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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% *Date of Decision : August 11, 2016*

+ **CHAT.A.REF.1/2012**

COUNCIL OF INSTT OF CHARTERED ACC
OF INDIA

.....Petitioner

Represented by: Mr.Rakesh Aggarwal, Advocate with
Mr.Pulkit Aggarwal, Advocate

versus

UMA SHANKAR JHA & ANR.

..... Respondents

Represented by: None

CORAM:

HON'BLE MR. JUSTICE PRADEEP NANDRAJOG

HON'BLE MS. JUSTICE PRATIBHA RANI

PRADEEP NANDRAJOG, J. (Oral)

1. This is a reference under sub-Section 5 of Section 21 of the Chartered Accountants Act, 1949. It has reached for hearing today. Mr.Rakesh Aggarwal Advocate and Mr.Pulkit Aggarwal Advocate have appeared for the Institute of Chartered Accountants. None has appeared for Sh.Uma Shankar Jha, the Chartered Accountant who has been indicted.

2. We have heard Sh.Rakesh Aggarwal who has very ably and painstakingly taken us through the record culminating in the report of the Disciplinary Committee constituted to look into a complaint dated July 05, 2005 lodged with the Institute of Chartered Accountants by the Assistant

General Manager (Inspection) of the Punjab and Sindh Bank Ltd.

3. M/s.J.S.Bedi and Co., Chartered Accountants of which Sh.U.S.Jha was a partner/member, he being a Chartered Accountant, were appointed concurrent auditors to audit the account of the Branch of Punjab and Sindh Bank New Delhi at Chandani Chowk for the period July 01, 2003 to June 30, 2004. As per the terms of appointment the audit spanned the entire working of the branch and shortcomings observed to be reported to the Branch Manager in the form of short notes for necessary rectification. If a fraud, fraudulent activity or foul play was noticed or detected it was to be reported to the General Manager (Vigilance) as also to the Zonal Inspectorate and the General Manager as well. Guidelines issued for the concurrent audit required to check the new accounts opened and particularly the current accounts and see whether the operations therein were unusual. To verify that the loans and advances were duly sanctioned as per guidelines of the bank. To verify the securities and documents received and in particular whether they were entered in the register. To check reconciliation of entries in the suspense accounts. To report any noticeable unauthorized use of discretionary powers. To report whether users had been made aware of the confidentiality of passwords. It was specifically brought to the notice of the auditors that recently a fraud allegedly committed by a staff member had been reported by the branch and a special audit conducted by the bank revealed that the fraudulent activities had continued to take place. The indictment was for carrying out the audit negligently while working as the concurrent auditors in not detecting fraudulent transactions details whereof were enclosed with the complaint received.

4. The respondent admitted that the firm J.S.Bedi & Co. was charged with the concurrent audit for the period in question and that it had carried out the concurrent audit under his supervision but denied any fraud perpetrated for the period of the audit. But surprisingly it was also simultaneously pleaded that the purported frauds began in July, 2002 and continued till April, 2005 and went undetected. A defence wherefrom we can only gather that the respondent intended to highlight that the frauds were of a kind which could not be detected during routine audits. Unfortunately we have no assistance from the side of the respondent and therefore do not have the benefit of what was intended to be said by the respondent because in the same breath it is pleaded that there was no fraud committed for the period covered in the audit and in the same breath it is pleaded that the fraud commenced much prior to the period of the audit and continued a little beyond.

5. The respondent also pleaded that a subsequent special audit report which unearthed the fraud had acknowledged that there was no control on the branch by the branch incharge and that the Chief Manager and the Senior Manager perpetrated the fraud in a manner that a normal audit could not detect the same. The respondent also highlighted the observations of the special audit report that vouchers were prepared to falsify certain entries. The respondent also highlighted that the special audit report brought out that most of the fraudulent entries pertained to the period pre and post July 01, 2003 to June 30, 2004. It was pointed out that the periods spanning the fraud was four financial years and neither year routine audit could detect the same. It was followed by an explanation, with reference to the vouchers and

documents of the bank for the period in question, as to how during normal audit the frauds could not be detected.

6. The findings by the Disciplinary Committee are that the respondent may be right that the manner in which the fraud was committed required an indepth investigation but opined that objective of a concurrent auditor was to keep a check on the general audit and qua the transactions which were carried out in the newly opened accounts the respondent had to be more vigilant because the term of the audit had brought to the notice of the auditors that recently a fraud allegedly committed by a staff member had been detected and that while carrying out the audit newly opened accounts should be kept under strict scrutiny. The committee opined that with a little more diligence the concurrent auditors could have unearthed the modus operandi. The conclusion is that the respondent would be guilty of professional misconduct falling within the meaning of clause (5), (6) and (7) of Part I of Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949.

