the absence of due diligence and objective review required by SA 220.

20) We note that in a disciplinary case[14] of ICAI, where a chartered accountant commenced the work of audit on the very day he sent a letter to the previous auditor the Disciplinary Council of ICAI had held that he was guilty of professional misconduct. The appointment could be accepted only when the outgoing auditor does not respond within a reasonable

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[10] SA 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing

[11] 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

[12] WP "K.9. Client-Engagement Acceptance & continuance checklist"

[13] Paragraph B.7.5 of the Reply to the SCN by the Audit Firm.

[14] As per the decision cited in the Code of Ethics 2009, issued by ICAI (S.N. Johri vs. N.K. Jain - Page 1042 of Vol.IV of the Disciplinary Cases - decided on 13th, 14th & 15th September 1973)

time. In another case[15], the Council found a chartered accountant guilty of professional misconduct because he commenced the audit without waiting for a reasonable time for a reply from the previous auditor.

C.2. Significant Matters Reported by the Previous Auditor

21) PW, the previous auditor, filed a report under section 143(12) of the Act with MCA and thereafter resigned from the audit engagement without issuing an audit report for FY 2018-19. M/s Dhiraj & Dheeraj, the new auditor appointed against the casual vacancy reported[16] in their report under Company Auditor's Report Order (CARO), 2016 that "*we have neither came across any instance of fraud by the company or by its officer or employee noticed or reported during the year....*". This report also drew attention to note 54 of the financial statements, in which RHFL stated that the matters reported by the previous auditor do not merit reporting under section 143(12). In this regard, the EP and the Audit Firm were charged with gross negligence, absence of due diligence and lack of professional skepticism because they did not obtain sufficient appropriate audit evidence to support the above opinion.

22) The EP and the Audit Firm denied the charges. On examination of the replies and records, we observe that the Audit File does not contain sufficient evidence of due examination of the matters reported by PW to the Government. There is no documentation of the ADT 4 form filed by PW, that contains the basis for PW's allegations. The EP stated in this regard that ADT 4 was requested from PW, but it was denied by PW citing confidentiality. Hence the Audit Firm obtained from the "*management*" the "*relevant observations*" of PW and "*evaluation of such observations by the management*". We find that this action of the Audit Firm is in disregard of its professional duties and shows the absence of professional skepticism because of the following facts:

a) In PW's NOC dated 05.07.2019, received by the Auditor, PW referred to its letter dated 18.04.2023 issued to RHFL. This letter contained the basis for the reporting of fraud by PW. Neither this letter nor a complete examination of the matters covered in this letter is found in the Audit File.

b) Also, the management response to the queries raised by PW was not documented in the Audit File. The EP submitted the response of the management along with the replies to the SCN. On perusal of this letter, we find that it did not contain all the details which were part of PW's letter dated 18.04.2023. According to PW's letter (which we obtained from PW), in the financial year 2018-19, the GPCL had increased from approximately ₹900 crores to approximately ₹7900 crore. The letter also included a list of GPCL borrowers, tested by PW on a sample basis, and the queries raised[17] to RHFL

[15] As per the decision cited in the Code of Ethics 2009, issued by ICAI (P.P. Sangani in Re: - Page 356 of Vol.VII(2) of Disciplinary Cases – Council's decision at 7th to 9th March, 1991 - Judgement dated 10th August, 1994

[16] Annexure A to the Independent Auditor's Report, clause x

[17] The key issues regarding GPCL included absence of business rationale for sanction of loans, issues in the internal control mechanism on sanctioning and disbursal of loans, procedures followed to monitor the end use of loans and for assessing the recoverability of loans, existence of borrowers, etc. In respect of certain borrowers which had negative net worth/ audit reports

in this regard. The response provided by management contained only a summary of those observations with no reference or details of the GPCL borrowers in respect of which the inconsistencies were noticed. The first paragraph of the management's response (dated May 9, 2019) states that the queries raised by PW in its letter dated April 18, 2019 "*was internally discussed with the Audit Committee at length*". However, there is no record of any Audit Committee meeting between April 18, 2019, to May 9, 2019. The first meeting of the Audit Committee for FY 19-20 was on 12th June 2019. Such instances should have alerted the ET about the veracity of the claims of the management. The absence of documentation of PW's letter and the form ADT 4 (while both were available with RHFL) is unacceptable since these were the very basis for significant matter affecting the Auditor's opinion. It is difficult to appreciate that an auditor who is aware of the filing of ADT 4 by the previous auditor should not document the issues raised and perform adequate audit procedures on the same. This shows a total absence of professionalism and is gross negligence on the part of the new Auditor. This is discussed in detail in the following paragraphs.

c) We also observe from the report of the expert[18] appointed by the Audit Firm to examine the matters reported by PW that the expert obtained from RHFL all the communications between the Company and PW, including the ADT 4 form filed by PW and PW's letter dated 18.04.2019. Yet, the Audit Firm's documentation did not contain any reference to these key communications.

d) There is no documented discussion amongst the ET members with an emphasis on material misstatement due to fraud, including how fraud might occur.[19] There is no documentation of the significant decisions reached in this regard[20]. In the limited WP[21] available, nothing is mentioned about the impact of matters reported by PW on the risk of material misstatement due to fraud. The WP only contains a list of around 20 discussion points, some of which are not even relevant to the audit of RHFL, evidencing that there were no specific discussions on PW matters.

e) It is the admitted position of the Auditor that they accepted the engagement knowing that there was a report under section 143(12) by the previous auditor. However, at the time of accepting the client itself, the Auditor concluded[22] that there was no risk of material misstatement due to fraud. There is no evidence of a due examination in this regard. There is also no proper identification and assessment of the Risk of Material

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on financial statements carried "Emphasis of matter Paragraph" on going concern status. Certain borrower companies did not seem to have any business other than borrowing from RHFL for onward lending, certain borrower companies were incorporated shortly before disbursement of loans, having limited/no revenue, and loan sanction date is same as the loan application date. Certain borrows having email IDs carrying 'Reliance ADA' domain, borrower company name containing 'Reliance' in its name, companies having directors which are employees of Reliance ADA group, multiple companies registered at the same physical address etc.

