भारतीय सनदी लेखाकार संस्थान
(संसदीय अधिनियम द्वारा स्थापित)
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
(Set up by an Act of Parliament)

PR-255/2013-DD/251/2013/DC/675/2017

**[DISCIPLINARY COMMITTEE [BENCH-II (2024-2025)]**
**[Constituted under Section 21B of the Chartered Accountants Act, 1949]**

**ORDER UNDER SECTION 21B (3) OF THE CHARTERED ACCOUNTANTS ACT, 1949 READ WITH RULE 19(1) OF THE CHARTERED ACCOUNTANTS (PROCEDURE OF INVESTIGATIONS OF PROFESSIONAL AND OTHER MISCONDUCT AND CONDUCT OF CASES) RULES, 2007**

**[PR-255/2013-DD/251/2013/DC/675/2017]**

**In the matter of:**
**Shri Arun Dalmia,**
**Secretary, NSEL Investor Forum,**
Technocraft House,
A-25, MIDC Industrial Area,
Road No. 3, Opp. ESIC Hospital,
Andheri (East)
**Mumbai-400093.** **.....Complainant**

**Versus**

**CA. Shrawan Bhagwati Jalan (M. No. 102102) and**
**CA. Amit Kabra (M. No. 094533),**
**M/s S V Ghatalia and Associates (FRN 103162W),**
14th Floor, The Ruby,
29, Senapati Bapat Marg,
Dadar (West)
**Mumbai-400028.** **.....Respondent(s)**

**Members Present:-**
**CA. Ranjeet Kumar Agarwal, Presiding Officer (in person)**
**Mrs. Rani S. Nair, IRS (Retd.), Government Nominee (through VC)**
**Shri Arun Kumar, IAS (Retd.), Government Nominee (through VC)**
**CA. Sanjay Kumar Agarwal, Member (in person)**
**CA. Cotha S Srinivas, Member (in person)**

**Date of Hearing : 28th March 2024**
**Date of Order : 11th July 2024**

1. That vide Findings under Rule 18(17) of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007, the Disciplinary Committee was, inter-alia, of the opinion that **CA. Shrawan Bhagwati Jalan (M. No.**

**102102) and CA. Amit Kabra (M. No. 094533)** (hereinafter referred to as the '**Respondent(s)**') are **GUILTY** of Professional Misconduct falling within the meaning of Item (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949.

2. That pursuant to the said Findings, an action under Section 21B(3) of the Chartered Accountants (Amendment) Act, 2006 was contemplated against the Respondent(s) and a communication was addressed to them thereby granting opportunity of being heard in person / through video conferencing and to make representation before the Committee on 28th March 2024.

3. The Committee noted that on the date of the hearing held on 28th March 2024, the Respondent(s) were present in person and made their verbal representation on the Findings of the Disciplinary Committee, inter-alia, stating that, that their professional reputation and professional work has suffered a lot as the case was going on since long time. The true and fair view of the financial statements of the Company for FY 2011-12 was not actually vitiated because of the Audit Opinion. The financial position of the Company was not affected by the alleged enhanced disclosures. The regulatory Show cause notices were never brought to their notice. On being asked in the meeting with the Management also, the Management gave a representation that they did not receive any regulatory communication to that effect. To that extent, they were victims of fraud or wrong information given to them by the management. They had no reason to doubt the credibility of the CEO or CFO at that point in time. There were no complaints from any of the purchasers. There was nothing in the bye-laws of the Company which suggested that how the margin money should be invested. More importantly, none of the money which was held as margin money in respect of the Settlement Fund had gone missing. There was no financial loss.

3.1 The Committee also noted that the Respondent(s) in their written representation on the Findings of the Committee, inter-alia, stated as under:

a. In September 2013 i.e., 18 months after the end of the last year audited by the Respondent(s) and 15 months after the subject Audit report had been issued, the management of National Spot Exchange Limited (NSEL) itself identified issues pertaining to the subsequent year i.e. FY 2012-13, that led to the withdrawal of audit reports by the then statutory auditors of both National Spot Exchange Limited (NSEL) and Financial Technologies India Limited (FTIL) (i.e. the parent company of National Spot Exchange Limited), being M/s Mukesh P. Shah & Co, and Deloitte Haskins & Sells LLP respectively. As is clear from the audit report for the year ended 31st March 2014, which explains the circumstances leading up to the withdrawal of the audit reports of Financial Technologies India Limited (FTIL) and National Spot Exchange Limited (NSEL), none of the issues identified related to the financial year ended 31st March 2012. In respect of FY 2011-12, the auditor's report for Financial Technologies India Limited (FTIL) was not withdrawn.

b. The financial statements of FY 2012-13 (i.e. the year in respect of which financial irregularities were noticed by the Company, and accordingly the audit reports withdrawn) were audited by M/s Mukesh P. Shah & Co., who was earlier the internal auditor of NSEL and had issued a clean audit report. It was only when the Company issued letters in September 2013, regarding discrepancies in its financial statements for FY 2012-13, that CA. Mukesh P. Shah withdrew his report.

c. The Director (Discipline) in his Prima Facie Opinion and the Disciplinary Committee in its Findings have relied upon a media report which was published on 3rd October 2012. The said media report is dated 5 months after the Respondent CA. Amit Kabra signed the audit report (for FY 2011-12), and within the period audited by CA. Mukesh P. Shah i.e. in FY 2012-13. Despite the media reports being in the public domain within the period audited by CA. Mukesh P. Shah, he expressed no apprehension in his audit report in respect of the financial statements, internal controls, fraud reporting etc. Despite the stark difference in circumstances where CA. Mukesh P. Shah actually had the benefit of such media reports within the year which he audited, CA. Mukesh P. Shah has been exonerated for 12 of 15 charges, whereas the Respondent(s) have been held guilty in many of such charges.

d. The Respondent(s) had also explained that they carried out appropriate audit procedures subsequent to the year-end (at paragraph 1.1.5 of submission dated 8 February 2023), which have been completely ignored in arriving at the Findings.

e. At no stage in the proceedings did the Disciplinary Committee ask the Respondent(s) to defend on the allegations other than those where Prima facie guilty- Findings were made in the Prima Facie Opinion.

f. With respect to Charge 1 of the Findings, the Respondent(s) stated that this was not the charge in the Prima Facie Opinion. Accordingly, this was not argued against, nor did the Hon'ble Bench ask the Respondent(s) to address this issue.

g. With respect to Charge 2 of the Findings, the Respondent(s) stated that CA. Mukesh P. Shah has not been charged with this allegation despite the facts and requirements of audit being similar in the subsequent year as regards verification of third-party inventory. There is nothing that even remotely suggests or supports that there was a shortfall in the inventory in the F.Y. 2011-12. The Audit procedures carried out were also detailed in the Written Submissions filed by the Respondent(s). However, the Disciplinary Committee completely ignored all the submissions made and the audit procedures highlighted by the Respondent(s).

h. With respect to the specific Settlement Guarantee Fund disclosure related allegations, the Respondent(s) stated that the Findings have failed to consider and address the detailed submissions of the Respondent(s).

i. With respect to Charge 4 of the Findings, the Disciplinary Committee did not provide an evidence or support to demonstrate how the failure to obtain insurance (beyond what the client had) created a reportable financial misstatement which the auditor failed to report upon. In the subsequent year (F.Y. 2012-13), the circumstances and the Company's position regarding quantum of insurance taken in respect of goods owned by third parties was similar to the year in which the Respondent(s) were the auditor (F.Y. 2011-12). Despite the similar circumstances in both the years, CA. Mukesh P. Shah has been exonerated in this matter, whereas, the Respondent(s) have been charged for the Company's "under-insurance". This Charge 4 has been made in the context of under insurance of the goods lying at the warehouses despite an express acknowledgment by the Director(Discipline) that "*liabilities attached to ownership continued to be with buyer/seller of commodities as a result of which there were no contingent liabilities that were required to be disclosed but were not disclosed*", which has not been controverted by the Disciplinary Committee.

j. With respect to Charge 5 of the Findings, the Respondent(s) stated that under-insurance was never a basis for the charge, nor was it raised during the proceedings. There being no substantial change in the internal control system of the Company between FY 2011-12 and FY 2012-13, this charge has not been levied on CA. Mukesh P. Shah.

k. With respect to Charge 6 of the Findings, the Respondent(s) stated that the Director (Discipline) had dropped the allegations in the complaint in respect of this matter and held that the Respondent(s) are not guilty. At the Hearing before this Disciplinary Committee, the Respondent(s) were held not guilty in respect of this charge, as the transcripts (page 33 of transcripts of hearing dated 25 July 2023) records as follows:

> *"Presiding Officer: Charge 7, whether you have been already discharged?*
> *Counsel for Respondent: Yes, your honour. Presiding Officer: Okay, charge 8."*

In fact, no further discussion on this charge occurred nor were any arguments sought by the Hon'ble Bench.

l. With respect to Charge 6 of the Findings, the Respondent(s) also raised a plea mentioning about the violation of Rule 9(3) of the CA Rules 2007 stating that this matter has not been placed before the Board of Discipline for their perusal and has instead been directly placed before the Disciplinary Committee by circumventing the authority and power of the Board of Discipline.

m. The Appellate Authority is currently not quorate and functional. There is no reason or basis not to defer the proceedings till such time that the Respondent(s) can avail their statutory remedies against any Order passed under Section 21B of the CA Act i.e. to seek the appellate remedy before the Appellate Authority. Such an approach would also be consistent with an Order passed by the Delhi High Court in similar circumstances. Thus, the Respondent requested the Committee not to pass any Orders till the Appellate Authority is functional, as they will not have

the ability to pursue their statutory right of appeal provided in the Chartered Accountants Act 1949.

4. The Committee considered the reasoning as contained in the Findings holding the Respondent(s) Guilty of Professional Misconduct vis-à-vis written and verbal representation of the Respondent. On consideration of the representation of the Respondent(s), the Committee noted that the primary grudge of the Respondent(s) is with respect to the following four issues:

(a) They have been held guilty in respect of charges for which another member against whom disciplinary proceedings had been initiated in respect of the same entity for a different financial year has been held Not Guilty at Prima Facie Opinion stage itself (i.e. charge no. 2,4,5 and 7 of the Findings)

(b) They have been held guilty in respect of the charge for which the Respondent had been held Not Guilty by the Director (Discipline) (i.e. charge 6 of the Findings)

(c) They have been held guilty for charges which were not there in the Prima Facie Opinion.

(d) To defer the consideration of their case for award of punishment since the Appellate Authority is non-functional.

5. Before deciding on the quantum of punishment to be awarded to the Respondent(s), the Committee considered the aforesaid four objections of the Respondent(s) and opined as under:

5.1 With respect to the first issue regarding comparing the instant case with an earlier decided case in respect of the same entity for a different financial year, the Committee opined that comparing two distinct disciplinary cases as *'eye to eye'*, is not warranted as each case is decided on merits on the basis of due consideration of all the facts, documents and submissions on record.

5.2 As regard the second issue which is in respect to Charge 6 of the Findings (i.e. non-disclosure of outstanding contracts i.e. contingent liabilities and commitments), wherein the Disciplinary Committee did not agree with the not-guilty opinion of the Director(Discipline) and held the Respondent Guilty for the same, the Committee noted that the Director(Discipline) in his Prima Facie Opinion in respect of 8 allegations opined as under:

| S.No. | Allegations | Prima Facie View of Director (Discipline) |
|---|---|---|
| 1. | Wrong mentioning of Nature of Stock exchange | **Held Guilty** |
| 2. | AS-9 not followed for warehouse receipts | **Held Guilty** |
| 3. | Deviation of amount from Settlement guarantee Fund | **Held Guilty** |

| | | |
|---|---|---|
| 4. | Short Insurance | **Held Guilty** |
| 5. | Lack of proper internal control procedures not reported | **Held Guilty** |
| 6. | Failed to disclose the details in financial statements as per AS-18 | Held Not Guilty |
| 7. | Non-disclosure of Contingent Liability and commitments | Held Not Guilty |
| 8. | As per Auditor's Report point no. XXI, the Respondents reported that no fraud on or by the Company is noticed despite that NSEL has defaulted in payment to its investors and also commodities were not physically available which resulted in fraud perpetrated by the Company and gross negligence on the part of the auditor of the Company. | **Held Guilty** |

5.3 The Committee noted that the Director (Discipline) in terms of Rule 9 of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007, held the Respondent(s) Prima-facie Guilty of Professional Misconduct falling within the meaning of Item (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949. Accordingly, in terms of the provisions of Rule 9(2)(a)(ii)) of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007 the Prima Facie Opinion of the Director(Discipline) was placed before the Disciplinary Committee. The Disciplinary Committee on consideration of the same opined as under:

*"The Committee on consideration of the same concurred with the reasons given against the charge (s) and thus, agreed with the prima facie opinion of the Director that the Respondent(s ) are Guilty of Professional Misconduct falling within the meaning of Clauses (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act 1949 except for the reasoning as regard the charge raised in para 1.7 of the complaint and dealt in para 17.21 to 17.28 of the said Prima facie opinion. It was viewed that the allegation dealt in the said paras pertains to the matter which was the very basis of NSEL Scam. Moreover, the Committee decided that the requirement of AS-29 vis-à-vis disclosures made in the extant case needs to be further investigated taking into consideration the nature of contracts entered into and stock taken against them together with the byelaws governing them. The Committee accordingly did not agree with the views of Director (Discipline) that no disclosures were required and hence decided to refer the said Charge for further enquiry."*

5.4 Accordingly, the Committee decided to proceed further under Chapter V of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of

Cases) Rules, 2007. Thus, the Committee noted that out of 8 allegations in the Prima Facie Opinion, the instant case had been referred for enquiry in respect of the following 7 charges:

| S.No. | Charges |
|---|---|
| 1. | Wrong mentioning of Nature of Stock exchange |
| 2. | AS-9 not followed for warehouse receipts |
| 3. | Deviation of amount from Settlement guarantee Fund |
| 4. | Short Insurance |
| 5. | Lack of proper internal control procedures not reported |
| 6. | Non- disclosure of Contingent Liability and commitments |
| 7. | As per Auditor's Report point no. XXI, the Respondents reported that no fraud on or by the Company is noticed despite that NSEL has defaulted in payment to its investors and also commodities were not physically available which resulted in fraud perpetrated by the Company and gross negligence on the part of the auditor of the Company. |

5.5 The Committee further noted that the Respondent(s) in their written submissions dated 12th January 2018 on the Prima Facie Opinion with respect to the instant charge of non-disclosure of outstanding contracts as contingent liability and commitment pointed out that the matter should have been dealt in terms of the provisions of Rule 9(3) of the aforesaid Rules which provides as under:

*"Where the Director in of the prima facie opinion that the member or the firm is not guilty of any misconduct either under the First Schedule or the Second Schedule, he shall place the matter before the Board of Discipline, and the Board of Discipline-*

*(a)* .....

*(b) If it disagrees with such opinion of the Director, then it may either proceed under chapter IV of these rules, if the matter pertains to First Schedule, or refer the matter to the Committee to proceed under Chapter V of these Rules, if the matter pertains to the Second Schedule or both the Schedules or may advise the Director to further investigate the matter."*

5.6 In this regard, the Committee noted that the (erstwhile) Disciplinary Committee had agreed with the substantial/majority charges/allegations of the Director(Discipline) wherein guilty opinion was given in the Prima Facie Opinion and accordingly, proceeded further under Chapter V of the aforesaid Rules. While doing so, the not-guilty opinion of the Director (Discipline) in respect of one of the allegations was not accepted.

5.7 The Committee noted that it is the case of the Respondent(s) that in respect of 'Not Guilty' charges, it was only the Board of Discipline which had the power to consider the same. However, the Committee was of the view that the Chartered Accountants Act 1949 and the Rules framed thereunder provide for the consideration of the Prima Facie Opinion *in toto* and not on piecemeal charge-wise basis.

