



Corporate Supervision Department  
Company Law Division

Before Abid Hussain – Executive Director (Corporate Supervision Department)

*In the matter of*

**Karamat Chaudhry & Co., Chartered Accountants- Auditors of Abson Diffusion (Private)  
Limited**

Number and date of notice: CSD/ARN/260/2016-2778, dated January 21, 2016  
Date of hearing: March 10, 2016  
Present: Mr. Karamat Ali Chaudhry, the respondent

**ORDER**

**UNDER SECTION 260 READ WITH SECTIONS 255 AND 476 OF THE COMPANIES  
ORDINANCE, 1984**

This order shall dispose of the proceedings initiated against Mr. Karamat Ali (the “respondent”), proprietor of Karamat Chaudhri and Co., Chartered Accountant (the “Auditor”) in respect of audit of annual financial statement (the “Accounts”) of Abson Diffusion Private Limited (the “Company”) for the years ended June 30, 2013, 2014 and 2015. The proceedings were initiated through show cause notice (“SCN”) dated January 21, 2016 under the provisions of section 260 read with sections 255 and 476 of the Companies Ordinance 1984 (the “Ordinance”).

2. The brief facts of the case are that examination of Accounts of the Company for the year ended June 30, 2013, 2014 and 2015 filed under section 242 of the Ordinance revealed that the Company had remained inoperative with its business suspended over these years. As per the Accounts, during the years 2012 through to 2015, the balances of all the line items of the balance sheet and profit and loss account during these years have remained stagnant and no income or expense had been reported. The directors’ report attached to the Accounts 2013 stated as under:

*“Your company’s total sales are Nil due to the crises; we are trying our best to start the business as soon as possible after come over the crises of the company raised by the previous management.” (Emphasis Added)*

Due to the aforementioned circumstances during all those years, material uncertainty existed on a continuing basis regarding the Company’s ability to continue as a going concern. Moreover, following discrepancies were also observed in the respective Accounts:

- (i) Accounts 2013, 2014 and 2015: During the years under review, the Company did not charge any depreciation or impairment on its fixed assets including building, plant and



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machinery, furniture and fixture, office and other equipment etc. against its stated policy under note 2.2, 3.2.3 and 3.2.4 in respective Accounts, and in violation of para 3.14 of the Accounting and Financial Reporting Standards ("AFRS" for Medium Sized Entities ("MSEs")); and

- (ii) Accounts 2013: The Company did not attach 'Statement of Compliance' with the Accounts as per requirements of para 1.3 of the AFRS for MSEs applicable to the Company.

3. The auditor gave the audit reports on the Accounts as under:

**Accounts 2013:** A clean report has been given without any modification to the opinion or any emphasis of matter paragraphs regarding going concern uncertainties.

**Accounts 2014 & 2015:** The auditor qualified his opinion with following qualifications:

(i) **The going concern issue:**

- "We have not noted any movement in any account during the year under audit"
- "In our opinion the company is not a viable concern and is subject to going concern uncertainties."

- (ii) **Non-verification of Assets and Liabilities:** "No appropriate auditable evidence has been provided to verify the continued existence of all assets and liabilities as reflected in the annexed financial statements"

The auditors' report on respective Accounts was not in accordance with the requirements of the Ordinance, as highlighted below:

- a) The auditor did not highlight the aforesaid non-compliances with AFRS for MSEs in his reports to members on respective Accounts;
- b) The auditor in his report on Accounts 2013 was required to either express a qualified opinion or adverse opinion, as appropriate in accordance with para 20 of International Standards on Auditing of ("ISA") 570, due to existence of material uncertainty regarding Company's ability to continue as a going concern and no disclosures were given by the management. However, instead of expressing a qualified or adverse opinion, the auditor in his report on the Accounts 2013, gave an unmodified opinion and also did not highlight the going concern issue.

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c) Moreover, adverse opinion / disclaimer of opinion were warranted in auditor's report to members on Accounts 2014 and 2015, as under:

- An adverse opinion warranted, owing to auditor's disagreement regarding appropriateness of management's use of going concern assumption.
- A disclaimer of opinion was warranted due to unavailability of appropriate auditable evidence to verify the continued existence of all assets and liabilities of the Company, in line with para 9 and 10 of ISA 705.

However, the auditor only qualified his opinion with regard to those issues in contravention with the requirements of the ISAs.

d) The auditor stamped and signed the Accounts 2013, 2014 and 2015 in violation of the ICAP's Circular 4 of the 1999 and financial reporting framework which prohibit the auditors from signing or stamping the financial statements to avoid giving wrong impression that the auditor prepared the Accounts

4. Due to the aforementioned facts, the auditors' reports on the Account 2013, 2014 and 2015 of the Company were, prima facie, not in accordance with the requirements of section 255 of the Ordinance and ISA, as it was not appropriately modified. Hence, prima facie, it failed to bring out material facts about the affairs of the Company making the auditor liable for action under section 260 of the Ordinance. Consequently the SCN was issued to the respondent whereby he was called upon to show cause in writing within fourteen days as to why penal action may not be taken against him for the alleged violations.