[18] WP E. Checklists\E.4.Standards on Auditing\E.4.2.SA Working Paper\WP SA 240

[19] Paragraph 15 and 44 of SA 240 and Paragraph 10 of SA 315

[20] Paragraph 44 of SA 240

[21] K.12. Fraud Meeting Discussion

[22] In WP K.9.Client-Engagement Acceptance & continuance checklist

Misstatement due to fraud at the financial statement level and at the assertion level as required by SA 315[23]. This is also a matter compulsorily required to be documented as per the documentation requirements of SA 240.

f) For loans and revenue, there is no documented examination of the incentive or pressure to commit fraud or a perceived opportunity to do so or the ability to rationalise a fraudulent action and audit procedures as required by SA 240[24], even after the reporting of suspected fraud by PW.

g) There is no challenge to the management or performance of audit procedures as required by SA 240[25] even though the loans to corporate bodies during the year unusually increased by 130% compared to the previous year. It constituted 48% of the total loans and about 43% of the total balance sheet size. The observations[26] in the Audit File, (such as "nil recovery rate, no credit assessment in terms of recoverability, no system of ascertaining end use, newly formed borrower companies having no business or project plan etc.) evidence that the recoverability of these loans was never assessed based on the strength of the borrower/ultimate borrower. There is also no challenge on any of the management contentions regarding irregularities in credit approval and sanction, credit policy, end use of borrowings, the creditworthiness of borrowers, the high risk and low success rate of some borrowers, cash flow mismatch, absence of business plan for certain borrowers, deviations in approval, and non-monitoring of borrowers accounts. The business rationale for sanctioning such loans[27] is not verified in all cases.

h) There is no documentation for understanding how those charged with governance (TCWG) exercised oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control to mitigate these risks[28].

i) WP SA 530.1 referred by the EP documents that 100% population needs to be tested for non-housing loans (GPCL). Later in the same work paper, the ET took less than three-fourths of the GPCL as the sample. The audit procedure performed is limited to verification of the arithmetical accuracy of the data given by the Company. Similarly, the Auditor contends that the evaluation of credit appraisal, authorization of loan disbursement, verification of end-use of funds, etc. was done on a test basis. However, sufficient substantive procedures have not been performed by the Auditor as discussed in detail in section C5 below. Further, the claim by the Auditor that impairment has been made on the specific loans identified by PW is unacceptable, since the Auditor's

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[23] SA 315, Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment

[24] Paragraph 5, 8, 11, 12 and paragraph 44 (b), 45 to 47 of SA 240 -The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements

[25] paragraphs 12 to 14, 23, 24, and 28 to 33 of SA 240

[26] WP "4.20 Observations on GPCL"

[27] paragraph 32(c) and A47 of SA 240

[28] Paragraph 20 of SA 240

procedures for verifying the Expected Credit Loss (ECL) on these loans were grossly inadequate as explained in section C4 of this Order.

j) As it is evident from the reply to the SCN, and as explained in pre-paragraphs, the Auditor has placed reliance only on enquiries with the management on several significant areas, including key observations of the previous auditor. However, as explained in paragraph A2 of SA 500, although inquiry may provide important audit evidence, inquiry alone ordinarily does not provide sufficient audit evidence of the absence of a material misstatement at the assertion level, nor of the operating effectiveness of controls. When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes, including as necessary in the circumstances[29]. Such evaluation is absent in this case.

23) In his reply, the EP referred to the resignation letter issued by PW and stated that *"It may be noted that PW in their resignation letter in point 2 and point 3 has specifically stated "2. As part of ongoing audit for FY 2018-19, we noted certain observations/transactions which in our assessment might, if not resolved satisfactorily, be significant, material and substantive to the financial statements... 3. We did not receive substantive/satisfactory responses to our queries in light of our observations. Accordingly, we sent a letter dated 18 April 2019 under the provisions of Section 143(12) of the Companies Act,2013....."..... ...The above statements of PW in their resignation letter, in the engagement team opinion, clearly and directly indicated that they did not receive substantive/satisfactory responses to their queries, which made them to report under section 143(12) of the Act. The legal opinions obtained by the management also confirmed the above, same understanding as of ours"*.

24) We note that no such conclusions are documented in the Audit File. Hence the above statements of the EP, endorsed by the Audit Firm and EQCR Partner, can only be considered as a rationalisation of the omissions. Further, the above statements are evidence of the absence of professional skepticism, because the whole focus of the EP is on the second part of the statement of PW where PW states the absence of a satisfactory response from RHFL regarding the transactions. However, according to PW, the impact of these transactions, if remained unresolved, would *"be significant, material and substantive to the financial statements"*. It was the professional duty of the Audit Firm to rule out any impact of these transactions on the financial statement assertions before concluding that there was no fraud or error. This required rigorous audit procedures, covering all the significant transactions pointed out by the previous auditor, with a focus on possible fraud factors as prescribed in SA 240, which is absent in this case. Any prudent auditor can understand the indications that the Company has attempted to depict irrecoverable loans as recoverable, thereby materially misstating the financial statements. Also, there were possible instances of siphoning off of money, indicated by irrational business decisions, multiple layers of transactions and borrowers having insufficient resources. In the latter case, the scope of the examination is much deeper than the reasonable assurance expected from a statutory auditor and hence called for specialised investigations. Until such investigations are

[29] Paragraph 9, SA 500 – Audit Evidence.

completed, the Auditor could not be in a position to conclusively rule out the reported fraud. However, neither the Auditor suggested any such investigations to the Company nor the company suo motu undertook any such examinations. Instead, the Company acquitted itself of the allegations and the Auditor agreed to the views of the Company without the required examination, as explained in the above paragraphs. Such actions of the Auditor amount to gross negligence since the matter involved was material and pervasive to the financial statements.

25) Based on the above, the charges in paragraph 21 regarding gross negligence, absence of due diligence and lack of professional skepticism in verifying the significant matters reported by the previous auditor are established.

C.3. Evaluation of the Going Concern Assumption

26) RHFL prepared its financial statements on the assumption that the Company was a Going concern. However, the Audit File did not contain sufficient basis for the Audit Firm to conclude and report that there was no material uncertainty regarding the Going Concern status of RHFL. The disclosure made by the Company in this regard was inadequate. The Auditor was hence charged with non-compliance with the requirements of paragraphs 19 and 23 of SA 570[30] regarding the procedures to be performed in the evaluation of the going concern assumption.