5.8 Further, there is sufficient documents/information available on record on the basis of which the Disciplinary Committee did not accept the not-guilty opinion of the Director (Discipline) in respect of one of the allegations and proceeded further in the matter. Detailed reasons, to this effect, were also provided to the Respondent(s) vide letter dated 17th November 2017 when the decision of the Disciplinary Committee on the Prima Facie Opinion of the Director(Discipline) was communicated to them. Further, the Respondent(s) in their written submissions dated 12th January 2018 on the Prima Facie Opinion also reiterated their response made vide their earlier written submissions dated 14th January 2013 at the Prima Facie Opinion stage in respect of the said charge which had been duly considered by the Committee before arriving at its Findings in respect of the said charge as referred to in para 30 of its Findings.

5.9 The Committee also noted that the case was listed for hearing on 15 occasions. During the course of fifteenth and final hearing held on 25th July 2023, the Respondent(s) were specifically asked by the Committee with respect to this charge as to whether they have been already discharged to which the counsel for the Respondent(s) answered in affirmative. The Committee was of the view that it is incumbent upon the parties to the case to bring correct facts before the Committee and thus, it was upon the Respondent(s) also to specifically bring to the notice of the Committee that the said charge had been referred for enquiry.

5.9.1 The Committee also specifically informed the Respondent(s) during the said hearing that since one of their claim in earlier hearing was that they had not been given natural justice as without asking them anything, the Opinion had been given by the Director(Discipline), they were given the opportunity to submit the document in their defence by the Committee which were duly considered by the Committee.

5.10 Thus, the Committee was of the view that the Respondent(s) at a later stage is estopped from pleading that due opportunity to defend their case was not provided to them and that no prejudice was caused to them.

5.11 The Committee was also of the view that apart from this charge, even otherwise also, the Respondent(s) had been held Guilty for various other charges of Professional misconduct in the instant case by the Committee.

5.12 As regard the third issue, the Committee held that it has arrived at its Findings holding the Respondent(s) guilty in respect of the charge alleged against them in Form 'I' only for which due

opportunity to defend their case was provided to the Respondent(s) in 15 hearing(s) when the case was listed for enquiry before it.

5.13 As regards the fourth issue, the Committee noted that the Respondent(s) referred to a decision dated 14th March 2023 of the **Hon'ble High Court of Delhi in Vijaykant Jagannath Kulkarni V.S. Disciplinary Committee, The ICAI and Ors. (W.P. (C) 1887 of 2023)** as a basis of their request to defer the Committee's decision to pass Orders under Section 21B(3) of the Chartered Accountants Act 1949. The Committee referred to the following contents of the said Order: -

> *"17. The Disciplinary Committee has at this stage passed an order holding the Petitioner guilty of professional misconduct. However, the final decision as to what action needs to be taken against the Petitioner is yet to be determined by the Disciplinary Committee. Under Section 21B(5), the Disciplinary Committee is to afford a proper hearing to the Petitioner and only thereafter proceed to take action. Such an order under Section 21B (5) is clearly appealable to the Authority.....*
>
> *18..... in the unique facts and circumstances of this case, the following directions are issued:-*
>
> ***i) The Petitioner shall appear before the Disciplinary Committee and make his submissions in respect of the action under Section 21B (5).***
> ***ii) A final order passed by the Disciplinary Committee shall be communicated to the Petitioner.***
> ***iii) The Petitioner would be entitled to approach the Appellate Authority under Section 22G both in respect of the Order dated 6th January, 2023 and the final Order to be passed by the Disciplinary Committee. For a period of eight weeks, the final Order that may be passed would not be given effect to in order to enable the Petitioner to approach the Appellate Authority under Section 22G.(emphasis provided)"***

5.14 Thus, the Committee held that even the Hon'ble Delhi High Court has not estopped the Disciplinary Committee from continuing with its proceedings in the case on the ground under consideration before it. Accordingly, the Committee was of the view that it is well within its right to consider the case of the Respondent(s) for award of punishment.

6. Thus, keeping in view the facts and circumstances of the case, material on record including verbal and written representation on the Findings, the Committee in respect of the following charge(s) was of the following view:

(a) First Charge: The Respondent(s) failed to bring on record documentary evidence to show that the Company (NSEL) was a regulated entity and had taken any permission to do the business of

spot exchange from any Government Authority / Agency. The Company was dealing with various persons, including stockbrokers, sub-brokers, Godown owners, bankers, and the general public, and taking margin money from them as well. Moreover, it was providing the service of spot exchange PAN India without involvement of any Government agency that can control the business activity of the Company to obtain robustness, safety and resilience in the activities conducted by them. The Respondent(s) gave the reference of notification issued by Department of Consumer Affairs (DCA) dated 6th February 2012 wherein Department of Consumer Affairs (DCA) appointed the Forward Markets Commission, Mumbai (FMC) as designated agency to which all information or returns relating to the trade shall be provided. Hence, Forward Markets Commission, Mumbai (FMC) will be the regulator for all future commodity exchanges in India. Thus, it shows that the Department of Consumer Affairs (DCA) is regulating the NSEL and the same is also in the knowledge of the Respondent(s) as they themselves have informed about the same. Also, the date of issue of said Notification is before the date of signing of financial statement. However, the Respondent(s) have not considered the same. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 25.4 to Para 25.6 of the Findings dated 7th February 2024 with respect to the first charge– page 42 to page 43 of the Findings)

(b) Second Charge: As per the Guidance Note on Audit of Inventories, an auditor is required to physically verify the inventory at client's place and should also obtain third party confirmations for whom the entity is holding significant amount of stock. However, in the instant case, the Respondent(s) have not verified the stocks lying at client's place simply taking the excuse that the stock is of third party. The Respondent(s) relied on the management representation that the parties whose stocks are lying with NSEL has conducted their check and failed to provide any evidence that whether they performed any counter check on the said inventory. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 26.2 of the Findings dated 7th February 2024 with respect to the second charge– page 44 to page 46 of the Findings)

(c) Third Charge: From the bye laws of NSEL, the Committee noted that it was clear that there is a requirement for maintaining a settlement Guarantee Fund in respect of different commodity segments of the Exchange for such purposes, as may be prescribed by the relevant Authority from time to time. Further, the amount of the deposit or contribution to be made by each member to the relevant Settlement Guarantee Fund is specified by the relevant Authority and the minimum amount in Settlement Guarantee Fund should not be less than Rs. 1 crore which may be increased. However, the amount maintained in Settlement Guarantee Fund is less than the specified amount. The Company invested the amount of Rs. 360.60 crores (approx.) in loans and advances, procurement advances, etc. which is not allowed as per byelaws. Although, the Respondent(s) obtained the 100% confirmation from the parties to whom the advances were given but since it was against the provisions, hence it was the duty of the Respondent(s) to report the same in their Audit report. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 27.2 of the Findings dated 7th February 2024 with respect to the third charge– page 47 to page 51 of the Findings)

(d) Fourth Charge: NSEL offered services like warehousing and collateral management services to market participants and market participants are doing transactions depending upon NSEL as they have confidence on them. The Committee further noted that NSEL has not taken insurance cover of the commodities lying at its warehouse amounting to Rs. 1000 crores to Rs. 1500 crores. However, the dependency of market participants casts responsibility on NSEL to take care of the goods of its clients and there should be an insurance cover upto a certain limit. On a combined reading of the requirement of para 11 of SA 315 with the defence provided by the Respondent(s), it is clear that the Respondent(s) have not spelt out whether any analysis of the business risks was undertaken by them and if so, their assessment of the same and its impact on the financial statement of the Company. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 28.2 of the Findings dated 7th February 2024 with respect to the fourth charge– page 52 to page 54 of the Findings)

(e) Fifth Charge: The Committee noted that the sample size selected by the Respondent(s) were not as per the relevant standard on auditing. Also, the samples selected by them were neither representative of the characteristics of whole population nor sufficient to reduce the sampling risk to an acceptably low level. They failed to point out any discrepancies in the financial statements even after perusing the internal audit report wherein various discrepancies are pointed out and issued a clean audit report. Looking into the irregularities pointed out by the Internal Auditor and NSEL Investors Forum, the Committee noted that the Respondent(s)' selection of sample was not enough to cover the whole relevant population to point out any single discrepancies regarding the operations of the Company.

(f) It was noted that if the Respondent(s) had employed appropriate procedures to obtain reasonable assurances about the sufficiency and efficiency of internal control system in place, they would have come to know that internal control procedure/system was not commensurate with the size and nature of the business. Further, the Respondent(s) failed to obtain sufficient information necessary for expression of an opinion as per reporting requirement under Para 4 (iv) of Appendix-I of CARO, 2003. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 29.2 of the Findings dated 7th February 2024 with respect to the fifth charge– page 55 to page 59 of the Findings)

(g) Sixth Charge: The Committee noted that as per byelaws of NSEL, if on an investigation the exchange concludes that any transactions executed are found to be in a fraudulent manner, the relevant Authority of the exchange have absolute authority and discretion to withdraw itself as a legal counter party to any transaction after giving an opportunity of being heard to all the parties affected by the decision and NSEL is required to disclose as regards the value of contracts outstanding for which the exchange shall act as a legal counter party and the transactions which may be excluded from the purposes. However, it is seen that no such disclosure is made. Also, the Respondent(s) have not denied that the NSEL is not a counter party to the transactions held.

(h) The Committee further noted that Department of Consumer Affairs (DCA) in exercise of powers conferred to it under section 27 of the FCRA vide notification no. S. O. 906(E) dated 5th June 2007 had exempted all forward contracts of one day duration for the sale and purchase of commodities traded on the NSEL, from operation of the provisions of the said Act. However, after analyzing the trade data received from NSEL, the Forward Markets Commission(FMC) identified issues relating to contracts traded on NSEL and sought clarifications from NSEL on 22 February 2012. The FMC requested the DCA to take necessary action regarding the above violations. DCA vide its letter dated 27 April 2012 directed NSEL to explain as to why action should not be initiated against them for violation of the conditions of the notification dated 5th June 2007.

(i) In response to the above, NSEL submitted a reply vide their letter dated 29 May, 2012 and after that DCA vide its letter dated 31st May, 2012, sought comments of the Commission on the NSEL letter dated 29 May, 2012. Thus from the above it is seen that some initial proceedings were on going against NSEL before the date of signing of financial statements by the Respondent(s) i.e. 21st May, 2012 which is impacting the financial position of the Company and has to be shown as contingent liability in financial statements as per paragraph 8.8.7 of the Guidance Note on the revised Schedule VI. However, the Respondent(s) did not care to disclose the same in their audit report for the period despite having knowledge of the same. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 30.3 of the Findings dated 7th February 2024 with respect to the sixth charge– page 60 to page 63 of the Findings)

(j) Seventh Charge: On perusal of the DCA notification, the Committee observed that in early 2012, the FMC was appointed as 'designated agency' to collect data from NSEL and protect investors' interest. On 27th April 2012, based on the data provided by the Forward Markets Commission (India), the Ministry of Consumer affairs issued a show cause notice to NSEL that it was violating the conditions of 2007 exemption like 'no short sale', 'no stock verification mechanism' and ' conducting trades beyond 11 days'. The newspapers reports are treated as hearsay evidence, yet, looking into the fact that Show cause notice had been issued to NSEL as early as in April 2012 and the audit report had been signed by the Respondent(s) on 21st May, 2012 and the Respondent(s) have not brought on record any documentary evidence to show the checks carried out by them after the Balance Sheet date to counter such claims being made in the newspaper reports. Thus, there were sufficient reasons to raise suspicion in the mind of the Respondent(s) so as to thoroughly check/investigate into the affairs of NSEL before signing their report for the Financial Year 2011-12. However, the Respondent(s) relied on management's representation letter that no fraud is noticed and chose not to report in their Audit report about the on-going fraud. (The misconduct on the part of the Respondent(s) has been dealt in detail in Para 31.2 of the Findings dated 7th February 2024 with respect to the seventh charge– page 65 to page 66 of the Findings)

6.1 Accordingly, the Committee noted that in the extant case, the auditor has neither applied his professional judgment while giving his opinion on true and fair view of the financial statements of the Company nor complied with the requirements of the Standard on Auditing (SAs) including SA

240 wherein he must plan and perform his audit procedures to address the risk of material misstatement due to fraud as well as SA 500 which requires that the auditor should obtain sufficient appropriate evidence to able to draw reasonable conclusions on which the audit opinion is formed.

6.2 Hence, professional misconduct on the part of the Respondent(s) is clearly established as spelt out in the Committee's Findings dated 7th February 2024 which is to be read in consonance with the instant Order being passed in the case.

7. Accordingly, the Committee was of the view that ends of justice will be met if punishment is given to them in commensurate with their professional misconduct.

**8. Thus, the Committee ordered that the name of Respondent(s) i.e. CA. Shrawan Bhagwati Jalan (M. No. 102102) and CA. Amit Kabra (M.No.094533) be removed from the Register of members for a period of 01(One) year which shall run concurrently with the punishment awarded in case no. PR/281/2013-DD/273/2013-DC/437/2016.**

**sd/-**
**(CA. RANJEET KUMAR AGARWAL)**
**PRESIDING OFFICER**

**sd/-**
**(MRS. RANI S. NAIR, IRS RETD.)**
**GOVERNMENT NOMINEE**

**sd/-**
**(SHRI ARUN KUMAR, IAS RETD.)**
**GOVERNMENT NOMINEE**

**sd/-**
**(CA. SANJAY KUMAR AGARWAL)**
**MEMBER**

**sd/-**
**(CA. COTHA S SRINIVAS)**
**MEMBER**

सही प्रतिलिपि होने के लिए प्रमाणित
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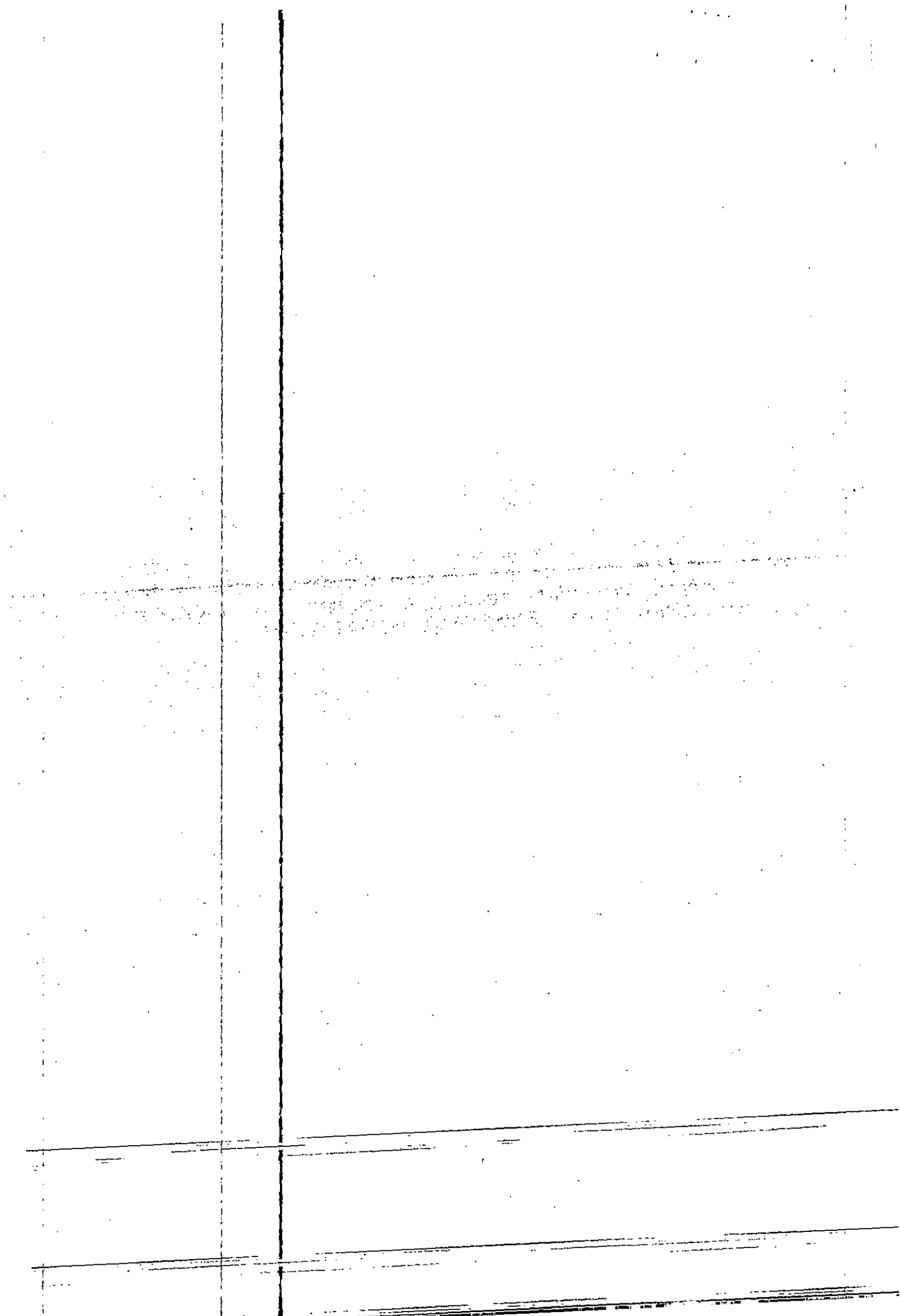
सीए श्रुति गर्ग / CA. Shruti Garg
सहायक निदेशक / Assistant Director
अनुशासनात्मक निदेशालय / Disciplinary Directorate
इंस्टिट्यूट ऑफ चार्टर्ड एकाउंटेंट्स ऑफ इंडिया
The Institute of Chartered Accountants of India