5. Since no response to the SCN was received, a hearing in the matter was fixed on March 10, 2016. The respondent appeared for the hearing before the undersigned on the due date and made the following submissions:

- Only qualified report was issued based on our knowledge, belief and best judgment. In our opinion, the effect of going concern issue was not so material and pervasive which required an adverse opinion, or a disclaimer. However, through your letter we have

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become wiser, knowledgeable and enlightened on issuance of modified report wherever the issue of going concern is suspected. We do express our regret for the oversight.

- Neither management/stakeholders nor our firm have got any benefit or put to any disadvantage for non-compliance of the requirement as laid down in section 255 of the Ordinance. The management is prepared to withdraw the original Accounts and we have no objection to revise our report in the light of your observations. The observations have been noted and will be complied in letter and spirit in future.

It was further stated by the respondent during hearing that the Company is a small company; therefore, considering the fact and the submissions made by him, a lenient view may be taken.

6. Before proceeding further, it is necessary to advert to the relevant provisions of the Ordinance, the Rules and ISAs.

## ISA 570 – Going Concern

6. *The auditor's responsibility is to obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern. This responsibility exists even if the financial reporting framework used in the preparation of the financial statements does not include an explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern.*

10. *When performing risk assessment procedures as required by ISA 315 the auditor shall consider whether there are events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.*

11. *The auditor shall remain alert throughout the audit for audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. (Ref: Para. A6)*

12. *The auditor shall evaluate management's assessment of the entity's ability to continue as a going concern. (Ref: Para. A7–A9, A11–A12)*

16. *If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern, the auditor shall obtain sufficient appropriate audit evidence to determine whether or not a material uncertainty exists through performing additional audit procedures, including consideration of mitigating factors.*



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17. The auditor shall conclude whether, in the auditor's judgment, a material uncertainty exists related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.

18. If the auditor concludes that the use of the going concern assumption is appropriate in the circumstances but a material uncertainty exists, the auditor shall determine whether the financial statements:

(a) Adequately describe the principal events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and management's plans to deal with these events or conditions; and

(b) Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business. (Ref: Para. A20)

19. If adequate disclosure is made in the financial statements, the auditor shall express an unmodified opinion and include an Emphasis of Matter paragraph in the auditor's report to:

(a) Highlight the existence of a material uncertainty relating to the event or condition that may cast significant doubt on the entity's ability to continue as a going concern; and

(b) Draw attention to the note in the financial statements that discloses the matters set out in paragraph 18. (Ref: Para. A21–A22)

20. If adequate disclosure is not made in the financial statements, the auditor shall express a qualified opinion or adverse opinion, as appropriate, in accordance with ISA 705. The auditor shall state in the auditor's report that there is a material uncertainty that may cast significant doubt about the entity's ability to continue as a going concern. (Ref: Para. A23–A24)

21. if the financial statements have been prepared on a going concern basis but, in the auditor's judgment, management's use of the going concern assumption in the financial statements is inappropriate, the auditor shall express an adverse opinion. (Ref: Para. A25–A26)

22. if management is unwilling to make or extend its assessment when requested to do so by the auditor, the auditor shall consider the implications for the auditor's report. (Ref: Para. A27)

### ISA 705 -Modifications to the Opinion in the Independent Auditor's Report

**A2.** ISA 700 requires the auditor, in order to form an opinion on the financial statements, to conclude as to whether reasonable assurance has been obtained about whether the financial statements as a whole are free from material misstatement. This conclusion takes into account the auditor's evaluation of uncorrected misstatements, if any, on the financial statements in accordance with ISA 450.5

6. The auditor shall modify the opinion in the auditor's report when:

(a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or (Ref: Para. A2–A7)

(b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. (Ref: Para. A8–A12)"

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9. *The auditor shall disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.*

10. *The auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial statements due to the potential interaction of the uncertainties and their possible cumulative effect on the financial statements.*

Section 255 of the Ordinance prescribes powers and duties of the auditors and sub-section (3) of section 255 prescribes requirements, manner and content of auditors' report on the Accounts.