27) In the Audit File[31] and minutes of the meeting with the management on the going concern, the Auditor has listed the following events and conditions that may cast significant doubt on the entity's ability to continue as a going concern:

a) *Reduction in Company's credit rating to "D" grade in respect of Non-Convertible Debentures (NCD), Short-term Debts and Long-term Debt Programme (Banking).*
b) *Liquidity crunch leading to defaults in repayment of its debt obligations amounting to ₹491.67 and extension of maturities of its non-convertible debentures amounting to ₹400 crore.*
c) *Non-recovery of loans granted under GPCL amounting to ₹566.30 crore.*
d) *Engaging with its lenders to enter into an Inter-Creditor Agreement (ICA) for the resolution of its debt.*
e) *Major shift in the primary business of the company from Housing Finance to Non-Housing Finance.*

28) Paragraph 16 of SA 570 requires that when the events and conditions are present that may cast significant doubt on the entity's ability to continue as a going concern, the auditor has to obtain sufficient appropriate audit evidence through audit procedures to determine whether a material uncertainty exists. The procedures include the evaluation of management's plan for future actions (paragraph 16 (b) of SA 570) and if a cash flow forecast is prepared by the management, then analysis of this forecast by evaluating the reliability of underlying data and evaluating the adequacy of the underlying assumptions (paragraph 16 (c) of SA 570).

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[30] SA 570, Going concern

[31] WP "SA 570.1"

29) The minutes of the meeting with management recorded the management's views that the above events do not cast a material uncertainty. However, there is no further independent examination by the Auditor of these contentions of the management, as required by paragraph 16 of SA 570. Though the ET obtained the cash flow forecast prepared by the management, it did not perform any audit procedure to evaluate the reliability of the underlying data and adequacy of the assumptions. The ET neither obtained nor analysed any detailed maturity profile (fortnightly and monthly) of assets and liabilities over the next 12 months to support the forecast given by the company nor did they examine the probability of the positive outcome of restructuring of loans and ICA (Inter-Creditor Agreement) (paragraph 16(b) of SA 570).

30) As per paragraph 18 of SA 570, a material uncertainty exists when the magnitude of its potential impact and likelihood of occurrence is such that, in the auditor's judgment, appropriate disclosure of the nature and implications of the uncertainty is necessary for the fair presentation of the financial statements. Thus, on noticing the significant events or conditions that may cause material uncertainty, the ET needs to consider:

a) the magnitude of potential impact, i.e., will the impact of these events effectively put the entity out of business or what is the worst-case scenario?
b) The likelihood of occurrence, i.e., does the management have a realistic contingency plan or how do they plan to deal with the impact on day-to-day operations?

None of the above requirements are considered by the ET. Scenario mapping is essential here and should form part of management's assessment of the going concern, which was absent in this case.

31) RHFL had entered into the ICA for the resolution of its debts. The EP in his reply stated that there was no material uncertainty in going concern as evidenced by the ICA, documented in the Audit File[32], for the resolution of debts. However, we observe that the existence of ICA containing a debt resolution plan cannot evidence the absence of material uncertainty on the going concern status. As per paragraph 26 of Ind AS 1[33] when an entity has a history of profitable operations and ready access to financial resources, the entity may conclude that the going concern basis of accounting is appropriate without detailed analysis. This is not the case here since RHFL does not have ready access to financial resources as evidenced by the need for entering into ICA, default on debt obligations and absence of fresh credit lines. In such cases, Ind AS 1 states that the management may need to consider a wide range of factors relating to current and expected profitability, debt repayment schedules and potential sources of replacement financing before it can satisfy itself that the going concern basis is appropriate. There are no such considerations in this case.

32) Assuming, but not admitting, that there is no material uncertainty as claimed by the EP, then paragraph 20 of SA 570 requires the auditor to evaluate the adequacy of disclosure in the financial statements where events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern. Note No. 17(d) of

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[32] In WP 570.1

[33] Indian Accounting Standard (Ind AS) 1 - Presentation of Financial Statements

the Financial Statements contains disclosure on the Company's going concern assumption which does not fully disclose the events or conditions and the mitigation plan. The disclosure made by the Company neither discussed the details of financing arrangements such as the magnitude, timelines, the availability of refinancing etc. The Independent Auditor's Report included an 'Other Matter' paragraph on going concern which stated that the liquidity mismatch was resulting in delayed payment of bank borrowings and the Company's ability to meet its obligation was dependent on "*material uncertain*" events. This is not in line with the Company's disclosure since the disclosure did not describe any of the events as "*material uncertain*". Such inconsistencies and non-compliance with SAs show that the audit opinion is without adequate basis.

33) Thus, when events that may cast significant doubt on the going concern status are present, the auditor must perform further audit procedures as mandated by SA 570 to rule out the existence of material uncertainty. No such procedures are performed by ET. The disclosures made in the financial statements and the reporting by the Audit Firm are incomplete and, therefore, misleading. Hence, there is no adequate basis for the Audit Firm to conclude that the going concern basis is appropriate. The charges in paragraph 26, therefore, are established.

34) We note the statement of the Audit Firm that their documentation is not strong enough to support their claims that they have carried out all the required compliances as required by SA 570 to prove that no 'material uncertainty' existed. However, we observe that this is not just a documentation issue; the audit procedures to obtain sufficient appropriate audit evidence mandated by SAs are absent in this case.

35) Such lapses have been viewed seriously by international regulators as well. For example, the Public Company Accounting Oversight Board (PCAOB), the US Regulator, charged[34] Bravos & Associates CPA's ("Firm") and Thomas W. Bravos, CPA ("Bravos") in connection with the audit of UAHC for FYE June 30, 2013, where Bravos authorized the issuance of the Firm's unqualified audit report, which included going concern explanatory language regarding those Financial Statements. However, Respondents did not have a reasonable basis for making these statements and issuing their audit report". For misconduct including this and others, PCAOB censured the firm by revoking its registration and imposed a civil monetary penalty of $ 10000 on the firm. Bravos was barred from being an associated person of a registered public accounting firm.