**CONFIDENTIAL**

**DISCIPLINARY COMMITTEE [BENCH – II (2023-2024)]**

**[Constituted under Section 21B of the Chartered Accountants Act, 1949]**

**Findings under Rule 18(17) of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007.**

**File No.: [PR-255/2013-DD/251/2013/DC/675/2017]**

**In the matter of:**

**Shri Arun Dalmia,**
**Secretary, NSEL Investor Forum,**
Technocraft House,
A-25, MIDC Industrial Area,
Road No. 3, Opp. ESIC Hospital,
Andheri (East)
Mumbai-400 093 **.....Complainant**

**Versus**

**CA. Shrawan Bhagwati Jalan (M. No. 102102) and**
**CA. Amit Kabra (M. No. 094533),**
**M/s S V Ghatalia and Associates (FRN 103162W),**
14th Floor, The Ruby,
29, Senapati Bapat Marg,
Dadar (West)
Mumbai-400 028 **.....Respondents**

**MEMBERS PRESENT:** (In person)

**CA Ranjeet Kumar Agarwal, Presiding Officer**
**Mrs. Rani Nair, I.R.S. (Retd.), Government Nominee**
**Shri Arun Kumar, I.A.S. (Retd.), Government Nominee**
**CA. Sanjay Kumar Agarwal, Member**
**CA. Sridhar Muppala, Member**

| | | |
|---|---|---|
| **DATE OF FINAL HEARING** | : | 25.07.2023 |
| **DATE OF DECISION TAKEN** | : | 25.08.2023 |

## PARTIES PRESENT DURING FINAL HEARING

**Complainant** : Not Present

**Respondents** : CA Shrawan Bhagwati Jalan (Through Video Conferencing Mode)

: CA Amit Kabra (Through Video Conferencing Mode)

**Counsel for Respondents:** CA Ajay Bahl along with his assistant CA Ayush (Both through Video Conferencing Mode)

## BACKGROUND OF THE CASE

1. The brief background of the case is that the Respondents were the statutory auditors of National Spot Exchange Limited (NSEL) for the three financial years ended March 31, 2010, March 31, 2011 and March 31, 2012. Shri Arun Dalmia, Secretary of NSEL Investors Forum has filed a complaint against the Respondents on ground of professional misconduct/negligence in respect of reporting in financial statements of NSEL for the period ending 31st March, 2012 which resulted in a fraud of Rs. 5500 crores to the investors as alleged in the complaint.

It is noted that the statutory auditor of NSEL were as under:

| **nancial Year** | **atutory Auditor** |
|---|---|
| 11-12 | s S V Ghatalia and Associates |
| 12-13 | s Mukesh P. Shah and Co. |

*** M/s Mukesh P. Shah and Co were the internal auditors of NSEL for FY 2011-12 and had become statutory auditor in FY 2012-13. It is noted that on 21st September 2013, M/s Mukesh P. Shah and Co withdrew their audit report for FY 2012-13**

**CHARGES IN BRIEF: -**

2. The Complainant vide his complaint dated 5th October, 2013 levied the following allegations against the Respondents:

| S.No. | Allegations | Prima Facie View of Director (Discipline) |
|---|---|---|
| 1. | Wrong mentioning of Nature of Stock exchange | **Held Guilty** |
| 2. | AS-9 not followed for warehouse receipts | **Held Guilty** |
| 3. | Deviation of amount from Settlement guarantee Fund | **Held Guilty** |
| 4. | Short Insurance | **Held Guilty** |
| 5. | Lack of proper internal control procedures not reported | **Held Guilty** |
| 6. | Failed to disclose the details in financial statements as per AS-18 | Held Not Guilty |
| 7. | Non- disclosure of Contingent Liability and commitments | Held Not Guilty* |
| 8. | As per Auditor's Report point no. XXI, the Respondents reported that no fraud on or by the Company is noticed despite that NSEL has defaulted in payment to its investors and also commodities were not physically available which resulted in fraud perpetrated by the Company and gross negligence on the part of the auditor of the Company. | **Held Guilty** |

***The Committee at the time of consideration of Prima Facie Opinion decided to refer the said allegation for further enquiry.**

3. The Respondents at the stage of PFO had inter-alia submitted as under:

a. The Respondents were the statutory auditors of NSEL as of and for the three financial years ended March 31, 2010, March 31, 2011 and March 31, 2012.

b. That the allegations made by the complainants were not maintainable due to applicability of one or more of the following reasons:

i. Outside the purview of Respondents engagement

ii. Beyond the specific duties which auditors have to perform

iii. Based on hearsay and unsubstantiated reports

iv. Based on erroneous understanding of the role of statutory auditors

v. Clearly indicative of non-understanding of the technicalities and specific responsibilities of a statutory auditor relating to Accounting Standards and Auditing Standards.

vi. Based on wrong interpretation of the information and background of the issues involved.

vii. Aimed at eliciting more information by raising issues those are by themselves baseless and devoid of appropriate evidence

viii. Stated without a detailed reading and understanding of the provisions contained in the Bye laws of NSEL

c. The statements by any person or any witness adverse to our interest particularly, those made after the Respondents last audit period ending March 31, 2012, could not be relied upon without affording the Respondents an opportunity to cross examine such third party or witness on whose statement reliance is being sought to be placed. Even otherwise, the statement of Mr. Anjani Sinha (Ex-CEO of NSEL) could not be read and relied upon in the context of the responsibility of the auditors as there was no mention of the same in such a statement.

d. In judging whether the Respondents exercised reasonable care and skill as expected from an auditor, it will not be correct to proceed on matters which have transpired subsequent to the Respondents engagement as statutory auditors. On the contrary, such a test of reasonable care and skill must be made keeping in mind the situation and information available with the Respondents at the time the Respondents audited the accounts. In relying upon statements made by the management, the Respondents firm as auditors of NSEL exercised reasonable care and skill in all auditing procedures as

there were no apparent reasons to doubt the veracity of the representations made to the Respondents firm by the management at that time.

3.1 Response to Allegation 1- Wrong mentioning of Nature of Stock Exchange

a. National Spot Exchange Ltd. was incorporated on May 18, 2005 as a public limited company with Financial Technologies India Limited ("FTIL") holding 99.99% of the share capital and National Agricultural Cooperative Marketing Federation of India Limited ("NAFED") holding 100 shares (i.e. 0.01% of the share capital), NSEL is an electronic spot trading platform for commodities.

b. Pursuant to the Gazette Notification dated June 5, 2007 issued by the Ministry of Consumer Affairs, Food and Public Distribution, Government of India ("DCA") Central Government exempted all forwards contracts of one day duration for the sale and purchase of commodities traded on NSEL from operation of the provision of Forward Contracts (Regulation) Act 1952 ("FCRA") subject to certain conditions.

c. NSEL obtained licenses from State Governments of Maharashtra, Karnataka, Gujarat, Madhya Pradesh, Orissa and Rajasthan as marketing of notified agricultural produce requires approval from Directorate of Agricultural Marketing of respective State Government ("DAMSC").

d. Based on above, it can be noted that NSEL was organized as a spot exchange having received approvals from DCA and DAMSCs to allow its members for spot trading in commodities. For the fiscal years ended March 31, 2010 and 2011, it is stated in the notes to the financial statements that NSEL is a self-regulated exchange.

e. The Forward Markets Commission ("FMC") is a regulatory authority set up by the Government of India in accordance with the provisions of section 3 (1) of the FCRA to regulate and control the commodity futures market. Similarly, Securities and Exchange Board of India (SEBI), under its regulations Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 regulates stock exchanges in India.

f. As stated earlier, the notes to financial statements for the years ended March 31, 2010 and March 31, 2011 stated that NSEL was a self-regulated exchange. Self-regulation means setting up of its own rules and regulations by an entity in order for it to run its business activities.

g. In order to facilitate trading in commodities by its members, NSEL had launched various contracts on its platform. These contracts prescribed in detail, the procedures relating to trading, quality and assaying requirements, delivery and funds pay-in/pay-out etc. All these contracts are also available in the public domain, and are therefore available for reading by members of NSEL and non-members alike (including clients of members). The audit committee and the Board of Directors met to review the operating performance of NSEL. Hence, NSEL management in its financial statements for the years ended March 31, 2010 and 2011 had stated that NSEL was "self-regulated". These explanations were provided to us by management, to support their conclusion that NSEL was a "self-regulated exchange"

h. Gazette notification of June 5, 2007 gave powers to the DCA to designate any other agency to receive all information or returns relating to trade. By virtue of Gazette notification of February 6, 2012, DCA exercised this power and designated the FMC to receive all information or returns relating to trade. FMC is the regulator for all future commodity exchanges in India. Thus, for the year ended March 31, 2012 NSEL had changed from the status of a self-regulated exchange to regulated under FMC. Accordingly, NSEL was self-regulated until the February 6, 2012 notification at which time it became regulated by FMC.

3.2 Response to Allegation 2- AS-9 not followed for warehouse receipts

The Respondents while rebutting the charge mentioned that out of the income of Rs.11.46 crores, the warehouse receipt transfer ("WRT") charges income consists of Rs. 8.48 crores and the warehouse income consist of Rs.2.98 crores.

Further they have performed audit procedures to address recognition of income, which included the following:

a. Obtained on a sample basis, various contracts launched by NSEL and applicability of WRT and warehouse income.

b. Performed a review, on a sample basis, of underlying supporting documentation viz., for the purpose of recording WRT and warehousing income.

c. Obtained a schedule of WRT and warehousing income from management and re-calculated such income on the basis of rates given in the contracts.

d. Performed an overall analytical review of WRT income

3.3 Response to Allegation 3- Deviation of amount from Settlement Guarantee Fund

a. That notes to accounts Note 39 of financial statements of FY 2011-12 does not refer to Settlement Guarantee Fund ("SGF') but instead, to the Settlement Fund ("SF").

b. As at March 31, 2012, the Company had the following aggregate balances reported in the financial statements Rs.360.60 crores of balance in the settlement fund, comprising Rs.328.93 crores of cash margin balance, and Rs.31.67 crores of margin received from members in the form of fixed deposits and guarantees, included in Note 10, and referred to in Note 39 to the financial statements for the year ended March 31, 2012 and (d) Rs.0.65 crores of balance in Settlement Guarantee Fund, included in Note 10 and referred to in Note 35, to the financial statements for the year ended March 31, 2012.

c. SGF is created by way of allocation of a portion of margin amounts collected from members. The Bye-Laws clause 12.5 specifically prescribes manner in which the SGF can be invested. As per clause 12.5, Funds in the Settlement Guarantee Fund may be invested in such approved securities and/or other avenues of investments, as may be provided for by the Board in the relevant Business Rules and Regulations in force from time to time".

d. The Respondents noted that there was no predefined investment policy enshrined in NSEL's Bye-Laws and Rules. In the absence of any such specific guidelines on investment of margin balance, as at March 31, 2012 NSEL has invested cash margin balance in mutual fund of Rs. 161.73 crores, loans to subsidiary Rs. 55 crores, procurement advance of Rs. 94.85 crores (total procurement advance of Rs. 136 crores), and Rs. 18 crores in cash and bank balances and earned a total income of Rs. 21.62 crores in the financial year 2011-12, from such investments.

e. From the above, it can be seen that approx. 50% of the margin balance has been deployed in liquid mutual fund and the balance in temporary loans and advance to generate income. It is important to note that the Company had generated income by investing these funds, and not kept them idle.

3.4 Response to Allegation 4- Short Insurance

a. That the management is running the business, and different group of individuals have different strategies to run their business activities. It is up to the management to see how much risk they are willing to take to operate a business. It is not the responsibility of the statutory auditors of a Company, in the context of their audit of the financial statements, to report or comment on the business strategies of the Company. Therefore, the statutory auditors are not expected to and cannot, comment on business strategies of a Company.

b. That the complainants stated that "*It seems serious deficiency of under insurance, causing the serious risk to the Exchange as well as Investors*". This suggests that it is complainant's view that NSEL should have taken 100% risk coverage of the commodities lying in the warehouse. The allegation itself suggests that the complainants are not sure about it and hence has used the word "it seems". Even if it is the complainant's view, it is merely a presumption and is not supported by any evidence.

3.5 Response to Allegation 5- Lack of proper internal control procedures not reported

That they have performed the following procedures to check whether there is proper internal control system:

a. Obtained delivery marking report ("DMR) for a large member for the year ended March 31, 2012.

b. Randomly selected 50 invoices (over a period of 5 days) for trades done by a large member and quality control cum warehouse inward receipt.

c. For above invoices and DMR, traced entries into members' obligation and fund settlement into the bank statements;

d. Selected 22 days and traced entries into bank and bank statements for settlement of transactions for a large member's transactions;

e. Selected entries from top 5 members' margin accounts and traced entries into the bank statements.

f. Traced subsequent movement in initial margin accounts for top 5 members and verified that margin accounts are not used for settlement of trades;

g. Performed on a random basis, testing for a few samples, subsequent to settlements of trades;

h. Confirmation from the Agricultural Produce Market Committee ("APMC"), Kadi stating that contracts are delivery based contracts

i. Obtained direct confirmation for margin balance for top members;

j. Obtained direct confirmation for sell/purchase volume, transaction and delivery charges paid by a large member.

k. NSEL provided a written representation to Respondents's firm that stock lying at NSEL warehouse at March 31, 2012 were confirmed / acknowledged by members.

3.6 Response to Allegation 6- Failed to disclose the details in financial statements as per AS-18 (Related Party Transactions)

a. Notes 28 and 29 (including Annexure B) to the financial statements for the year ended March 31, 2012, deal with related party disclosures. As is

evident from the disclosures made in the financial statements, these cover the following aspects:

*i. the name of the transacting related party;*

*ii. a description of the relationship between the parties;*

*iii. a description of the nature of transaction;*

*iv. volume of transactions either as an amount or as an appropriate proportion;*

*v. the amounts or appropriate proportions of outstanding items pertaining to related parties at the balance sheet date and provisions for doubtful debts due from such parties at that date; and*

*vi. amounts written off or written back in the period in respect of debts due from or to related parties*

b. That the allegation is extremely generic, and does not specify what other element of the related party transactions is necessary for an understanding of the financial statements that has not been disclosed.

c. Based on the information and explanations provided to the Respondents, by the Company during the course of out audit, there was no other element of the related party transactions necessary for an understanding of the financial statements. In view of the foregoing, it is the Respondents submission that the Respondents have carried out the procedures required to be performed under auditing standards generally accepted in India, in relation to related party disclosures. Accordingly, we find the allegation, that "*This also reflects that the financial statements of the company do not reflect true and fair view of the affairs of the company as at balance sheet date as required u/s 209 and 211(3C) of the Companies Act, 1956.*" to be completely unfounded.