7. The report was considered by the Council at its meetings held on January 16 and 17, 2011. After deliberating on the report and the respondent's response, the Council opined as under:-

“8.2 The Council after deliberations in this matter took note of the fact that one of the basic objective of concurrent audit is to keep the current routine work under continuous check and to ensure adherence to the system and procedures from the view point of internal control and statutory compliance. The Council further observed that in the instant matter the entries/transactions emanating out of the fraud perpetrated by a senior level Branch Manager remained undetected for nearly

three years escaping attention of many officers and also the various auditors involved during the period of three years. The Respondent was only one of the three concurrent auditors involved with the Bank Branch in these three years period beginning from July 1st 2003 to June 30th 2004 whereas the fraudulent activities as per the Respondent had started a year before he had taken over as concurrent auditor and continued even after the Respondent's term.

8.3 The Council in this context deliberated upon the applicability of Clauses (5) and (6) of Part I of Second Schedule to the Chartered Accountants Act, 1949 and noted in this regard that Clause (5) of Part I of Second Schedule envisages the non disclosure of a material fact known to the auditor which is not disclosed in a Financial Statement but disclosure of which is necessary to make the Financial Statement not misleading and Clause (6) of Part I of the Second Schedule envisages the non-reporting of a material misstatement known to the auditor to appear in a Financial Statement with which he is concerned in a professional capacity. However, the Council keeping in view the scope of work assigned to a concurrent auditor and also in the instant matter wherein it was almost impossible to detect the fraud committed over a period of time even by preceding and successive auditors and/or during inspection by the senior officer of Bank and inspection audit done by RBI, was of the view that in the instant matter where undisclosed material fact or unreported material misstatement had emanated as a result of the fraud committed by an employee of the Bank in the said Branch, the same cannot be expected to be within the knowledge of the Respondent and certainly there was no mala-fide intention on his part. Hence, the Council held the view that the Respondent cannot be held guilty of any misconduct under these Clauses (5) and (6) of Part I of the Second Schedule to the Chartered Accountants Act, 1949. The Council, however while noting the terms of reference of the Respondent's appointment was of the further view that although the fraudulent

transactions were carried out in the Branch wherein the Respondent had acted as a concurrent auditor but had the Respondent while carrying out his professional duties acted with more care and caution, such modus operandi/or at least certain transactional entries would have been disclosed/unearthed by him in course of his routine cross-checking particularly wherein the terms of reference very well covered checking of such kind of transactions also. The Council, therefore, was thus of the view that the Respondent had basically acted negligently to some extent in performing his duties as a concurrent auditor. The Council thus accepted the Report of the Disciplinary Committee to the extent the Respondent was held guilty of professional misconduct falling within the meaning of Clause 97) of Part I of the Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949.

9. Thus, on consideration of the Report of the Disciplinary Committee alongwith the Written Representation dated 11th January, 2011 received from the Respondent, and also the oral submissions made by the authorized representative(s) of the Complainant-Bank and the Respondent respectively before it, the Council decided as under:-

(a) to accept the report of the Disciplinary Committee to the extent wherein the Respondent was held guilty of professional misconduct falling within the meaning of Clause (7) of Part I of the Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949.

(b) NOT to accept the report of Disciplinary Committee to the extent wherein the Respondent was held guilty of professional misconduct falling within the meaning of Clauses (5) and (6) of Part I of the Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949.

10. In respect of (a) above, the Council also decided to

recommend to the High Court that the name of the Respondent be removed from the Register of Members for a period of one month.”

8. Having perused the documents we find that the Disciplinary Committee of the Council had accorded full opportunity to the respondent to present his case. All material documents have been considered by the Disciplinary Committee. The Council has very fairly considered the respondent's response to the report of the Disciplinary Committee and has re-appraised the material to conclude that whereas the respondent cannot be held guilty of professional misconduct within the meaning of clauses (5) and (6) of Part I of Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949, he would be guilty of professional misconduct within the meaning of clause (7) thereof.

9. Misconducts listed in (5), (6) and (7) of Part I of Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949 are as under:-

“(5) fails to disclose a material fact known to him which is not disclosed in a financial statement, but disclosure of which is necessary to make the financial statement not misleading;

(6) fails to report a material misstatement known to him to appear in a financial statement with which he is concerned in a professional capacity;

(7) is grossly negligent in the conduct of his professional duties;”

10. It is apparent that the misconduct contemplated by clauses (5) and (6) are severe vis-a-vis clause (7).

11. Taking into account said fact and that we are deciding the reference in the year 2016 we are of the opinion that accepting the decision of the Council at its meetings held on January 16 and 17, 2011 in so far it concludes the respondent guilty of misconduct contemplated by clause (7) of Part I of Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949, ends of justice would suffice if penalty of severe reprimand contemplated by Section 21(6)(c) of the Chartered Accountants Act, 1949 is inflicted upon the respondent.

12. Ordered accordingly.

(PRADEEP NANDRAJOG)
JUDGE

(PRATIBHA RANI)
JUDGE

AUGUST 11, 2016

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