C.4. Verification of Expected Credit Loss (ECL) on Financial Assets

36) The value of loans given as on 31st March 2019 amounted to ₹16,251.09 crore (net of ECL of ₹278 crore). The loans constituted around 90% of RHFL's balance sheet size. In this regard, the EP and the Audit Firm were charged with failure to notice the deficiencies in the internal controls over ECL on the loans, deficiencies in the ECL model of the Company and material shortfall in ECL provisions. The EP and the Audit Firm were also charged with failure to perform planned audit procedures, despite identifying ECL as a Key Audit Matter (KAM).

[34] PCAOB release No. 105-2015-028 dated 23.07.2015.

37) In their reply, the EP and the Audit Firm referred to WPs at the audit planning stage[35] in which it had noted the planned procedures in respect of ECL. All the WP references provided in the response to SCN primarily reflect the audit plan/strategy relating to ECL. The Auditor failed to show sufficient appropriate evidence to support the assertions in the financial statements relating to ECL. In the absence of adequate evidence, we conclude that the following omissions and commissions, as conveyed in the SCN, contributed to the absence of verification of ECL.

a) There is insufficient evidence of substantive procedures performed to verify the ECL model. The WP[36] available in this regard is a copy of the calculations of ECL as per the Company's ECL model. As per the model, the Company classifies an asset into one of the three stages solely based on Days Past Due (DPD) status. There is no consideration of the qualitative criteria for classifying loans. This is not in conformity with paragraph 5.5.11 of Ind AS 109, which states that if *"reasonable and supportable forward-looking information is available without undue cost or effort, an entity cannot rely solely on past due information when determining whether credit risk has increased significantly since initial recognition. However, when information that is more forward-looking than past due status (either on an individual or a collective basis) is not available without undue cost or effort, an entity may use past due information to determine whether there have been significant increases in credit risk since initial recognition."* As per the requirements of SA 540, and SA 200 it is required to exercise professional skepticism particularly when auditing complex accounting estimates, such as ECL. Note 1 d. (ii) of the financial statements[37] underlines the complexity of ECL calculations. Yet, there is no challenge to the assumptions and the underlying data sources, which shows the absence of professional skepticism.

b) Similarly, the Company's assessment of whether a loan or portfolio of loans has experienced a significant increase in credit risk should also be based on forward-looking indicators, if available without undue cost or effort, as per Ind AS 109. Paragraph B5.5.17 of Ind AS 109 gives a non-exhaustive list of information that may be relevant in assessing changes in credit risk. Accordingly, the assessment of a significant increase in credit risk is generally driven by the credit rating of the loan and also considers a combination of other information that is specific to individual borrowers or portfolios, as the case may be. However, the calculations in the Audit File do not consider any such factors in assessing the increase in credit risk.

c) There are several significant loans[38] where the standard conditions were waived, eligibility was not as per norms, loan amount exceeded the maximum permitted, return on investments was below norms, no credit ratings, no ESCROW accounts and no cashflows/income. The ET also noted that *"GPCL has been sanctioned to Newly Formed Entities (formed in 2018-19) without having Credit/business*

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[35] WP "K.2 – Audit Programme" and WP "K.5 Overall Audit Strategy"

[36] "2.ECL MODEL DEVELOPMENT.pdf"

[37] *"The measurement of the ECL allowance is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses)."*

[38] As per the WP "SA 705.2"

assessment/project report". Many borrowers did not have the financial strength to get such loans but the loans were disbursed. Therefore, all such loans disbursed during the year met the definition of Purchased or Originated Credit Impaired asset (POCI). However, the company did not recognise these loan assets as POCI thereby violating provisions of Ind AS 109 and Ind AS 107. Such loans were originated credit impaired and hence were required to account with a carrying value reflecting the lifetime expected credit losses as per Ind AS 109. A few instances noticed, to gauge the extent of misstatements, are given below.

i) RHFL sanctioned loans of ₹50 crore to Hirma Power Ltd, and ₹55 crore to Tulip Advisors Private Ltd in FY 18-19. The total exposure of these two Companies was shown as ₹444.67 crore as per the ECL workings[39]. As per the audit documentation[40], these two companies had virtually no revenues and were in losses. The net worth was completely eroded, and the loans were disbursed without any security, having no credit rating and after waiving all the requirements for a corporate loan as per the company's policies. Still, these loans were classified under stage 1, with a nominal ECL of ₹41 lakh[41]. These loans were evidently credit impaired right from the time they were made. As per Ind AS 109, financial assets that are credit-impaired upon initial recognition are categorized within Stage 3 with a carrying value already reflecting the lifetime expected credit losses. However, the loan was classified under stage 1 without any reduction in carrying value to reflect the credit impairment. This has resulted in material misstatements in the Financial Statements leading to the understatement of losses and overstatements of loans, the quantum of which cannot be assessed in the absence of data.

d) The ET noted in the Audit File[42] certain Risks of Material Misstatements (ROMM) as per SA 315. Regarding ECL it is mentioned that "*Risk identified is of inappropriate assumption used or judgement made may result in material misstatement.*" However, there is no documentation of the risk assessment procedures performed as per paragraph 6 of SA 315 to arrive at the above conclusion. There is also no identification and assessment of ROMM at the assertion level for classes of transactions, account balances, and disclosures. There is no linking of the identified risks (the completeness of which is not evidenced) to 'what can go wrong' at the assertion level. Also, there is no mention of whether the identified risks are significant.

e) As per KAM, testing of internal controls over ECL was one of the procedures claimed as performed. However, the Audit File[43] did not even mention ECL anywhere in control testing. The WP in this regard appears to be copied from somewhere else since the controls still mention AS 22 and AS 18, while the applicable standards were Ind AS. The details of who prepared this WP, who reviewed it and the timing of audit procedures performed are also absent in this WP. The KAM also mentions the

[39] WP 1.ECL FRM disclosure working 19Aug2019.

[40] WP 4.10.CAM

[41] Sheet Mar' 19 of WP 1.ECL_FRM disclosure working 19Aug2019.