3.7 Response to Allegation 7- Non disclosure of Contingent Liability and commitments

a. The Respondents drew attention to the following extract of Clauses 3.7, 5.17, 5.21 and 5.26 and 7.9, 9.6, 12.14 from the Bye Laws of NSEL Based on combined reading of all of above Clauses, it can be noted that:

i. Exchange members are full responsible for closing out trade transactions and shall indemnify NSEL for any losses that are incurred on account of non-settlement or non-closure of transaction.

ii. NSEL does not guarantee the financial obligations of a defaulting clearing member to other members, who are doing clearing and settlement through them.

iii. NSEL does not guarantee financial obligation of any defaulting member or any other member or the delivery, the title, genuineness, quality or validity of any goods etc.

iv. NSEL's liability is limited to balance lying in settlement guarantee fund.

b. The Respondents also highlighted para no.8.8.7 of the Guidance Note on the revised Schedule VI. The Respondents also highlighted the following:

i. as represented to the Respondents during the course of his audits, there was no claim against the Company that was not acknowledged as debt, except to the extent, if any, disclosed in the financial statements.

ii. NSEL's eventual liability is only to the extent of balance lying in SGF which was disclosed in the notes to the financial statements.

iii. Having regard to the previous explanations, there are no other monies for which the Company is contingently liable.

iv. The transactions on the Exchange are not in relation to contracts on capital account

v. The transactions on the Exchange are not in relation to uncalled liability on shares or partly paid invests; and

vi. Having regard to the previous explanations, there are no commitments involved.

Accordingly, the question of disclosure either as a contingency or a commitment does not arise. Further no other exchange discloses total open positions as a

"Contingent Liability" in their financial statements. Since nothing is specified in GAAP on such matters, generally accepted practices of other entities operating in the same industry become accepted accounting and disclosure practices.

3.8 Response to Allegation 8- Reported that no fraud on or by the Company is noticed despite that NSEL has defaulted in payment to its investors and also commodities were not physically available which resulted in fraud

a. The Respondents wishes to submit that the allegation appeared to be based on facts known on or after August, 2013, which was well after the Respondents audit report dated May 2012. The Respondents can only be expected to consider events upto the date of the Respondents's auditor's report, under SA-560 –"Subsequent Events"

b. The Respondents drew attention to Paragraph 4 (xxi) of CARO which required the auditor to report on

*"Whether any fraud on or by the Company has been noticed or reported during the year. If yes, the nature and the amount involved is to be indicated".*

In this connection, the Respondents drew reference to paragraph 77(a) of the Statement on the Companies (Auditor's Report) Order 2003, issued by the ICAI, which stated

*"The scope of auditor's inquiry under this clause is restricted to frauds, noticed or reported' during the year. The use of the words* ***"noticed or reported" indicates that the management of the company should have the knowledge about the frauds",*** *(emphasis supplied) on the Company or by the Company that have occurred during the period covered by the Auditor's report."*

During the course of the Respondents audit based on his audit procedure and also based on the information, explanations and representations

provided to the Respondents by management of NSEL, there were no frauds noticed or reported during the year. Accordingly, the Respondents had reported as such in his auditor's report referred to above.

c. With respect to commodities not being physically available, it is important to understand the auditor's responsibility towards such physical stock. NSEL is an exchange platform and is not the owner of physical stock. These stocks are not part of the balance sheet of NSEL. The physical stock is owned by trading members. Further there is no specific duty is cast upon the auditors under any of the guidance notes, orders, etc. issued by the ICAI and the only remaining duty cast upon the auditors is that of exercising reasonable skill and care, in discharging their functions as an auditor. The Respondents performed various procedures to review settlement of transactions and based on that there is no need to perform a physical verification of stock of third parties lying with NSEL.

4. The Director (Discipline) had, in his Prima Facie Opinion dated 10th April, 2017 with respect to **first allegation** noted that that the Respondents has brought on record the copy of the Gazette notification dated 6th Feb 2012, to show that it was a regulated exchange. On perusal of the media reports, it was observed that in early 2012 the FMC was appointed as 'designated agency' to collect data from NSEL and protect investors' interest. On 27 April 2012, based on the data provided by the Forward Markets Commission (India), the Ministry of Consumer affairs issued a show cause notice to NSEL that it was violating the conditions of 2007 exemption like 'no short sale', 'no stock verification mechanism' and ' conducting trades beyond 11 days'. So from early 2012- July 2013, the FMC knew about fraudulent NTSD (Non-Transferable Specific Delivery) contracts rampantly being conducted without registration under section 14A-14B of FCRA but for reasons unknown did not act. NSEL kept operating outside the realms of law and in March 2012, it notched up a Rs. 45,500 crore (about 7.5 Billion USD) turnover, the highest ever monthly average.

4.1 The Director (Discipline) further noted that although, the newspapers reports were treated as hearsay evidence, yet, looking into the fact that Show cause notice had been issued to NSEL as early as in April 2012 and the audit report had been signed by the Respondents on 21st May 2012 and the Respondents had not brought on record any documentary evidence to show the checks carried out by them after the Balance Sheet date to counter such claims being made in the newspaper reports. Thus, there were sufficient reasons to raise suspicion in the mind of the Respondents so as to thoroughly check/investigate into the affairs of NSEL before signing their report for the Financial Year 2011-12. In view of the above, **the Respondents were held prima facie Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

4.2 With respect to **second allegation** observed that in effect, third party inventories were held by NSEL. It is further noted that the Guidance Note on Audit of inventories provides as under:

*"In carrying out an audit of inventories, the auditor is particularly concerned with obtaining sufficient appropriate audit evidences to corroborate the management's assertions regarding the following:*

*Existence - that all recorded inventories exist as at the year-end*

*Ownership - that all inventories owned by the entity are recorded and that all recorded inventories are owned by the entity*

*Valuation - that the stated basis of valuation of inventories is appropriate and properly applied, and that the condition of inventories is recognized in their valuation.*

*The auditor should also obtain confirmation from such third parties for whom the entity is holding significant amount of stocks."*

However, the Respondents in their defence were silent about the same. He had not clearly spelt out what audit steps had been carried out by him to ensure the

correctness of the inventory including whether any third party confirmations was sought. **Thus, the Respondents were held prima facie Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

4.3 With respect to **third allegation**, it was observed that Note no. 39 to the financial statements refers to the Settlement Guarantee Fund and the same were shown as other liability in the financial statement of the Company for the F.Y. 2011-12 and had been recognized in accordance with the bye laws of the Company. The Respondents had drawn attention to Note no. 10 of the financial statements. On perusal of the same along with breakup given by the Respondents in their Written Statement, it was observed that the breakup given by the Respondents were not disclosed in the Financial Statement despite the fact the amount of the fund was 360.60 crores. This being a material amount was required to have been disclosed separately. Further, this amount was not traceable from Balance Sheet. It was observed that in the bye laws of NSEL there is no requirement of Settlement Fund. Further, the Respondents in his written statement also admitted that there was no specific guideline on investment of margin balance i.e. there was no policy of NSEL for investment of margin money and thus, the policy adopted by the Company should have been specifically brought out in the Notes to Accounts to convey a better picture as regards the basis on which the margin money was being invested It was also brought on record that although the Complainant had used the terminology Settlement Guarantee Fund with respect to the amount of Rs. 360.60 crores. It was actually Settlement Fund as referred to in the financial statements. Thus, the matter needs to be enquired into further with respect to this charge and **accordingly, the Respondents were held prima facie Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

4.4 With respect to **fourth allegation**, it is observed that that NSEL offered trading in various agricultural, metals and industrial commodities through its platform. It

offered customized procurement solutions to government agencies and private Companies. It also offered services like warehousing and collateral management services to market participants. Thus, the liabilities attached to ownership continued to be with the buyer/seller of commodities On a combined reading of the requirement of para 11 of SA 315 with the defence provided by the Respondents, it is clear that the Respondents have not spelt out whether any analysis of the business risks was undertaken by him and if so, his assessment of the same and its impact on the financial statement of the Company. **Thus, the Respondents were held prima facie Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

4.5 With respect to **fifth allegation**, it was noted that Paragraph 4(iv) of CARO requires the auditor to report on the following matter:

*"Is there an adequate internal control system commensurate with the size of the company and the nature of its business, for the purchase of inventory and fixed assets and for the sale of goods and services. Whether there is a continuing failure to correct major weaknesses in internal control system"*

However it was seen that the Respondents had not brought on record the audit procedures performed by them on the work of the internal auditor. The Respondents had merely commented that the internal auditors would have tested the relevant processes. In this regard, it was further held that the external auditor had the sole responsibility for the expression of the audit opinion and that his responsibility was not reduced by the external auditor's use of the work of the internal auditors. Thus, it was held that appropriate procedures were not employed by him to obtain reasonable assurance as regards the sufficiency and efficiency of the internal control system. **Thus, the Respondents were held prima facie Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

4.6 With respect to **sixth allegation**, it is noted that under Note no. 29 and 30 of the financial statements of the company for the year ended 31st March 2012 following information is provided:

*29. Related parties*
*Names of related parties where control exists irrespective of whether transactions have occurred or not:*

*Notes of financial statements for the year 2011-12*
*Holding Company: Financial Technologies (India) Limited*
*Subsidiary Company: Indian Bullion Market Association Limited*

*Names of other related parties with whom transactions have taken place during the year*

*Fellow Subsidiaries:-*

| | |
|---|---|
| *1* | *Atom Technologies Limited (Atom)* |
| *2* | *National Bulk Handling Corporation Limited (NBHC)* |
| *3* | *Tickerplant Limited (Tickerplant)* |
| *4* | *Financial Technologies Communications Limited (FTCL)* |
| *5* | *Credit Market Services Limited (CMSL)* |
| *6* | *Riskraft Consulting Limited (Riskraft)* |

| | |
|---|---|
| ***Associate*** | *Multi Commodity Exchange of India Limited (MCX)* |

***Key Management Personnel***

| | |
|---|---|
| *Jignesh Shah* | *Director* |
| *Anjani Sinha* | *Chief Executive Officer and Managing Director* |

30. ***Transactions with Related Party*** *- Refer Annexure B*

Thus, the aforesaid information covers the requirements of the AS 18. Also, the Complainant had not brought on record any information which should have been provided in terms of Pt (v) (*any other elements of the related party transactions*

*necessary for an understanding of the financial statements)* as per requirements of AS-18. Thus, the aforesaid charge fails against the Respondents and was **held Not Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

4.7 With respect to **seventh allegation**, the Director (Discipline) having regard to the byelaws of the exchange, requirements of AS 29 (Provisions, Contingent Liabilities and Contingent Assets) and the revised Schedule VI, opined that no disclosure as regards the value of the contracts outstanding for which exchange is counter party and the value of stock held by the exchange in the warehouse against the counter party liability is required. Thus, the aforesaid charge fails against the Respondents and was **held Not Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

**Committee's view on the seventh allegation:** However at the time of consideration of Prima Facie Opinion, the Committee is of the view that the allegation dealt in the above mentioned para is very basis of NSEL Scam. Moreover, the Committee decided that the requirement of AS-29 vis-à-vis disclosures made in the extent case needs to be further investigated taking into consideration the nature of contracts entered into and stock taken against them together with the bye-laws governing them. The Committee accordingly did not agree with the view of Director (Discipline) that no disclosures were required and hence, **decided to refer the said charge for further enquiry.**

4.8 With respect to **eighth allegation**, the Director (Discipline) noted that Respondents based on their audit procedure and also based on the information, explanations and representations provided to them by management of NSEL, reported that there were no frauds noticed or reported during the year. However, in view of the observation made in respect of first charge, it was opined that the matter needs to be examined further, in respect of this allegation also

**accordingly, the Respondents were held prima facie Guilty** for the professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

5. Accordingly, the Director (Discipline) in terms of Rule 9 of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007, held the **Respondents Prima-facie Guilty** of Professional Misconduct falling within the meaning of Items (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949. The said Item to the Schedule to the Act, states as under:

***Item (7) of Part I of Second Schedule:***

"A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he–

*(7): does not exercise due diligence, or is grossly negligent in the conduct of his professional duties;*

***Item (8) of Part I of Second Schedule:***

"A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he–

*(8): 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;*

6. The Respondents had made submissions dated 12th January 2018 in response to Prima Facie Opinion. The gist of submissions are as under:

   a. Media information is hearsay and is unreliable. They relied upon management discussions and management representations for the purpose of audit.

b. They obtained direct confirmation from NSEL members for stock lying at NSEL warehouse on sample basis.

c. There were no recorded inventories at year end. Hence there was no need of verification of existence.

d. Whether to take insurance cover or not is decision of the proprietary and does not require auditor comment or consideration.

e. The audit procedures deployed by them were different from internal auditors, hence they had considered observations of internal auditors but had not relied upon their work.

f. As regards disclosure of outstanding contracts as contingent liability they agree with findings of Director (Discipline) wherein they were held Not Guilty.

g. As regards fraud in NSEL, the allegation appears to be known on or after August 2013, whereas they had submitted report in May 2012.

7. The Respondents had made further submissions dated 22nd May 2019 wherein they had mentioned that:

a. There is no locus-standi of the Complainant.

b. The Complainant did not specify the clauses.

c. Director (Discipline) applied clauses at his own choice.

**Brief Facts of the Proceedings**

8. The Committee noted that the instant case was fixed for hearing on following dates:

| S.No. | Date | Status of Hearing |
|---|---|---|
| 1. | 30.05.2019 | Adjourned on the request of the Respondents |
| 2. | 25.06.2019 | Adjourned due to paucity of time |
| 3. | 09.08.2019 | Adjourned on the request of the Complainant |
| 4. | 04.09.2019 | Adjourned on the request of the Respondents |
| 5. | 06.01.2020 | Adjourned on the request of the Respondents |
| 6. | 25.11.2020 | Meeting cancelled due to unavoidable circumstances |

| | | |
|---|---|---|
| 7. | 02.09.2021 | Adjourned on the request of the Respondents and Complainant |
| 8. | 19.09.2022 | Part heard and adjourned |
| 9. | 07.11.2022 | Part heard and adjourned |
| 10. | 29.12.2022 | Part heard and adjourned on the request of the Respondents |
| 11. | 16.01.2023 | Part heard and adjourned on the request of the Respondents |
| 12. | 25.01.2023 | Part heard and adjourned |
| 13. | 06.04.2023 | Respondent opted for de-novo hearing. Accordingly, after taking the oath, the matter was adjourned |
| 14. | 11.07.2023 | Adjourned on the request of the Respondents |
| 15. | 25.07.2023 | Concluded and Judgement Reserved |
| 16. | 25.08.2023 | Final decision taken on the case |

9. On the day of **first hearing** held on 30th May, 2019, the Committee noted that the Respondents had sought an adjournment. The Committee further noted that the Complainant was not present. The Committee looking into the absence of both the parties, decided to adjourn the matter to the next date.

10. On the day of **second hearing** held on 25th June, 2019, the hearing was adjourned due to paucity of time.

11. On the day of **third hearing** held on 9th August, 2019, the Committee noted that the Counsel for the Complainant was present. He requested for adjournment of hearing due to his personal difficulty. On the same, the Committee decided to adjourn the hearing with information to the Respondents. The Committee also informed that next hearing in the matter will be held on 4th September 2019. With this, hearing in the matter was adjourned.

12. On the day of **fourth hearing**, held on 4th September, 2019, the Committee noted that the Respondents had sought an adjournment. The Committee looking into the absence of Respondents, decided to adjourn the matter to the next date.

13. On the day of **fifth hearing** held on 6th January, 2020, the Committee noted that the Respondents had sought an adjournment. The Committee looking into the absence of Respondents, decided to adjourn the matter to the next date.

14. On the day of **sixth hearing** held on 25th November, 2020, the Committee noted that the meeting was cancelled due to unavoidable circumstances.

15. On the day of **seventh hearing** held on 2nd September, 2021, the Committee noted that the Complainant vide email dated 18th August, 2021 had sought an adjournment in the matter for 8 weeks. The Respondents also sought adjournment on the ground of unavailability of his counsel on date of hearing. The Committee looking into the same acceded to their request and granted the adjournment. The Office was directed to inform the parties accordingly.

16. On the day of **eighth hearing** held on 19th September, 2022, the Committee noted that the Complainant was not present. However, the Respondents were present through Video Conferencing Mode through their Counsel CA. A.P. Singh. The Respondents were administered on Oath. Thereafter, the Committee enquired from the Respondents as to whether they were aware of the charges. On the same, the Respondents replied in the affirmative and pleaded Not Guilty to the charges levelled against them. Thereafter, the Counsel of the Respondents sought adjournment in the matter. The Committee, looking into the fact that this was the first hearing, decided to adjourn the hearing to a future date. With this, the hearing in the matter was partly heard and adjourned.

17. On the day of **ninth hearing** held on 7th November, 2022, the Committee noted that the Respondents along with their Counsel CA. A.P Singh were present at ICAI Tower, BKC Mumbai. The Committee noted the Complainant was not

present despite notice being duly served to him. The Committee, looking into the facts of the present case, directed the Respondents to submit the following:

a. Whether any Internal Audit Committee and/or Risk Management Committee were in existence/established by the Company? If yes, then whether any meetings were held
b. Attendance and Minutes of those meetings
c. As to why the Internal Audit Report was not considered by the Respondents as Statutory Auditor.

With the above directions, the Committee decided to adjourn the hearing to the next date.

17.1 The Committee noted that the Respondents in their response had inter-alia submitted as under:

a. That the functions and also the nature of responsibilities, of an internal auditor and a statutory auditor who audits the financial statements of the Company under Companies Act, 1956 are very different.

b. As per Standard on Auditing (SA) 610 (Revised) Using the work of Internal Auditors-
*"Nothing in this SA requires the external auditor to use the work of the internal audit function to modify the nature or timing, or reduce the extent, of audit procedures to be performed directly by the external auditor; it remains a decision of the external auditor in establishing the overall audit strategy".*

c. Further para 11 of SA 610 states that – *"The external auditor has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the external auditor's use of the work of the internal audit function or internal auditors to provide direct assistance on the engagement……."*

d. Paragraph 4(vii) of the CARO requires the auditor to report as follows:

*"In the case of listed companies and/or other companies having a paid-up capital and reserves exceeding Rs.50 lakhs as at the commencement of the financial year concerned or having an average annual turnover exceeding five crores rupees for a period of three consecutive financial years immediately preceding the financial year concerned, whether the company has an internal audit system commensurate with its size and nature of its business."*

e. They performed the audit procedures of the nature indicated by the paragraph 61(i) of the statement on CARO issued by ICAI.

f. Based on above it can be noted that statutory auditors are not mandated to rely on the work of internal auditor. That they had reviewed the internal audit reports and the observations relevant to financial statement audit were duly considered.

g. The Respondents audited the NSEL for the years ended 31st March, 2010, 2011 and 2012. Section 292A of the Companies Act, 1956 states that every public Company having paid-up capital of not less than five crores of rupees shall constitute a committee of the Board known as "Audit Committee". Further, Section 295 of the Companies Act 1956 states that a meeting of its Board of directors shall be held at least once in every three months and at least four such meetings shall be held in every year. As part of their audit procedures, they reviewed minutes of the audit committee and board meetings. They also obtained a letter of representation from management for each year of audits stating dates and nature of the meeting and also produced the dates of board meeting.

h. Based on information, explanation and from the documents made available to them, they noted that NSEL had formed the audit committee required under Section 292A of the Companies Act 1956. As part of audit for the years ended March 31, 2010, March 31, 2011 and March 31, 2012, NSEL provided the minutes of the audit committee meetings. Based on the documents provided, they placed reliance on these to

understand that the audit committee discussed various matters including review and recommendation of audited financial statements to the Board for approval. They had also reviewed minutes of board meeting that noted approval of financial statements. It can further also be noted that financial statements were signed by directors who were also members of the audit committee. They had attached the copy of audit committee and board meeting minutes provided by the Company.

i. It was noted that they had performed detailed understanding of the entire trading and settlement process of NSEL. Through this understanding risk involved were assessed. They also performed procedures to address these risks and documented our conclusions.

j. They had complied with the requirements of SA 315 and SA520 (revised), as well as the other auditing standards issued by the ICAI, in audits of the financial statements of NSEL. Consequently, and in the absence of any matters to be considered for reporting under SA 700 (AAS 28) "The Auditor's Report on Financial Statements", there was no reason to invite attention of the shareholders to any material departure from the generally accepted auditing procedure applicable to the circumstances.

18. On the day of **tenth hearing** held on 29th December, 2022, the Committee noted that the Respondents i.e. CA. Amit Kabra alongwith his Counsel CA. A P Singh were present through video conferencing mode. The Committee noted that the Complainant was not present. Thereafter, the Committee asked the Respondents to make his submissions. The Respondents in his submissions had inter-alia mentioned as under:

a. That since one of the Respondents was out of India and for most of the allegations his presence is required hence he was limiting the discussions.

b. That the charges in this case have not been provided to the Respondents.

c. That the Director (Discipline) had himself applied the Items which are not in the Complaint.

d. That there is no copy of any media report however the media report was being referred to in the opinion.

e. That he submitted his line of defense referring the paras of Prima Facie Opinion and Standards on Auditing.

f. That Ms. Anjani Sinha, Managing Director and CEO of NSEL and Mr. Kotiyan who is the former CEO confirmed them in their closing discussion that NSEL had not received any notice or inspection from the FMC or any Government Authority then how the auditor could be aware of any Government Complaint.

g. That they have reviewed the list of Complaints against NSEL and did not find any complaint in connection with the matter allegedly identified any media report.

18.1 The Committee noted that the Respondents counsel sought adjournment on the ground that the other Respondents, i.e. CA. Shrawan Bhagwati Jalan, was not in India and his physical presence is necessary in the matter. Thereafter, the Committee looking into his request decided to adjourn the case to further date. The Committee, while adjourning the matter, directed the Respondents to submit the present status of cases pending before Courts relating to NSEL within next 10 days. With this, the hearing in the matter was partly heard and adjourned.

18.2 The Committee noted that Respondents had inter-alia made the submissions dated 06th January 2023 as per their directions given in the meeting held on 29th December 2022 wherein they has raised certain questions and sought certain documents from them and they are directed to submit a note on pending matters which may impact the outcome of the proceedings in the current matter:-

The Respondents had submitted the list of cases pending against them before various courts/tribunals on the similar issues. They have also submitted their response on the questions raised during meeting by reiterating their submissions made in their written statement. They further submitted that they had obtained the minutes of audit committee meeting wherein it has mentioned that audit committee had reviewed the half yearly and annual accounts. They had not relied on report of internal auditor instead perform their own procedures. Also it

was not mandatory to rely on the work of internal auditor. They had performed the detail understanding of entire trading and settlement process of NSEL and through this understanding risk involved were assessed. They also performed procedures to address these risks and documented their conclusions. Further they had complied with all the accounting standards issued by ICAI and there was no reason for them to invite attention of the shareholders to any material departure from the generally accepted auditing procedure applicable to the circumstances.

19. On the **eleventh day of hearing** held on 16th January, 2023, the Committee noted that both the Respondents alongwith their Counsel CA. A P Singh were present through video conferencing mode. The Committee noted that the Complainant was not present. Thereafter, the Counsel for the Respondents sought adjournment on account of his personal commitments. Thereafter, the Committee looking into his request decided to adjourn the case to a later date.

20. On the **twelfth day of hearing** held on 25th January, 2023, the Committee noted that the Complainant was not present, and no intimation was received from the Complainant in reply to the duly served notice. The Committee noted that the Respondents had changed their counsel and taken the services of Shri Ajay Bahl, Advocate and they were present through video conference mode. Thereafter, the Committee asked the Respondents to make his submissions. The Respondents in his submissions had inter-alia submitted as under:

    a. That the Director (Discipline) has levied the charge which was not there in the original complaint filed by the Complainant.
    b. That the said matter should be referred back to Director (Discipline) as he has not been given an opportunity of being heard and to respond on the allegations.
    c. That the Complaint is not relevant to the audit period during which he was the auditor.

20.1 The Committee posed certain questions to Respondents to understand his submissions. The Committee noted that the Counsel for the Respondents raised objections by stating that the charges framed by the Director (Discipline) were different from those alleged in the complaint by the Complainant. On the same, the Committee directed the Respondents to submit those objections in detail along with evidence within the next 7 days. The Committee also directed the Office to forward such objections to the Director (Discipline) for his comments thereon, if any, in terms of the provisions of Rule 18(5) of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007. The Committee also directed the Respondents to submit their submissions on the merits within the next 14 days.

20.2 The Committee noted that the Respondents had inter-alia made the following submissions as per their direction:

Submissions dated 1st February 2023

a) The Respondents had submitted that the Director (Discipline) had dealt with the matter with significant hindsight bias. Such an approach does not reflect an assessment of the work done by the Respondents against the facts and circumstances which existed as at the dated on which the audit report of NSEL for the financial year ended 31st March, 2012 was issued.

b) The Respondents drew attention to Para A26 of SA 200 wherein it was mentioned that the judgement on the work of the auditor should be evaluated based on the circumstances that, to his knowledge and belief, existed at the time of conducting the audit of the Company for the said financial year.

c) The Respondents further submitted that the PFO had made new allegations against the Respondents that were not alleged in the Complaint without giving any opportunity to provide an explanation and present their case which is contrary to the provisions of the CA Act and Rules. The

Respondents also quoted some case laws to prove the same. Hence the Respondents should be provided with an opportunity to explain allegations against it, prior to issuance of the PFO.

d) That if the Respondents had been provided with an opportunity to explain the new allegations, they would have very easily demonstrated that, since the inventory in the warehouse does not belong to NSEL, they have no obligation to verify the said inventory nor seek any third party confirmations.

e) That if a statement made or document or report prepared by a third-party have been or are relied upon by the Disciplinary Committee to hold the Respondents guilty, the Respondents must be provided with an opportunity to cross-examine such third parties with respect to the statement, document or report being relied upon.

20.3 The Respondents further made their submissions dated 8th February, 2023 on merits and had inter-alia mentioned as under:

a) At the time the Respondents issued the Subject Audit Report they were neither aware of any show cause notice of April 2012 nor any government action nor any media report referring to any such show cause notice. Also the Director (Discipline) has provided no evidence that any such media reports existed at the relevant time nor did he identify any such media report in paragraph 17.7 of the PFO.

b) Since the inventory in the warehouses did not belong to NSEL, the Respondents had no obligation to verify the said inventory or seek any third-party confirmation (as mention in guidance note on audit of inventories). Based on their testing of documents related to the flow of transactions and funds settlements, the auditors noted that no matters arose to suggest that inventory was not physically available at the relevant warehouses

c) Margin money of Rs. 328.93 crores received by the company in its bank accounts were reflected under various asset heads in the financial statements for the year ended 31st March, 2012.

d) It is reiterated that NSEL had no obligation to insure the goods lying in the warehouses since they did not belong to NSEL and is not a business risk of NSEL that could have created a risk of material misstatements in the financial statements nor the misstatements of an assertion risk as that term is explained in SA 315.

e) Further merely because the statutory auditors reviewed the internal auditors report with a view to address, observations raised by the internal auditors in such report (and to ensure that relevant deficiencies identified by the internal auditor are ignored) does not mean that the statutory auditors relied on the internal auditors' report for issuing its own statutory audit report.

f) During the course of the Subject Audit, based on audit procedures performed by them and representations provided to them by NSEL management, there were no frauds noticed or reported during the year.

20.4 Thereafter the Director (Discipline) had made his submissions on the said allegations of the Respondents made in the above submissions:

a) That the Director (Discipline) has the authority under Chartered Accountants Act, 1949 (hereinafter referred to as 'the CA Act') and the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007 (hereinafter referred to as 'the Misconduct Rules') to enlarge the scope of the allegations from those set out in the Complaint and/or to make new allegations.

b) It is submitted that the role of Director (Discipline) under Section 21 (2) of the CA Act read with Chapter III (Rule 8-12) of the Misconduct Rules is inquisitorial in nature wherein the Director (Discipline) conducts an

investigation into the allegations raised in the Complaint and, thereafter, forms a prima facie opinion based on the facts emerging from the said investigation.

c) It is submitted that the allegations contained in the Complaint are the starting point for triggering of the said investigation. The Director (Discipline) is required to comprehensively investigate the entire matter, i.e., the allegations made in the Complaint, with all the evidences, documents or analysis collected during the investigation and forms his Prima Facie Opinion accordingly.

d) The Director (Discipline) is well within its rights to enlarge the scope of the allegations contained in the Complaint and/or to make new allegations that emerge from the said investigation or come to his notice while undertaking the said investigation.

e) In this context, regard may be placed on Rule 9 of the Misconduct Rules which indicates that the Prima Facie Opinion of the Director (Discipline) must be formed after due examination of not only the complaint but also the written statement, rejoinder and any other additional particulars or documents which will emerge out of investigation into the allegations contained in the Complaint.

f) Reliance is placed on the decision of Excel Crop Care Ltd. v. Competition Commission of India 8 SCC 47 (2017) wherein the Hon'ble Supreme Court of India while dealing with analogous question relating to the role of Director- General, Competition Commission of India under the Competition Act, 2002 have held that the Director General has the power to add on allegations than those contained in the information/complaint.

g) Applying the said proposition to the role of Director (Discipline) under CA Act it is submitted that the complaint filed by the complainant was the starting point of investigation by Director (Discipline). The PFO dated 10th April 2017 was issued after due examination of the papers on record including the Complaint and the Written Statement.

h) The alleged additional/new allegations contained in the said Prima Facie Opinion dated 10th April 2017 have emerged from the investigation

conducted by Director (Discipline), which can be seen from the explanation provided in relation to the specific charges hereinafter. Accordingly, the Director (Discipline) is well within its powers to include them in their Prima Facie Opinion.

i) It is submitted that under the provisions of CA Act and Misconduct Rules, the matter cannot be remanded back, at this stage, for the issuance of a fresh Prima Facie Opinion. It is submitted that Rule 9 of the Misconduct Rules lays down the procedure in relation to placing of the Prima Facie Opinion before the Hon'ble Disciplinary Committee and the manner in which it can be proceeded further by the Hon'ble Disciplinary Committee.

j) It can be seen that the Hon'ble Disciplinary Committee can only remand/send the matter back to Director (Discipline) at Rule 9 stage wherein it disagrees with the Prima Facie Opinion of the Director (Discipline). It is further submitted that wherein the Hon'ble Committee agrees with the Prima Facie Opinion of the Director (Discipline), it has to necessarily proceed with the adjudication of matter in accordance with Chapter V of the Misconduct Rules.

k) In the present matter, the Prima Facie Opinion dated 10th April 2017 was placed for the consideration of the Hon'ble Disciplinary Committee on 12th September 2017 wherein the Hon'ble Committee concurred with the reasons given against the charge (s) (except for the reasoning as regard the charge raised in Para 1.7 of the complaint and dealt in para 17.21. to 17.28 of the said Prima Facie Opinion) and, thus, agreed with the Prima Facie Opinion of the Director (Discipline).

l) The Scheme of the Rules are crafted in such a way that except at the stage of consideration of the Prima Facie Opinion, the Committee is not empowered to refer back the matter for further investigation to the Director (Discipline).

m) No hindsight bias can be alleged against Director (Discipline) as allegations against the Respondents have been tested on the parameters of professional responsibilities expected out of a Chartered Accountant as provided under various applicable rules and regulations.

n) Media reports were available in public domain at the relevant time which ought to have made the Respondents suspicious of how the business of spot exchange was being carried out and regulated by NSEL.

o) The Respondents ought not to have merely relied on confirmation and representation of the management and ought to have obtained sufficient audit evidence to corroborate that all stored goods on behalf of third parties existed at the relevant time to ensure correctness of the inventory.

p) Despite the amount of margin money being huge and material, no disclosure, whatsoever, of such a significant policy of NSEL was brought out in the Notes to Account. Further, the Respondents also failed to disclose the basis on which the margin money was being invested by NSEL.

q) It is submitted that under-insurance is an important business risk that can have severe consequence for a business including finding itself severely out of pocket. The Respondents have not provided any analysis of the business risks relating to under-insurance done by them. Infact they have submitted that they had not done the analysis of business risks relating to under insurance.

r) The Respondents had failed to employ appropriate and independent audit procedures to obtain reasonable assurances about the adequacy and sufficy of internal control system.

s) The Respondents had not brought any satisfactory documentary evidence to show that the checks carried out by them to counter such claims being made in the newspaper reports.