[42] WP "K. 13 WP SA 315.1,"

[43] WP "K.8. Internal Financial Control Testing.pdf'

engagement of specialists to test the ECL model. However, no such experts were engaged as per SA 620. There is also no documentation in the Audit File regarding the skills and competencies of the ET members who were conversant with ECL calculations. This is in contravention of paragraph 14 of SA 540 as well.

f) In the Audit Report on internal financial controls over financial reporting, a qualified opinion is provided stating that the company's internal financial control system over financial reporting was not operating effectively for "*General Purpose Corporate Loan Product*" due to weak credit appraisal and loan sanctioning mechanism. However, there is no assessment of the consequences of this material weakness on ECL calculations. There is also no separate test of the design, implementation, and operating effectiveness of internal controls on ECL as required by SA 540 and SA 315.

g) The Company provided the percentages of average Probability of Default (PD) rates, Loss Given Default (LGD) rates, and the ECL amount. However, other than checking the arithmetical accuracy of the calculations[44] there is no examination by the ET. Even the basic tests or questions to the management were not raised in evaluating the ECL. For instance, there is no evidence of:

   i) How the Auditor ruled out the possible management bias in the ECL model and calculations.

   ii) The Company's and borrower's (group companies) going concern were affected by significant uncertain events. There is no evidence of how these events were factored into the working of PD. As it appears from the WPs, the Company has simply adopted the average PD and LGD calculated in the previous year without considering any adjustments for the forward-looking information reflecting the uncertainties at present. The Audit Firm did not examine how these events had impacted the criteria for the significant increase in credit risk underlined by Ind AS 109.

   iii) There is no documentation regarding the ET's understanding of how the relationships between macroeconomic variables and (i) default rates, (ii) collateral values and (iii) repayment history have been established to estimate PD and LGD. This may include the identification of what statistical approach/framework has been applied to establish these links and what testing has been carried out to determine the statistical significance and unbiased nature of the model.

38) The above facts prove that the Auditor did not perform any of the audit procedures stated as performed in the KAM. The limited procedures performed are not sufficiently responsive to the actual risk associated with the financial statement assertions, particularly regarding the GPCL of ₹7849 crore to credit-impaired entities on which ECL was only ₹173 crore[45]. The Auditor did not examine the internal controls over ECL, deficiencies in the ECL model of the Company and material shortfall in ECL provisions. In the light of above, the KAM and the audit opinion issued are false. Thus, the charges in paragraph 36 above are established.

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[44] WP 4.14, 4.2, 4.3 etc.

[45] WP 1.ECL_FRM disclosure working_19Aug2019, tabMar'19, column filters AP-'Corporate Lending' and AH 'MORTGAGES – CORP'.

39) Such lapses in challenging the management and absence of professional skepticism are viewed seriously by audit regulators across the world. In the matter of K.R. Margetson Ltd. and Keith R. Margetson[46], the US audit regulator PCAOB imposed sanctions on an auditor for failure to appropriately evaluate the reasonableness of a discount rate used in developing the valuation estimate. The sanctions included revocation of registration of the firm, restrictions in acting as EP and a civil money penalty of $30,000. In the matter of Martin Lundie, CPA[47] (Partner, EY Canada), PCAOB imposed sanctions for failing to sufficiently test the assumptions underlying the estimate and by failing to sufficiently test the accuracy and completeness of data on which that estimate was based. Sanctions included debarring from being an associated person of a registered public accounting firm and a civil money penalty of $65,000.

C.5. Modification of the Audit Opinion on the Financial Statements

40) The Auditor issued a qualified opinion on the basis that sufficient appropriate audit evidence was not available to ascertain the recoverability of principal and interest, including the time frame of recovery, of overdue amounting to ₹566.30 crore of General Purpose Corporate Loans as on March 31, 2019. In this regard, the EP and the Audit Firm were charged with failure to consider the pervasiveness of GPCL transactions and balances while forming the audit opinion, thereby violating SA 330[48] and SA 705(Revised).

41) In their reply to the SCN, the EP and the Audit Firm reiterated their conclusions recorded in the Audit File and stated that "*Our concern on the GPC loan was primarily regarding non-availability of audit evidence to ascertain recoverability of principal and interest including time frame of recovery of overdues of GPCL as on March 31, 2019. Since this matter was isolated and specific to recovery of overdues of GPCL, in our professional judgement had concluded that our audit report should be qualified in respect of this matter.*" The Audit Firm also stated that "*There is no material misstatement in recording of GPCL transaction with respect to income recognition, provisioning and classification.*"

42) Without prejudice to the fact that the ET failed to obtain sufficient appropriate evidence regarding ECL provision and GPCL given to group companies, as proved in the previous sections, we observe the following regarding the Audit Firm's contentions on modification of the audit opinion:

a) The Independent Auditor's Report contains a qualified opinion, concerning GPCL aggregating to ₹7,849.89 crore, because of not getting sufficient audit evidence to ascertain the recoverability of principal and interest including the timeframe of recovery of overdue of ₹566.30 crores. This overdue is only the principal outstanding as on 31-03-2019. There is no disclosure of the interest overdue of ₹86 crore, though the non-availability of sufficient appropriate audit evidence includes the interest also.

b) There were other loans of ₹292 crore disbursed to the same borrowers in FY 2018-19, before the default on the first loans. There was also an accrued interest of ₹26 crore on these loans. On default of the first loans, no audit checks were conducted to ensure that

[46] PCAOB Release No. 105-2023-023 September 12, 2023.

[47] PCAOB Release No. 105-2022-040 December 22, 2022

[48] SA 330, The Auditor's Responses to Assessed Risks

the fresh loans sanctioned before default will be recovered by the Company on due dates. Hence there is no sufficient appropriate audit evidence for the recoverability of the new loans also.

c) The ECL provision on the total loans amounting to ₹945.58 crore (i.e., loans mentioned in the qualification and other loans to the same parties not considered in the qualification) was ₹107 crore. This ECL of ₹107 crore is not a subject matter of qualification. However, there is no basis for the accuracy of ECL, which should be a forward-looking estimate, when the ET was unable to obtain evidence on the recoverability of the loan balances.

d) The Audit File[49] lists significant deviations from the lending policy, while sanctioning loans to 45 borrowers whose outstanding GPCL amounted to ₹7490 crore. These borrowers were evidently credit impaired. The listed deviations also included factors such as not registering the charges, sanction of loans to new entities without any business assessment, irregularities/deviations in the approval process, discrepancies in credit appraisal, no recovery steps despite defaults in repayment, non-monitoring of borrower accounts post-disbursal, etc. The management has failed to provide any explanations regarding the recoverability of the entire outstanding balance. So, there is not enough basis for the ET to conclude that the absence of sufficient evidence is limited only to the principal and interest outstanding on some loans out of this population.

e) Note no. 4 of the financial statements contain the disclosures about the loan balances where the company has asserted that the loans and other credit facilities given to customers are secured. However, the ET had observed that in many cases loans were disbursed without the creation of security. This impacts recoverability and shows the Auditor's agreement with the misleading assertion by the Company.

f) Overall materiality was fixed at ₹15.34 crore. The principal overdue and interest overdue were much above the materiality level. Since there is no evidence for the recoverability of GPCL, the accounting assertions of valuation of the loans amounting to at least ₹945.58 crore, accuracy of interest outstanding amounting to ₹112 crore and accuracy of ECL amounting to at least ₹107 crore remains unverified. The above assertions had impacted the Total Income, Total Expenditure, Net Profit, Earnings Per Share, Total Assets, Total Liabilities, Net worth and Notes to Accounts. Hence the misstatements were pervasive in terms of SA 705 because they are not confined to just one element of the financial statements. However, the Audit Firm concluded that "*....the possible effects on the financial statements are Material but Not Pervasive...* " and issued a qualified opinion, that too with partial disclosures under the basis of qualified opinion in the audit report. In this case, as per SA 330 read with SA 705 (Revised) it was required to issue a disclaimer or adverse opinion, which the Audit Firm did not do.

43) In light of the above, the Auditor is guilty of professional misconduct of not complying with the requirements of SA 705 (Revised) and SA 330 and the charges in paragraph 40 above are established.

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[49] WP 'SA 705.2 Significant Deviation.pdf and WP "WP SA 705.2 Observations on GPCL"

C.6. Use of the work of Management's Expert and Auditor's Expert

44) In note 54 of the financial statements regarding the reporting by PW, RHFL asserted that "*The Company has examined the matter and has concluded that the issues raised by the previous auditors, do not merit reporting under the said Section. The Company also appointed legal experts, who independently carried out an in-depth examination of the matter and the issues raised by the previous auditor. The legal experts have concluded and confirmed that there was no matter attracting Section 143(12) of the Companies Act, 2013.*" In addition to the legal experts (management's expert) mentioned above the Audit Firm also appointed a legal expert (auditor's expert) to examine the same matter. In this regard, The EP and Audit Firm were charged with failure to comply with the requirements of SA 500[50] and SA 620[51] regarding using the work of the management's expert and auditor's expert respectively. Consequently, they were also charged with failure to exercise due diligence and the required professional skepticism as mandated by SA 200.

45) The EP and the Audit Firm submitted that they did not consider any of the legal opinions as the basis for concluding the matter of fraud and hence compliance with the requirements of SA 500 and SA 620 does not arise. We observe that the submissions are contradictory to the facts, as explained hereafter.

a) Note 54 discloses a material matter that has a pervasive effect on the financial statements. The Auditor concurred with this note explicitly in their audit report as explained in the previous paragraphs of this Order. As per note 54 quoted above, the basis for ruling out fraud, reported by PW under Section 143(12) was, (a) the Company's examination of the matter and (b) an "*in-depth examination*" by the management's experts. In its audit report under CARO 2016, the Audit Firm drew attention to note 54 of the financial statements. These facts show that the EP had used the work of the legal experts, without which he cannot endorse a statement made by the company regarding the work of the management's experts.

b) However, the Auditor admitted that they had not relied on management's experts. Also, as evidenced by the Audit File and as admitted, the EP has not complied with the prerequisites for the use of the work of an expert. As far as the stated examination by the Company, we have already concluded in the previous paragraphs that the Auditor failed to obtain sufficient appropriate evidence regarding the matter reported by PW. Hence there is no adequate basis for the Auditor to endorse the assertions contained in note 54. The evident use of the work of experts, as is seen from the audit report, is thus misleading the users.

c) Even after documenting various pieces of evidence supporting the previous auditor's observations, the Auditor went along with the management in stating that there was no fraud in the Company. It was observed that the legal opinions obtained by the management were based only on the correspondence between the Company and PW. The mandate given by the Company to the legal experts did not include the merits of the transactions referred by the previous auditor. Yet, the Audit Firm endorsed, without

[50] SA 500, Audit Evidence

[51] SA 620, Using the Work of an Auditor's Expert

basis, the conclusion reached by the Company based on legal opinion that there was no fraud, while the matter was still pending with the regulator (MCA), to which a statutory report under Section 143(12) had been filed by the previous auditor.

d) The Auditor's expert[52] was engaged to examine the matter reported by PW, but no agreement was documented regarding the nature, scope, and objectives of the expert's work. The expert's opinion was based solely on correspondence between the company and PW, with no documentation of how the expert accessed this information. Key documents, such as the report filed by PW, stated as obtained by the Auditor's expert were not even seen by the ET. There is no documentation evaluating the adequacy of the expert's work or their findings' relevance and reasonableness. No audit procedures as required by SA 620[53] were documented in the Audit File.

46) In light of the above, it is clear that the Auditor has failed to carry out adequate audit procedures. Its purported independent examination of the matters was significantly deficient in arriving at a reasonable conclusion on the matter of suspected fraud. The Auditor's said opinion is neither supported by the works of the management's expert nor the auditor's expert. Consequently, we conclude that the Audit Firm issued a misleading audit report. Hence, the charges in paragraph 44 above are proved.

C.7. Engagement Quality Control Review (EQCR)

47) The EQCR Partner and the Audit Firm were charged with failure to ensure compliance with SA 220[54] and SQC-1 because of the EQCR Partner's failure to objectively evaluate the significant judgments and conclusions of the ET. The EQCR Partner failed to conduct the review on time at appropriate stages during the engagement (paragraph 66 of SQC 1) and document procedures or observations on any of the significant matters arising during the audit as required by SA 220. The WPs[55] are limited to a checklist and the EQCR partner's blind agreement to the conclusions of the ET.