21. On the day of **thirteenth meeting** held on 6th April, 2023, the Committee noted that the Respondents along with their counsel, CA. Ajay Behl (along with his Assistant CA Ayush) were present through Video Conferencing and appeared before it. The Committee further noted that neither the Complainant was present, nor any intimation was received despite notice/email duly served upon him.

21.1 The Committee noted that the present matter was also listed earlier on various dates before different Committees. The Committee noted that the constitution of earlier Committees is as under:

| Council Year | Name of members of the Committee |
|---|---|
| 2019-20 | CA. Atul Kumar Gupta (Presiding Officer)<br>Shri Rajeev Kher, I.A.S. (Retd.), Government Nominee<br>CA. Amarjit Chopra, Government Nominee<br>CA Rajendra Kumar P, Member<br>CA. Chandrashekhar Vasant Chitale, Member |
| 2020-21 | CA. Atul Kumar Gupta (Presiding Officer)<br>Shri Rajeev Kher, I.A.S. (Retd.), Government Nominee<br>CA. Amarjit Chopra, Government Nominee<br>CA Rajendra Kumar P, Member<br>CA Pramod Kumar Boob, Member |
| 2021-22 | CA (Dr.) Debashis Mitra, Presiding Officer<br>Shri Rajeev Kher, I.A.S. (Retd.), Government Nominee<br>CA. Amarjit Chopra, Government Nominee<br>CA Rajendra Kumar P, Member<br>CA. Babu Abraham Kallivayalil, Member |
| 2022-23 | CA (Dr.) Debashis Mitra, Presiding Officer<br>Mrs. Rani Nair, I.R.S. (Retd.), Government Nominee<br>Shri Arun Kumar, I.A.S. (Retd.), Government Nominee<br>CA Rajendra Kumar P, Member<br>CA Cotha S Srinivas, Member |

21.2 The Committee further noted that since the composition of the Committee had changed further to the previous hearing, the Committee enquired from the Respondents, whether they wished to have a de-novo hearing which was accepted by the Respondents. Hence the Committee acceded to the request of the Respondents and started a fresh hearing on the matter. The Respondents

were administered on Oath. Thereafter, the Committee enquired from the Respondents as to whether they were aware of the charges. On the same, the Respondents replied in the affirmative and pleaded Not Guilty to the charges levelled against them. Thereafter, looking into the fact that this was the first hearing, the Committee decided to adjourn the hearing to a future date.

22. On the day of **fourteenth meeting** held on 11th July, 2023, the Committee noted that the Respondents had sought adjournment vide email dated 05th July, 2023 on ground that their Counsel was travelling abroad. The Committee noted that neither the Complainant was present nor any intimation was received despite notice/email duly served upon him. The Committee looking into the grounds of natural justice acceded to the adjournment request made by the Respondents, and accordingly, the case was adjourned. The Committee also directed to Office to inform the parties that no more extension shall be granted to the parties.

23. On the day of **fifteenth and final hearing** held on 25th July, 2023, the Committee noted that the Respondents along with their counsel, CA. Ajay Behl (along with his Assistant CA Ayush) were present through Video Conferencing and appeared before it. The Committee further noted that neither the Complainant was present, nor any intimation was received despite notice/email duly served upon him.

23.1 The Committee noted that the present case was listed for 14 occasions however because of various reasons it could not be completed. The Committee informed the Respondents that since one of the claim of Respondents in earlier hearing are that they had not been given a natural justice by without asking them anything and the finding had been given by Director (Discipline). Now since this Committee is superior to Director (Discipline), they have been given the opportunity to submit the document in their support and it will be considered by the Committee and after that the Committee will take the appropriate decision. Further since the Respondents were being given a fresh hearing hence whatever the issues had been raised earlier by them were of no relevance now.

23.2 Thereafter, the Committee asked the Respondents to make their submissions. The Respondents in their submissions had inter-alia submitted as under:

a. That they have submitted their reply on 8th February, 2023 wherein they had mentioned that the Complainant and Director have dealt with the matter on a significant hindsight bias and all the allegations and charges made are the result of such bias.

b. Such an approach does not reflect the assessment of the work done by the Respondents against the facts and circumstances which existed on the date on which audit report was issued.

c. With respect to **first charge**, it is submitted that there is absolutely no evidence as to the media reports were in the public domain before they signed the audit report.

   i. There is not a single document to suggest that they had seen or were aware of the media reports.

   ii. They were also not aware of the show cause notice issued to NSEL and there is no evidence to establish that the said show cause notice was brought to their attention before signing the report.

   iii. Further there is nothing in the Management Representation letter to doubt the credibility of the managing director and CEO of the Company. If the management has received something and doesn't give to them, they have no way of knowing that the notice has been received.

   iv. Moreover, they have ran all the procedures to perform post balance sheet events also and reviewed on sample basis subsequent payments and receipts, minutes and board meetings, etc. up to 20th May, 2012.

d. With respect to **second charge**, it was submitted that the NSEL is only a platform for conduct of activity and it does not holds any inventory. As per CARO, an auditor is required to comment on whether the management has conducted the physical verification of inventory at reasonable

intervals and they were told by the management that whose inventory were lying there had come and checked the event and therefore they have no obligation to verify the same.

i. The bail applications of the Respondents were favourably considered wherein the court has said that they were not supposed to verify the goods. As per Guidance note on CARO also, those people whose inventory was lying there were responsible for getting it checked.

ii. In fact, they have checked the complaint register and did not find any complaints suggesting that there were any shortfalls in the inventory of third parties. The fact that NSEL have issued a warehouse receipt doesn't make auditor responsible to treat the inventory as inventory of NSEL. They have also done a complete fraud assessment.

iii. That ownership and custody are two different things and ownership has nothing to do with the custody. They have verified all details of delivery. They have also tested trade cases based on sampling wherein 22 days of settlement were checked, 92% of the margin that was deposited has been traced and trades traded between unconnected parties has been checked.

iv. Moreover delivery has been achieved through the transfer of warehouse transfer receipts which evidence the existence of goods. They have run all the tests and noting alarms them that there is any shortfall.

e. With respect to **third charge**, it was submitted that the amount of settlement guarantee fund was not material and thus not disclosed separately in the financial statements. Further the requirement here is to keep a margin. Every member has to keep a margin which is a liability but it is available to settle a default by that member in favour of somebody else. They had run test to show that these funds, margin money was not used in breach of the byelaws.

i. Margin is of two kinds, one is the money that is given to the Company as the margin by the member who retains certain portion of money. Second is where they give bank guarantees and FDs which are of

balance sheet items, which are their assets but don't come into the books but are marked as a lien so that those assets are available to Company but not come into the bank account. So fixed deposits of Rs 31.67 crores included in settlement fund is available but never received by the Company to represent as an asset or liability.

ii. That the amount was collected as margin and settlement fund was identified and checked. The utilization of fund received. Their investment was tested and it was evident that the corresponding funds were largely liquid or been recovered.

iii. No evidence of settlement defaults and claims having a negative impact on the liability. Neither assets nor liabilities have been understated. Nor is the profit been impacted by this. Adequate diligence to trade the margin money received. No misutilization of the margin has been pointed out.

f. With respect to **fourth charge**, it is submitted that they have done a complete review of the business. They have taken a look at the risk associated with it and have tested the resource. The risks against the checks and balances that exist in the likelihood of a risk resulting into a financial implication but to the extent that doesn't belongs to NSEL and they are not required to be responsible for it, which is basically somebody else's asset. Further the financial risks that were required to be assessed have already been assessed and the Director (Discipline) in his Prima Facie Opinion also says that the liabilities attached to ownership. Moreover the same issue is in subsequent year also however the order has been passed for that year which is in the public domain and in that particular order there is no reference that under insurance is a risk to Company.

g. With respect to **fifth charge**, it is submitted that they have read the report of the internal auditor but not relied on that and have performed their own procedures. They have done their work independently and

requested the Committee to test the work done by them instead of simply relying on the assumption that nothing has been done by them.

h. With respect to **eighth charge**, it is submitted that there is no evidence that media reports were available. Further as per guidance note on CARO, it was the management who should have brought it to auditor's attention about the fraud in Company. However, no such fraud has been brought to attention by management. Infact they have given a representation that there were no ongoing fraud in NSEL. Inspite of that they have run a complete fraud assessment for identifying the fraud. They had done their own analysis and take a counter representation from management as well to make sure that the statement is received.

23.3 The Committee noted all the arguments of the Respondents. The Committee posed certain questions to the Respondents to understand the issue involved and the role of the Respondents in the case and also taken on record all papers submitted by them and make them part of the proceedings. After consideration of the same, the Committee directed that the Respondents to submit following in the next 15 days:

a. Present status of the case against the Respondents at EOW/other forums
b. Summary of his submissions

23.4 After detailed deliberations, and on consideration of facts of the case, various documents on record as well as oral submissions of Respondents before it, the Committee decided to conclude the hearing in the instant case by reserving its judgement.

24. Thereafter, this matter was placed in meeting held on 25th August 2023 for consideration of the facts and arriving at a decision by the Committee. The Committee noted that the above case was concluded on 25th July, 2023 with the directions to Respondents to submit the following documents within the next 15 days:

a. Present status of the case against the Respondents at EOW/other forums
b. Summary of his submissions.

24.1 The Committee noted that the Respondents had submitted certain documents and on perusal of the oral submissions vis-a-vis submitted documents it was noted by the Committee that the Respondents not only failed to exercise due diligence while auditing but also failed in obtaining sufficient information for expressing an opinion

24.2 Accordingly, keeping in view the facts and circumstances of the case, the material on record and the submissions of the parties, the Committee passed its judgement.

**FINDINGS OF THE COMMITTEE**

25. The Respondents submission that charges which are not given by the Complainant have been allegated and the Respondents have been held guilty on them without reference to them and such matter be sent back to Director (Discipline). The erstwhile Committee called the comments of Director (Discipline) and the same are given in Para 20.4 of these findings. The Respondents demanded the same so that they can give their submissions. The Committee is of the view that the same is not required because the case is being heard de-novo and the Respondents had already made its submissions on merits on each charge in Prima Facie Opinion and the Committee had later on records all of them. The Committee heard at length the Respondents on this and as such the Committee is making its findings in foregoing paragraphs charge wise.

25.1 **Charge 1**

The Committee noted that the first charge against the Respondents is that in the notes to financial statements, in point 1, it is stated that National Spot Exchange is a regulated electronic spot exchange, however as per available information in the media and Government findings, NSEL is an unregulated exchange and this has caused serious damage to the investor while protecting the interest worth

Rs.5,550 crores as investment are made with this belief that exchange is regulated.

25.2 **Submissions of the Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents have submitted that for the year ended March 31, 2012 NSEL had changed the status of a self-regulated exchange. Accordingly, NSEL was self-regulated until the February 6, 2012 notification at which time it became regulated by FMC.
b. That media information is hearsay and is unreliable. They relied upon management discussions and management representations for the purpose of audit.
c. That they have reviewed the list of Complaints against NSEL and did not find any complaint in connection with the matter allegedly identified any media report.
d. That the Director (Discipline) has dealt with the matter with significant hindsight bias.
e. At the time the Respondents issued the Subject Audit Report they were neither aware of any show cause notice of April 2012 nor any government action nor any media report referring to any such show cause notice.
f. Further there is nothing in the Management Representation letter to doubt the credibility of the managing director and CEO of the Company.
g. Moreover, they have ran all the procedures to perform post balance sheet events also and reviewed on sample basis subsequent payments and receipts, minutes and board meetings, etc. up to 20th May, 2012.

25.3 The Committee on the plea of the Respondents noted that the Director (Discipline) is well within its rights to enlarge the scope of the allegations contained in the Complaint and/or to make new allegations that emerge from the said investigation or come to his notice while undertaking the said investigation.

Further NSEL was issued a show cause notice by the Ministry of Consumer Affairs on 27th April 2012 in relation to violations before signing of the Audit Report by the Respondents which ought to have made the Respondents suspicious of how the business of spot exchange was being carried out and regulated by NSEL.

**Findings of the Committee on Charge 1:**

25.4 The Committee on perusal of Note no. 1 of notes to accounts to financial statements for the financial year ending 31st March 2012 noted that the Company mentioned as under:

*"National Spot Exchange is a pan India regulated electronic spot exchange offering trading in various agricultural, metals and industrial commodities through its platform. It also offers customized procurement solutions to government agencies and private companies. It also offers services like warehousing and collateral management services to market participants."*

25.5 From the above notes, it appears that the Company was a regulated electronic spot exchange. However, it was observed that the Respondents failed to bring on record documentary evidence to show that the Company (NSEL) was a regulated entity and had taken any permission to do the business of spot exchange from any Government Authority / Agency. The Committee observed that the company was dealing with various persons, including stock brokers, sub-brokers, godown owners, bankers, and the general public, and taking margin money from them as well. Moreover, it was providing the service of spot exchange PAN India without involvement of any government agency that can control the business activity of the company to obtain robustness, safety and resilience in the activities conducted by them.

25.6 The Committee further noted that the Respondents had given the reference of notification issued by DCA dated 6th February, 2012 wherein DCA has appointed the FMC as designated agency to which all information or returns relating to the

trade shall be provided to FMC. Hence, FMC will be the regulator for all future commodity exchanges in India. Thus, it shows that DCA is regulating the NSEL and the same is also in the knowledge of the Respondents as they themselves have informed the same. Also the said notification is before the date of signing of financial statement however the Respondents have not considered the same hence they are **held guilty of professional misconduct for the said charge** falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

26. **Charge 2**

The Committee noted that the second charge relates to violation of AS 9 on Revenue Recognition for consideration of warehouse receipts:

(a) as per note No.20 Revenue from operations –out of Rs.81.93 crores *'income from operations'* Rs. 11.46 crores have been collected as warehouse receipt transfer charges and warehouse income. Approx. 13.99% of the income pertain to this head, whether the auditor has verified the underlying goods while accounting for such a significant income.

(b) Statutory Auditors of the Company in their attestation function should have ensured that revenue is recognized as per the accounting policy and applying the principles and procedures laid down in the Guidance Note –Guidance Note on audit of revenue issued by the ICAI.

Guidance note states that the auditor should employ appropriate audit procedures to obtain reasonable assurance about various assumptions in recognition of the revenue.

26.1 **Submissions of Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents have submitted that they have performed audit procedures to address recognition of income which includes reading and reviewing the

income from warehouse on basis of samples and also performed overall analytical review of WRT income.

b. That they had obtained direct confirmation from NSEL members for stock lying at NSEL warehouse on basis of sample and there were no recorded inventories at year end.

c. Since the inventory in the warehouses did not belong to NSEL, the Respondents had no obligation to verify the said inventory or seek any third-party confirmation.

d. As per CARO, an auditor is required to comment on whether the management has conducted the physical verification of inventory at reasonable intervals and they have obtained the management confirmation for the same.

e. As per Guidance note on CARO also, those people whose inventory was lying there were responsible for getting it checked.

f. They have also done a complete fraud assessment. They have verified all details of delivery and trade cases based on sampling.

26.2 **Findings of the Committee on Charge 2:**

The Committee in view of merits of findings noted that Guidance Note on Audit of Revenue issued by ICAI obligated an auditor to employ appropriate audit procedures to obtain reasonable assurance about various assumptions in recognition of the revenue. However, the Respondents have not applied these procedures and simply accrued revenues without verifying underlying transactions or inventory which is basis for accrual of warehouse income.