48) In response to the above charges, the EQCR Partner stated that he was involved in the evaluation of significant judgements made by the ET through participation in planning and audit committee meetings, discussion with the EP, review of certain documents and documentation as per the checklist provided by the Audit Firm. He further claimed that the documentation requirements specified in paragraph 25 of SA 220 are met and that he is not bound by SA 230.

49) On perusal of the WPs and the response submitted by the Auditor, we observe the following:

a) Paragraph 20 of SA 220, which describes the responsibility of EQCR Partner, specifically requires EQCR Partner to objectively review selected audit documentation relating to the significant judgments the ET made and the conclusions it reached.

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[52] M/s Mrugank and Basutkar, Advocates, were deployed by the Auditor and opinion obtained therefrom was placed in audit file at "WP Opinion.4.pdf"

[53] Paragraph 9 to 13 of SA 620

[54] SA 220, Quality Control for an Audit of Financial Statements

[55] Contained in the Audit File's folder namely "J. Engagement Quality Control Review".

Paragraph 20 also mandates discussions with the EP. However, except for the sign-offs by the EQCR Partner on limited WPs[56], the Audit File does not contain evidence of any objective evaluation of WPs by the EQCR Partner or of discussions with the EP.

b) The preceding paragraphs already show EP's failure to perform sufficient audit procedures as mandated by SAs. By agreeing with all the conclusions of the EP, the EQCR partner demonstrated failure to perform his duty of objective evaluation of the significant judgements made by the EP.

c) Given the mandatory provisions in SA 220, the EQCR Partner is required to document the reasons and the bases for its conclusions, the review procedures adopted, the professional judgments made, the areas in which the EQCR challenged the audit team, the significant matters the EQCR discussed with the audit team, the areas of disagreements, the resolutions reached, and the additional evidence/ documents/explanations considered in such cases. This is in addition to the mandatory documentation requirement of that standard. However, as explained in the previous paragraphs of this Order, the cryptic documentation of the EQCR Partner did not evidence compliance with all the requirements of SA 220 and the Audit Firm's responsibilities as per SQC1.

50) In light of the above, it is proved that the EQCR Partner has failed to exercise due diligence and carry out adequate audit procedures as required by SA 220 and SQC 1. The Audit Firm did not supervise the work of the EQCR adequately, leading to the serious omissions of the ET remaining unquestioned. Hence the charges in paragraph 47 above regarding non-compliance with SA 220 and SQC-1 stand proved.

51) We also observe that such lapses have been viewed seriously by international regulators as well. For example, PCAOB[57], the US Regulator, charged Grant L. Hardy (CPA) for his failure in connection with his role as Engagement Quality Reviewer ('EQR' hereafter) in the audit of financial statements of some of the issuer clients and noted that "Hardy violated PCAOB Auditing Standard No. 7, Engagement Quality Review ("AS 7") by providing his concurring approval of issuance without performing with due professional care the EQRs required by this standard for the Firm's audits of COPsync and Forever Green's December 31, 2010, financial statements and AEG's June 30, 2011, financial statements." For this misconduct, PCAOB censured the EQR, barring him from being an associated person of a registered public accounting firm for 1 year.

52) PCAOB in the matter of Cheryl L. Gore, CPA and Stanley R. Langston, CPA, charged[58] Stanley R. Langston (CPA) for his failure in connection with his role as Engagement Quality Reviewer in the audit of financial statements of some of the issuer clients and noted in its order dated 14.12.2021 that "Langston violated AS 1220, Engagement Quality Review, by providing his concurring approval of issuance of the Firm's audit reports without performing the required engagement quality reviews with due

[56] WP pertaining to risk assessment and going concern assumption assessment

[57] PCAOB release no 105 2015 001 dated 12.01.2015

[58] PCAOB Release No. 105-2021-020 December 14, 2021

professional care." For this misconduct, PCAOB imposed restrictions on Langston, barring him from being an "engagement partner" or EQC Reviewer for 1 year and also imposed a monetary penalty of $10,000. Furthermore, in another case, PCAOB found[59] that Donald R. Burke, CPA, failed to evaluate properly the engagement team's assessment of, and audit responses to, significant risks identified by the engagement team, including fraud risks. As a result of his failure to perform Engagement Quality Reviews with due professional care, among other things, Donald R. Burke, CPA was suspended from being an associated person of a registered public accounting firm for a period of one year and imposed a $10,000 civil money penalty upon Burke.

C.8. Compliance with SA 230

53) The Auditor was charged with non-compliance with paragraph 9 of SA 230 which requires documentation of who performed the audit work, the date such work was completed, who reviewed the audit work performed, date and extent of such review. There are several key workpapers[60] in the Audit File without such details.

54) The Auditor stated that they will be more vigilant and cautious in future in this regard. This charge, though proven, is not considered in the determination of sanctions, given the admission and commitment by the Auditor.

D. FINDINGS ON THE ARTICLES OF CHARGES OF PROFESSIONAL MISCONDUCT

55) As discussed, the Auditor has made a series of departures from the Standards and the Law, in conduct of the audit of Reliance Home Finance Limited for FY 2018-19. Based on the above discussion, it is proved that the Audit Firm issued an audit opinion on the Financial Statements without adequate supporting evidence. Based on the discussion and analysis, we conclude that the EP, EQCR Partner and the Audit Firm have committed Professional Misconduct as defined in the Act, as below:

a) The Audit Firm M/s Dhiraj & Dheeraj and the EP CA Piyush Patni committed professional misconduct as defined by Section 132(4) of the Companies Act, 2013, read with Section 22 and Clause 5 of Part I of the Second Schedule of the Chartered Accountants Act, 1949 (No. 38 of 1949) as amended from time to time, which states that a CA is guilty of professional misconduct when he "fails to disclose a material fact known to him which is not disclosed in a financial statement, but disclosure of which is necessary in making such financial statement where he is concerned with that financial statement in a professional capacity".

   This charge is proved as the Audit Firm and EP failed to disclose in their report the material non-compliances the Company made as explained in sections **C.2 to C.6** above.

b) M/s Dhiraj & Dheeraj and CA Piyush Patni committed professional misconduct as defined by Section 132 (4) of the Companies Act, 2013, read with Section 22 and Clause

[59] PCAOB release no. 105-2021-012 dated 29.09.2021

[60] WPs "K.1 Understanding the Entity and its environment.pdf", "K.6 Substantive Audit Procedure.pdf", "K.10. Preliminary Variance Analysis.pdf", "SA 265.1", "SA 520.1", "4.20.GPCL Observation", etc.

6 of Part I of the Second Schedule of the Chartered Accountants Act, 1949 (No. 38 of 1949) as amended from time to time, which states that a CA is guilty of professional misconduct when he "fails to report a material misstatement known to him to appear in a financial statement with which he is concerned in a professional capacity".

This charge is proved as the Auditor failed to disclose in their report the material misstatements made by the Company as explained in paragraphs **C.2 to C.6** above.

c) M/s Dhiraj & Dheeraj, CA Piyush Patni and the EQCR Partner CA Pawan Kumar Gupta committed professional misconduct as defined by Section 132 (4) of the Companies Act, 2013, read with Section 22 and Clause 7 of Part I of the Second Schedule of the Chartered Accountants Act, 1949 (No. 38 of 1949) as amended from time to time, which states that a CA is guilty of professional misconduct when he "does not exercise due diligence or is grossly negligent in the conduct of his professional duties".

This charge is proved as the Auditor, conducted the audit of a Public Interest Entity in total disregard of their statutory duties, evidenced by multiple critical omissions and violations of the standards. The instances of failure to conduct the audit in accordance with the SAs and applicable regulations, and failure to report the material misstatements in the financial statements and non-compliances made by the Company are as explained in paragraphs **C.1 to C.7** above.

d) M/s Dhiraj & Dheeraj, CA Piyush Patni and CA Pawan Kumar Gupta committed professional misconduct as defined by Section 132 (4) of the Companies Act, 2013, read with Section 22 and Clause 8 of Part I of the Second Schedule of the Chartered Accountants Act, 1949 (No. 38 of 1949) as amended from time to time, which states that a CA is guilty of professional misconduct when he "fails to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion".

This charge is proved as the Auditor failed to conduct the audit in accordance with the SAs and applicable regulations as well as due to their total failure to report the material misstatements and non-compliances made by the Company in the financial statements as explained in paragraphs **C.1 to C.7** above.

e) M/s Dhiraj & Dheeraj and CA Piyush Patni committed professional misconduct as defined by Section 132 (4) of the Companies Act, 2013, read with Section 22 and Clause 9 of Part I of the Second Schedule of the Chartered Accountants Act, 1949 (No. 38 of 1949) as amended from time to time, which states that a CA is guilty of professional misconduct when he "fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances".

This charge is proved since the Auditor failed to conduct the audit in accordance with the SAs as explained in paragraphs **C.1 to C.7** above but falsely reported in their audit report that the audit was conducted as per SAs.

f) M/s Dhiraj & Dheeraj, CA Piyush Patni and CA Pawan Kumar Gupta committed professional misconduct as defined by Section 132 (4) of the Companies Act, 2013, read with Section 22 and Clause 8 of Part I of the First Schedule of the Chartered

Accountants Act, 1949 (No. 38 of 1949) as amended from time to time, which states that a CA is guilty of professional misconduct when he "fails to communicate with outgoing auditor".

This charge is proved since the Auditor failed to accept the audit in accordance with the law as explained in paragraphs **C.1** above.

56) Therefore, we conclude that the charges of professional misconduct in the SCN, as detailed above, are established based on the evidence in the Audit File, the audit reports on the standalone financial statements for the FY 2018-19 dated 13th August 2019 and the submissions made by the Auditor, and the Annual Report of Reliance Home Finance Limited for the FY 2018-19.

E. PENALTY AND SANCTIONS

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

58) As per the financial statements, RHFL's total assets were ₹18,100 crore and total external liabilities were around ₹16,300 crore as of 31.03.2019. The external liabilities included a debt of over ₹14,800 crore, in the form of debentures, borrowings from banks, commercial papers etc. Given the high degree of public interest in this listed entity, it was the duty of the Auditor to conduct the audit with the highest level of professional skepticism and due diligence and report their opinion in an unbiased manner. Despite the resignation of the previous auditor and a reporting of suspected fraud, the Auditor failed to conduct the audit as per standards on auditing. The major lapses started from the acceptance of the initial appointment of Dhiraj & Dheeraj as statutory auditors and continued throughout the audit of loans, going concern evaluation, risk assessment and reporting. The Auditor did not conduct the audit as per professional standards. The material misstatements in the financial statements due to inadequate provision, unjustified valuation of loans and irrational business practices were concurred by the Auditor in disregard of their responsibilities under the Act and SAs. The deficiencies in the audit resulted in rendering the audit opinion unreliable as the material misstatements in the financial statements assertions remain unreported. The Auditors also demonstrated a lack of professionalism by rationalising the actions of the Company, inappropriately evaluating the work of the previous auditor, and ignoring the fundamentals of auditing. Such actions of the Auditors necessitate stricter sanctions and penalties taking into account the letter and spirit of the law.

59) Because professional misconduct has been proved and considering the nature of violations and principles of proportionality, we, in the exercise of powers under Section 132 (4) (c) of the Companies Act, 2013, order:

a. Imposition of a monetary penalty of Rupees One crore on the Audit Firm M/s Dhiraj & Dheeraj.
b. Imposition of monetary penalties of ₹50,00,000/- (Rupees Fifty Lakh) and ₹10,00,000/- (Rupees Ten Lakh) respectively on CA Piyush Patni (EP) and CA Pawan Kumar Gupta (EQCR).
c. In addition, EP and EQCR partners are debarred for five years and three years respectively 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.

60) This order will become effective after 30 days from the date of issue of this order.

Sd/-
(Dr Ajay Bhushan Prasad Pandey)
Chairperson

Sd/-
(Dr Praveen Kumar Tiwari)
Full-Time Member

Sd/-
(Smita Jhingran)
Full-Time Member

Authorised for issue by the National Financial Reporting Authority.

Date: 26.04.2024
Place: New Delhi

(Vidhu Sood)
Secretary

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

To,

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Membership No. 143869

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Copy To: -

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