26.2.1 Further, if auditee is recognizing the revenue as "warehouse receipt" which shows that the auditee is in control of warehouse and its contents. Further the Para 23 of the Guidance Note on the Audit of Inventories specifically states that the auditor should obtain confirmation from third parties. Paragraph 48 of the ICAI Guidance on CARO, 2003 do not exclude inventories being held on behalf of third parties and requires checking of adequacy and reasonableness

of the physical verification of inventory in line with the nature of business. Further as far as the plea of Respondents that Guidance Note on Audit of Inventories has no nexus with Charge no. 2 is concerned, though there is no doubt this relates to AS 9, however, as per allegation, warehouse receipt transfer (WRT) charges forms 65% of income from sale of services, hence, WRT was required to be checked in depth. For checking/verification of WRT, the underlying inventory held by NSEL on behalf of third party was also required to be checked. Therefore, reference of Guidance Note on Audit of Inventories in the prima facie opinion while dealing with this allegation cannot be termed as irrelevant as claimed by the Respondents in their submissions.

26.2.2 The Committee also noted that as per Guidance Note on Audit of Inventories, verification of inventories may be carried out by employing the following procedures:

*(a) examination of records;*

*(b) attendance at stock-taking;*

*(c) obtaining confirmations from third parties;*

*(d) examination of valuation and disclosure; and*

*(e) analytical review procedures.*

*The nature, timing and extent of audit procedures to be performed is, however, a matter of professional judgement of the auditor.*

**(b) *Attendance at Stock-taking***

*Physical verification of inventories is the responsibility of the management of the entity. However, where the inventories are material and the auditor is placing reliance upon the physical count by the management, it may be appropriate for the auditor to attend the stock-taking*

**(c) *Confirmations from Third Parties***

*the auditor should also obtain confirmation from such third parties for whom the entity is holding significant amount of stocks*

From the above provision it was noted that an auditor is required to physically verify the inventory at client's place and should also obtain third party confirmations for whom the entity is holding significant amount of stock. However in the instant case the Respondents have not verified the stocks lying at client's place simply taking the excuse that the stock is of third party. Further, the Respondents relied on the management representation that the parties whose stocks are lying with NSEL has conducted their check and fails to provide any evidence that whether they perform any counter check on the said inventory. Moreover only on the basis that warehouse receipts are issued and the buyer of the goods made the payment does not substantiate that there is no shortfall and goods are lying in the warehouse at the time of transaction and as such **Committee held the Respondents Guilty of professional misconduct for the said charge** falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

27 **Charge 3**

The Committee noted that the third charge relates to deviation of amount from settlement guarantee fund. As per Notes to Accounts No.39, Settlement Guarantee Fund ("SGF") of Rs.360.60 crores has been maintained as on 31st March, 2012, which has been received in the form of Bank Deposits, FDs, Cash, etc. should have been deployed in the same manner in liquid assets. But the SGF has been diverted to unrelated assets such as Trade Receivable, Short Term Loans and Advances and other current assets, against the Bye Laws of the Exchange. This also reflects that the financial statements of the Company is not reflecting true and fair view of the affairs of the Company as at balance sheet date as required u/s section 209 of the Companies Act, 1956 (which requires that the Companies should maintain proper books of accounts) for financial year 2011-12.

27.1 **Submissions of the Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents had submitted that notes to accounts Note 39 does not refer to Settlement Guarantee Fund ("SGF') but instead, to the Settlement Fund ("SF"). The Respondents noted that there was no predefined investment policy enshrined in NSEL's Bye-Laws and Rules. In the absence of any such specific guidelines approx. 50% of the margin balance has been deployed in liquid mutual fund and the balance in temporary loans and advance to generate income. It is important to note that the Company had generated income by investing these funds, and not kept them idle.

b. Margin money of Rs. 328.93 crores received by the company in its bank accounts were reflected under various asset heads in the financial statements for the year ended 31st March, 2012.

c. The amount of settlement guarantee fund was not material and thus not disclosed separately in the financial statements.

d. There is no evidence of settlement defaults and claims having a negative impact on the liability. Neither assets nor liabilities have been understated. Nor is the profit been impacted by this. Adequate diligence to trade the margin money received. No misutilization of the margin has been pointed out.

27.2 **Findings of the Committee on Charge 3:**

The Committee in view of findings that they heard on merits noted that the settlement fund was received in the form of Bank Deposits, FDs, Cash etc. and should have been deployed in the same manner as in the case of liquid assets. However, SGF was diverted to unrelated assets against the bye-laws of the exchange. It was observed that despite the amount of margin money being huge and material, no disclosure, whatsoever, of such a significant policy of NSEL was brought out in the Notes to Account. Further, the Respondents also failed to disclose the basis on which the margin money was being invested by NSEL. It is submitted that disclosure of breakup of

Settlement Fund and policy relating to investment of margin money are necessary for true and fair view of the financial statements.

27.2.1 The Committee observed that the settlement fund of Rs 360.60 crores being a material amount was required to have been disclosed separately. It is observed that in the bye laws of NSEL there is no requirement of Settlement Fund. Further, the Respondents in his written statement also admitted that there was no specific guideline on investment of margin balance i.e. there was no policy of NSEL for investment of margin money and thus, the policy adopted by the Company should have been specifically brought out in the Notes to Accounts to convey a correct picture as regards the basis on which the margin money was being invested.

27.2.2 The Committee further noted that requirement of maintenance of Settlement Guarantee Fund (SGF) is given in Clause 12 of the Bye-laws of the Company which states as follows:

*"**12. Settlement Guarantee Fund***

*12.1 The Exchange to maintain Settlement Guarantee Fund*

*12.1.1 The Exchange shall maintain Settlement Guarantee Fund in respect of different commodity segments of the Exchange for such purpose, as may be prescribed by the Relevant Authority from time to time.*

*12.1.2 .....*

***12.1.3 The minimum corpus of the Settlement Guarantee Fund to be ensured before commencement of trading will be Rs. 1 crore, which will be suitably increased from time to time, as the Board may decide.***

*"12.2 **Contribution to and Deposit with Settlement Guarantee Fund***

*12.2.1 Each member shall be required to contribute to provide a minimum security deposit, as may be determined by the Relevant Authority from time to time, to the relevant Settlement Guarantee Fund. The Settlement Guarantee Fund shall be held by the Exchange. The Money in the Settlement Guarantee Fund shall be applied in the manner, as may be provided in these Bye-Laws, Rules, Business Rules and Regulations of the Exchange and notices and orders issued thereunder from time to time.*

*..."*

*12.3 The Relevant Authority may, in its discretion, permit a member to contribute to or provide the deposit to be maintained with the Settlement Guarantee Fund, in the form of either cash, fixed deposit receipts, bank guarantees or in such other form or method and subject to such terms and conditions, as may be specified by the Relevant Authority from time to time.*

*12.6 **Administration and Utilisation of Settlement Guarantee Fund***

*12.6.1 The Settlement Guarantee Fund may be utilised for such purposes, as may be provided in these Bye-laws and Regulations and subject to such conditions as the Relevant Authority may prescribe from time to time, which may include:*

*a) defraying the expenses of creation and maintenance of Settlement Guarantee Fund,*

*b) temporary application of SGF to meet shortfalls and deficiencies arising out of the clearing and settlement obligations of clearing members in respect of such transactions, as may be provided in these Bye-laws, Rules, Business Rules and Regulations of the exchange in force from time to time,*

c) *payment of premium on insurance cover(s) which the Relevant Authority may take from time to time, and/or for creating a default reserve fund by transferring a specified amount every year, as may be decided by the Relevant Authority from time to time,*

d) *meeting any loss or liability of the exchange arising out of clearing and settlement operations of such transactions as may be provided in these Bye-laws, Rules, Business Rules and Regulations of the exchange in force from time to time,*

e) *repayment of the balance amount to the member pursuant to the provisions regarding the repayment of deposits after meeting all obligations under the Bye-laws, Rules, Business Rules and Regulations of the exchange, when such member ceases to be a member, and*

f) *any other purpose, as may be specified by the Relevant Authority, from time to time.*

*12.6.2 The Exchange shall have full power and authority to* ***pledge, re-pledge, hypothecate, transfer, create an interest in, or assign*** *any or all of the (a) cash or fixed deposits receipts of SGF (b) securities or other instruments in which the cash corpus of SGF is invested, and (c) or bank guarantees or any other instrument issued on behalf of a clearing member in favour of the Exchange towards deposit to the SGF."*

27.2.3 From the above, the Committee noted that it was clear that there is a requirement for maintaining a settlement guarantee fund in respect of different commodity segments of the Exchange for such purposes, as may be prescribed by the relevant authority from time to time. Further, the amount of the deposit or contribution to be made by each member to the relevant Settlement Guarantee Fund is specified by the relevant authority and the minimum amount in SGF should not be less than Rs 1 crore which may be increased. However the amount maintained in SGF is less than the specified amount.

27.2.4 The Committee also noted that, as per Clause 12.3 of the Bye-laws, contributions to the Settlement Guarantee Fund were to be made in the form of either cash deposit receipts, bank guarantees, or in such other form as may be specified by the relevant authority. However, the Respondents have not disclosed the break-up of the investment of SGF in financial statements which should have been specifically brought out in the Notes to Accounts to convey a better picture. Further the Company has invested the amount of Rs 360.60 crores (approx.) in loans and advances, procurement advances, etc. which is not allowed as per bye-laws. Although, the Respondents has obtained the 100% confirmation from the parties to whom the advances were given but since it is against the provisions, hence it is the duty of the Respondents to report the same in their report. It is further noted that there is ongoing fraud in NSEL which is also in the common knowledge. Hence, the Respondents were required to put an extra effort before coming to any conclusion however the Respondents choose not to report about the same. **Thus the Respondents are grossly negligent in conduct of their professional duties and are Guilty on this charge of professional misconduct** falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

28. **Charge 4**

The Committee noted that fourth charge relates to short insurance. The annual report shows that a partly amount of Rs.14.76 lakhs is paid towards insurance while the average commodities lying at warehouse during the Fin. Year 2011-12 amounted to Rs.1,000 to Rs.1,500 crores. It seems serious deficiency of under insurance, causing the serious risk to the Exchange as well as Investors. It was the duty of the auditor to verify the same and particularly when Exchange performs the business and stake of small investors are involved. It is sheer negligence on the part of the Respondents as auditor to not perform the basic functions of audit.

28.1 **Submissions of the Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents have submitted that the statutory auditors are not expected to and cannot, comment on business strategies of a Company.

b. Whether to take insurance cover or not is decision of the proprietary and does not require auditor comment or consideration.

c. That NSEL had no obligation to insure the goods lying in the warehouses since they did not belong to NSEL and is not a business risk of NSEL that could have created a risk of material misstatements in the financial statements nor the misstatements of an assertion risk as that term is explained in SA 315.

d. The risks against the checks and balances that exist in the likelihood of a risk resulting into a financial implication but to the extent that doesn't belongs to NSEL and they are not required to be responsible for it, which is basically somebody else's asset.

28.2 **Findings of the Committee on Charge 4:**

The Committee in view of findings that they heard on merits noted that under-insurance is an important business risk that can have severe consequence for a business including finding itself severely out of pocket. The said risk is material and non-reporting of the same can result in risks of material mis-statement and, hence, the Respondents ought to have reported or commented on the same in his audit report.

28.2.1 The Committee further noted that the provisions of SA-315 "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment", Para 11 reads as under:-

*"11. The auditor shall obtain an understanding of the following:*

*(a) Relevant industry, regulatory, and other external factors including the applicable financial reporting framework. (Ref: Para. A17-A22)*

*(b) The nature of the entity, including:*

*(i) its operations;*

*(ii) its ownership and governance structures;*

*(iii) the types of investments that the entity is making and plans to make, including investments in special-purpose entities; and*

*(iv) the way that the entity is structured and how it is financed; to enable the auditor to understand the classes of transactions, account balances, and disclosures to be expected in the financial statements. (Ref: Para. A23-A27)*

*(c) The entity's selection and application of accounting policies, including the reasons for changes thereto. The auditor shall evaluate whether the entity's accounting policies are appropriate for its business and consistent with the applicable financial reporting framework and accounting policies used in the relevant industry. (Ref: Para. A28)*

*(d) The entity's objectives and strategies, and those related business risks that may result in risks of material misstatement. (Ref: Para. A29-A35)*

*(e) The measurement and review of the entity's financial performance. (Ref: Para. A36-A41)"*

28.2.2 The Committee noted from above provisions that it is the responsibility of the auditor to obtain an understanding of the entity and identify the risk involved which may result in risks of material misstatement. In the present case, it is seen that NSEL offered services like warehousing and collateral management services to market participants and market participants are doing transactions depending upon NSEL as they have confidence on them. The Committee further noted that NSEL has not taken insurance cover of the commodities lying at its warehouse amounting to Rs. 1000 crores to Rs. 1500 crores. However, the dependency of market participants casts responsibility on NSEL

to take care of the goods of its clients and there should be an insurance cover upto a certain limit. It can also be seen from the example of a courier company who is responsible for shipping of goods of third party from one place to another place. If the goods are lost or some mishappening occurs in transit then the courier company will be held responsible. In a similar way, NSEL is held responsible for goods lying at its warehouse.

28.2.3 The Committee noted that on a combined reading of the requirement of para 11 of SA 315 with the defence provided by the Respondents, it is clear that the Respondents have not spelt out whether any analysis of the business risks was undertaken by them and if so, their assessment of the same and its impact on the financial statement of the Company.

28.2.4 The Committee observed that there should be an insurance cover however instead of qualifying the said misstatement they have shifted the liability on the management of NSEL. The Respondents has not quantified the amount of risk involved due to under insurance. They simply stated that since the asset belongs to somebody else hence NSEL is not required to review on the same. Thus they themselves accepted that they have not done any review of the risk involved in relation to goods of third party lying at warehouse of NSEL. Hence, the Respondents have not performed their duties in due diligence and are **being held Guilty on this charge of professional misconduct** falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

29. **Charge 5**

The Committee noted that the fifth charge relates to non-reporting of lack of proper internal control system. It is seen that as per point No. IV of Annexure to Auditor's Report (CARO) the auditor has stated that there are adequate internal control procedures commensurate with the size of the Company and the nature of its business, for the purchase of inventory and fixed assets and for the sale of

goods and services. However there is lack of proper internal control system in the Company.

29.1 **Submissions of the Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents have submitted that they have performed various procedures to check whether there is proper internal control system.
b. That they have read the report of the internal auditor but not relied on and they have performed their own procedures.
c. They have done their work independently and requested the Committee to test the work done by them instead of simply relying on the assumption that nothing has been done by them.

29.2 **Findings of the Committee on Charge 5:**

The Committee in view of findings that they heard on merits noted that the Respondents have placed on record the procedures followed by them in their audit process and submits that they have not relied on internal auditor report instead performed their own procedures independently. The Committee noted that the internal auditor in his report has raised alarm for some areas. However, the Respondents has not raised any such alarm and issued a clean audit report despite the fact that they themselves accepted that they have read the report of internal auditor but the issuance of clean audit report shows lack of due diligence by them.

29.2.1 Further with regard to sample size, for warehouse inward receipt, it is noted by the Committee with respect to FY 2011-12 that from HDFC Bank Statement given in Annexure 19 as produced on record by the Respondents, the following is observed:

i. For the month of April, 2011, there were 414 entries in the single month. Out of these, 9 entries were related to N.K. Protein Ltd i.e. large member which 2.17% of total sample size.

ii. For the month of May, 2011, it was observed that the statement of bank runs into 22 pages covering 505 entries. However, the Respondents did sampling only for one date of May month i.e. 10 May and only 23 entries has been marked as sample.

iii. For the month of June, 2011, it is observed that out of 507 entries, only 19 entries has been marked as sample and 15 entries was related to only one date i.e. 8 June, 2011.

29.2.2 With regard to sample size of margin accounts, it is noted that the Respondents has selected top 7 members whereas in selecting sample, he selected 10 entries for N.K. Protein Ltd. only. With regard to settlement of transactions, it is observed that the Respondents had selected 22 days for large member's transactions. The details of which is given below:

| S.No. | Month | Number of days per month |
|---|---|---|
| 1. | April | Nil |
| 2. | May | 1 |
| 3. | June | 1 |
| 4. | July | 1 |
| 5. | August | 5 |
| 6. | September | 3 |
| 7. | October | 1 |
| 8. | November | 3 |
| 9. | December | 2 |
| 10. | January | 2 |
| 11. | February | 1 |
| 12. | March | 2 |

From the above, it is noted that in the month of April, no date was selected. Moreover, in the month of August only, 5 dates were selected. It is viewed that

no basis for selection of the dates has been provided, accordingly, it is difficult to see whether the dates selected by the Respondents is appropriate or not.

29.2.3 With regard to sample size selected for subsequent settlements of trades, the Respondents stated that he had tested samples on random basis. However, while reviewing the documents submitted by him, he had reviewed only April month for N.K. Protein Ltd. only with clearance on 4th May, 2012.

29.2.4 It is noted that relevant standard on Sampling, SA 530, states as under:

*"When designing an audit sample, the auditor shall consider the purpose of the audit procedure and the characteristics of the population from which the sample will be drawn. (Ref: Para. A4-A9)*

*The auditor shall determine a sample size sufficient to reduce sampling risk to an acceptably low level. (Ref: Para. A10-A11)*

*The auditor shall select items for the sample in such a way that each sampling unit in the population has a chance of selection. (Ref: Para. A12-A13)"*

*The auditor shall perform audit procedures, appropriate to the purpose, on each item selected. If the audit procedure is not applicable to the selected item, the auditor shall perform the procedure on a replacement item. (Ref: Para. A14)*

*If the auditor is unable to apply the designed audit procedures, or suitable alternative procedures, to a selected item, the auditor shall treat that item as a deviation from the prescribed control, in the case of tests of controls, or a misstatement, in the case of tests of details. (Ref: Para. A15-A16)"*

The above mentioned paras of SA 530 sufficiently requires auditor to select the sample which is representative of the characteristics of whole population and sufficient to reduce the sampling risk to an acceptably low level. However, as per the submissions of the Respondents it is noted that the sample selected by them

were insufficient and inadequate and are afterthought. The Respondents had submitted that they had applied adequate procedures to verify the transactions.

However it is noted that the Respondents in the present case with respect to warehouse inward receipt has selected only one day in almost every month or data related to only one Company (few examples of which are mentioned in Para 29.5.1 above) which shows that the sample size selected by the Respondents were not adequate. Also with respect to margin accounts, the Respondents had selected entries of only one member which might not include the characteristic of all the entries of other members. Further with respect to settlement of transactions also, it is noted that the sample size selected by the Respondents were not distributed equally due to which sample from each unit is not selected. Further with respect to settlement of trades, it is noted that the Respondents had reviewed data for the month of April only which shows that the sample selected does not cover the characteristics of all entries/transactions.

In view of above it is noted that the sample size selected by the Respondents were not as per the relevant standard on auditing. Also the samples selected by them were neither representative of the characteristics of whole population nor sufficient to reduce the sampling risk to an acceptably low level. They failed to point out any discrepancies in the financial statements even after perusing the internal audit report wherein various discrepancies are pointed out and issued clean audit report. This resulted in the fraud of around Rs 5600 crore was done by NSEL. In the instant case seeing the irregularities pointed out by the Internal Auditor and NSEL Investors Forum, it is noted that the Respondents' selection of sample was not enough to cover the whole relevant population to point out any single discrepancies regarding the operations of the Company

29.2.5 The Committee further noted from the charge related to short insurance that the Respondents have not performed their work due diligently and failed to report about lack of proper internal control as NSEL had not taken the insurance cover for the goods worth of Rs 1000 crores to Rs 1500 crores lying at their

warehouse and also saying that since the goods belongs to third parties, they are not responsible for the same. However involvement of such huge amount needs to be given special attention as it impacts the financial position of the Company. Further the charge related to deviation of funds of settlement guarantee fund also substantiates the lack of professionalism on part of Respondents. Thus, on overall consideration of the charges against the Respondents, it was noted that they have failed to report on lack of proper internal control system in NSEL.

29.2.6 The Committee noted that there was a lack of due diligence and gross negligence on the part of the Respondents. It is noted that if the Respondents have employed appropriate procedures to obtain reasonable assurances about the sufficacy and efficiency of internal control system in place, they would have come to know that internal control procedure/system are not commensurate with the size and nature of the business. Further, the Respondents have failed to obtain sufficient information necessary for expression of an opinion as per reporting requirement under Para 4 (iv) of Appendix-I of CARO, 2003. **Accordingly, the Respondents are being held Guilty of professional misconduct for the said charge** falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

30. **Charge 6**

The Committee noted that the sixth charge relates to non-disclosure of contingent liabilities and commitments. It was alleged that the auditor should have gone through Bye-Laws of NSEL. In the notes, the value of the contracts outstanding for which exchange is counter party and the value of stock held by the exchange in the warehouse against the counter party liability should have been disclosed. However it was seen that no note has been given on the contingent liability /commitment. Since this is very significant and a major commitment, non–disclosure of the same seriously distorts the true and fair nature of the financial statement and this become further important where the insurance cover was not adequately taken.

30.1 **Submissions of the Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents have submitted that they drew attention to the extract of Clauses 3.7, 5.17, 5.21 and 5.26 and 7.9, 9.6, 12.14 from the Bye Laws of NSEL. The Respondents also highlighted para no.8.8.7 of the Guidance Note on the revised Schedule VI and submits that the question of disclosure either as a contingency or a commitment does not arise. Further no other exchange discloses total open positions as a "Contingent Liability" in their financial statements. Since nothing is specified in GAAP on such matters, generally accepted practices of other entities operating in the same industry become accepted accounting and disclosure practices.

30.2 The Director (Discipline) had held the Respondents not guilty for this charge on the grounds that no such disclosure is required as per byelaws of the exchange, requirements of AS 29 and the revised Schedule VI. However the Committee noted that since it is the very basis of NSEL scam hence requires further investigation.

30.3 **Findings of the Committee on Charge 6:**

The Committee in view of findings that they heard on merits noted that *Clause 5.26 of Bye laws* of NSEL states as under:

*"The relevant authority of the Exchange may specify from time to time the types of transactions in specific commodity or commodities with regard to which the Exchange shall act as a legal counter party and the transactions that may be excluded from this purposes……."*

*"Provided that if on an investigation by the Exchange, the Exchange concludes that either all the transactions or part thereof in any commodity are found to have been executed on "NEST" or any other trading system of the Exchange in a fraudulent manner and /or / are done as financial transaction or structured deals and / or with a design to defraud settlement guarantee fund, the relevant authority of the Exchange shall have absolute authority and discretion to withdraw itself as a legal counterparty to any transaction".*

*"Provided further that where the Relevant Authority decides to exercise its discretion to withdraw itself as a legal counter party to transactions, either in full or part, and/or either from both sides or single side of the transaction, it shall afford an opportunity of being heard to all the parties affected or likely to be affected by such decision. The decision taken by the Relevant Authority thereafter shall come into force forthwith and shall be final and binding on all the parties concerned, including the clients."*

Further paragraph 8.8.7 of the Guidance Note on the revised Schedule VI states as follows:-

*"8.8.7 Contingent liabilities and commitments:-*

*(i) Contingent liabilities shall be classified as:-*

*(a) Claims against the company not acknowledged as debt.*

*(b) Debts*

*(c) Other money which the Company is contingent liable.*

*(ii) Commitments shall be classified as:-*

*(a) Estimated amount of contracts remaining to be executed on capital account and not provided for;*

*(b) Uncalled Liability on shares and other investments partly paid*

*(c) Other Commitments (specified nature)"*

30.3.1 The Committee noted that as per bye laws, if on an investigation the exchange concludes that any transactions executed are found to be in a fraudulent manner, the relevant authority of the exchange have absolute authority and discretion to withdraw itself as a legal counter party to any transaction after giving an opportunity of being heard to all the parties affected by the decision and NSEL is required to disclose as regards the value of contracts outstanding for which the exchange shall act as a legal counter party and the transactions which may be excluded from the purposes. However, it is seen that no such disclosure is made. Also, the Respondents have not denied that the NSEL is not a counter party to the transactions held. The Committee further noted that DCA in exercise of powers conferred to it under section 27 of the FCRA vide notification no. S. O. 906(E) dated 5th June, 2007 had exempted all forward contracts of one day duration for the sale and purchase of commodities traded on the NSEL, from operation of the provisions of the said Act subject to the following conditions, namely:-

a) No short sale by members of the Exchange shall be allowed;
b) All outstanding positions of the trade at the end of the day shall result in delivery;
c) The National Spot Exchange Ltd shall organize spot trading subject to regulation by the authorities regulating spot trade in the areas where such trading takes place;
d) All information or returns relating to the trade as and when asked for shall be provided to the Central Government or its designated agency;
e) The Central Government reserves the right to impose additional conditions from time to time as it may deem necessary and
f) In case of exigencies, the exemption will be withdrawn without assigning any reason in public interest.

However, after analysing the trade data received from NSEL, the FMC identified the following issues relating to contracts traded on NSEL and sought clarifications from NSEL on 22 February, 2012.

a) As per the trade data submitted by NSEL, it was observed that 55 contracts offered for trade on NSEL were with settlement periods exceeding 11 days and all such contracts traded on NSEL were in violation of provisions of FCRA.

b) The condition of 'no short sale by members of the exchange shall be allowed' was not being met by NSEL.

The FMC requested the DCA to take necessary action regarding the above violations. DCA vide its letter dated 27 April 2012 directed NSEL to explain as to why action should not be initiated against them for violation of the conditions of the notification dated 5th June, 2007. In response to the above, NSEL submitted a reply vide their letter dated 29 May, 2012 and after that DCA vide its letter dated 31st May, 2012, sought comments of the Commission on the NSEL letter dated 29 May, 2012.

Thus from the above it is seen that some initial proceedings were on going against NSEL before the date of signing of financial statements by the Respondents i.e. 21st May, 2012 which is impacting the financial position of the Company and has to be shown as contingent liability in financial statements as per paragraph 8.8.7 of the Guidance Note on the revised Schedule VI however the Respondents does not care to disclose the same in their audit report for the period despite of having knowledge of the same. **Accordingly, the Respondents are being held Guilty of professional misconduct for the said charge** falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

31. **Charge 7**

The Committee noted that seventh charge relates to non-reporting of ongoing fraud in NSEL. It is alleged that as per Auditor's report point no. XXI, the Respondents reported that no fraud on or by the Company has been noticed or reported during the course of the Respondents audit. However, NSEL has

defaulted in payment to its investors and it is established that commodities were not physically available and it has resulted in fraud perpetrated by the Company and gross negligence on the part of the auditor of the Company. The Respondents have not complied with the Standard of Auditing which has led to misstatement in the financial statements that could have been discovered by the Respondents.

31.1 **Submissions of the Respondents**

The crux of the submissions of the Respondents with respect to the said charge is as under:

a. The Respondents had drawn attention to Paragraph 4 (xxi) of CARO which required the auditor to report on

*"Whether any fraud on or by the Company has been noticed or reported during the year. If yes, the nature and the amount involved is to be indicated"*

In this connection, the Respondents drew reference to paragraph 77(a) of the Statement on the Companies (Auditor's Report) Order 2003, issued by the ICAI, which stated *The scope of auditor's inquiry under this clause is restricted to frauds, noticed or reported' during the year. The use of the words* ***"noticed or reported" indicates that the management of the company should have the knowledge about the frauds",*** *(emphasis supplied) on the Company or by the Company that have occurred during the period covered by the Auditor's report.*

b. That there is no evidence that media reports were available.

c. As per guidance note on CARO, it was the management who should have brought it to auditor's attention about the fraud in Company however no such fraud has been brought to attention by management.

d. Infact they have given a representation that there were no ongoing fraud in NSEL. Inspite of that they have ran a complete fraud assessment for identifying the fraud.

31.2 **Findings of the Committee on Charge 7**

The Committee in this regard noted that, on perusal of the DCA notification, it is observed that in early 2012 the FMC was appointed as 'designated agency' to collect data from NSEL and protect investors' interest. On 27th April 2012, based on the data provided by the Forward Markets Commission (India), the Ministry of Consumer affairs issued a show cause notice to NSEL that it was violating the conditions of 2007 exemption like 'no short sale', 'no stock verification mechanism' and ' conducting trades beyond 11 days'.

Further the NSEL scam is estimated to be a Rs. 5600 crore fraud as per Complainant that came out to light after the National Spot Exchange failed to pay its investors in commodity pair contracts after 31 July 2013. So from early 2012- July 2013 the FMC knew about fraudulent NTSD contracts rampantly being conducted without registration under section 14A-14B of FCRA but for reasons unknown did not act. NSEL kept operating outside the realms of law and in March 2012, it notched up a Rs. 45,500 crore turnover, the highest ever monthly average.

31.2.1 The Committee further noted that although, the newspapers reports are treated as hearsay evidence, yet, looking into the fact that Show cause notice had been issued to NSEL as early as in April 2012 and the audit report had been signed by the Respondents on 21st May, 2012 and the Respondents have not brought on record any documentary evidence to show the checks carried out by them after the Balance Sheet date to counter such claims being made in the newspaper reports. Thus there were sufficient reasons to raise suspicion in the mind of the Respondents so as to thoroughly check/investigate into the affairs of NSEL before signing their report for the Financial Year 2011-12. However the Respondents relied on management's representation letter that no fraud is noticed and choose not to report in their report about the on-going fraud. **Accordingly, the Respondents are being held Guilty of professional misconduct for this charge** also falling within

the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

32. Keeping in view of above charges, the Committee noted that audited financial statements have an extremely high degree of reliability and validity in comparison with unaudited financial statements. The auditor should exercise his professional judgment and maintain professional skepticism throughout the audit. As per the requirements of Companies Act, 1956, the auditor is responsible for preparing an audit report based on the financial statements of the company and should be in accordance with the relevant laws. He must ensure that the financial statements comply with the relevant provisions of the Companies Act 1956, relevant Accounting Standards etc. In addition to this, it is imperative that he ensures that the entity's financial statements depict a true and fair view of the company's financial position. However, the Committee is of the view that in the extant case, the auditor has neither applied his professional judgment while giving his opinion on true and fair view of the financial statements of the Company nor complied with the requirements of the Standard on Auditing (SAs) including SA 240 wherein he must plan and perform his audit procedures to address the risk of material misstatement due to fraud as well as SA 500 which requires that the auditor should obtain sufficient appropriate evidence to able to draw reasonable conclusions on which the audit opinion is formed. Accordingly, the Committee noted that the Respondents were grossly negligent in conduct of their duties as well as failed to obtain sufficient information for expressing their opinion and therefore holds the Respondents Guilty of professional misconduct falling within the meaning of Items (7) and (8) of Part I of Second Schedule to the Chartered Accountants Act, 1949.

## CONCLUSION

33 In view of the above observations, considering the submissions of the Respondents and documents on record, the Committee held the Respondents

**GUILTY** of Professional Misconduct falling within the meaning of Item (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949.

**SD/-**
**(CA. RANJEET KUMAR AGARWAL)**
**PRESIDING OFFICER**

**SD/-**
**(MRS RANI NAIR, I.R.S. RETD.)**
**GOVERNMENT NOMINEE**

**SD/-**
**(SHRI ARUN KUMAR, IAS, RETD.)**
**GOVERNMENT NOMINEE**

**SD/-**
**(CA. SANJAY KUMAR AGARWAL)**
**MEMBER**

**SD/-**
**(CA. SRIDHAR MUPPALA)**
**MEMBER**

**DATE: 07TH FEBRUARY, 2024**

**PLACE: NEW DELHI**

प्रमाणित सत्य प्रतिलिपि/Certified true copy

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