Rule 17 (A) of the Companies (General Provisions and Forms) Rules, 1985 (the "Rules") states that the auditors' report on the accounts and books of accounts and balance-sheet and profit and loss account of a company required by section 255 of the Ordinance shall be on a prescribed format contained in FORM 35-A, and the prescribed format, inter alia, contains the statement by the auditor that "*we conducted our audit in accordance with the auditing standards as applicable in Pakistan*"

Section 260 of the Ordinance states as under:

*"(1) If any auditor's report is made, or any document of the company is signed or authenticated otherwise than in conformity with the requirements of section 157, section 255 or section 257 or is otherwise untrue or fails to bring out material facts about the affairs of the company or matters to which it purports to relate, the auditor concerned and the person, if any, other than the auditor who signs the report or signs or authenticates the document, and in the case of a firm all partners of the firm, shall, if the default is wilful, be punishable with fine which may extend to one hundred thousand rupees.*

*(2) If the auditor's report to which sub-section (1) applies is made with the intent to profit such auditor or any other person or to put another person to a disadvantage or loss or for a material consideration, the auditor shall, in addition to the penalty provided by that sub-section, be punishable with imprisonment for a term which may extend to one year and with fine which may extend to one hundred thousand rupees."*

In terms of the Commission's notification SRO 1003 (I)/2015 dated October 15, 2015, the powers to adjudicate cases under section 260 of the Ordinance have been delegated to Executive Director (Corporate Supervision Department).

7. I have analyzed the facts of the case, the relevant provisions of the Ordinance, the Rules, requirements of ISAs and the arguments put forth by the respondent. My observations in this regard are as under:

a) A statutory auditor is bound to follow the requirements prescribed by the Ordinance, the

Rules and the ISAs and has to express an opinion remaining within the confines set by



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them. The ISAs contain objectives, requirements and application and other explanatory material that are designed to support the auditor in obtaining reasonable assurance. The ISAs require that the auditor exercise professional judgment and maintain professional skepticism throughout the planning and performance of the audit. In terms of the Ordinance and the ISAs it is auditor's duty to identify and assess risks of material misstatements, obtain sufficient appropriate evidence and form an opinion based on conclusions drawn from the audit evidence.

- b) The respondent gave an unmodified opinion in his audit report on Accounts 2013 despite the fact that there was material uncertainty about Company's ability to continue as a going concern, as its core business was suspended for past many years and there were no sales. The management failed to give any disclosure regarding going concern uncertainties. The respondent was, therefore, required to obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in preparation of the financial statements and to conclude whether there was a material uncertainty about the entity's ability to continue as a going concern. The respondent have failed to discharge his duties in this regard as he neither appeared to have carried out the assessment of going concern nor did he appropriately modify his opinion in his report on Accounts 2013.
- c) The respondent issued a qualified opinion in his report on the Accounts 2014 and 2015. As has been highlighted in the preceding paragraphs, as of Jun 30, 2014 and 2015, the Company had completely ceased its business and there was no operational income. There was material uncertainty about the Company's ability to continue as a going concern. Moreover, as qualified by the respondent in his report, he was not given the appropriate auditable evidence to verify the continued existence of all assets and liabilities as reflected in the Accounts 2014 and 2015. The going concern issue coupled with non-verification of continued existence of all assets and liabilities had material and pervasive effect on the Accounts of the Company. The Company failed to give any disclosure regarding going concern issue in Accounts 2014 and 2015. In view of these facts, an adverse opinion in line with requirements of para 21 of ISA 570 was warranted. With reference to non-verification of liabilities and assets, a disclaimer of opinion was warranted in line with para 9 of ISA 705, which states the auditor shall disclaim an opinion when the auditor is unable to obtain



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*sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive. However, the respondent only qualified his opinion instead and, therefore, has failed to discharge his duties appropriately.*

- d) Preparation of financial statements is responsibility of the management and it is auditor's responsibility to express an independent opinion on the financial statements. The respondent signed and stamped the Accounts 2013 and Accounts 2014. Signing and stamping of the financial statements by the auditor is prohibited to avoid a possible wrong impression that the same have been prepared by the auditor. The respondent has failed to comply with the requirement.

8. Before proceeding to decide the matter, I deem it necessary to make some observations on the role of auditor of a company. The duties and responsibilities of an auditor appointed by the shareholders under the law can best be understood if we look at the place of an auditor in the scheme of the company law. The capital required for the business of a company is contributed by its shareholders who may not necessarily be the persons managing the company. They elect directors and entrust the affairs of the company to them with responsibility that they will manage the company to shareholders' benefits. There is no such arrangement in place whereby the shareholders can have an independent view as to how the directors have managed the affairs of the company. The financial statements are the most important source of reliable information for the shareholders who make their investment decision based on such information. The financial statements not only show the financial position and performance of the company but also show the results of management's stewardship of resources entrusted to it. Therefore, correct reporting in the financial statements in line with applicable financial reporting framework is of utmost importance. The law, therefore, recognizing this situation, has provided for the appointment of auditors who shall be responsible to audit the books of account, documents and financial statements required by the law and make out a report on them at the end of each year. This being the only safeguard provided by law to the shareholders to ensure accountability of the management, put the auditors to a high level of accountability in case they fail to make out a report in accordance with the legal requirements. For these reasons, it is of utmost importance for the auditors to exercise due care and diligence in performing their duties and discharging their responsibilities and maintain a high level of trust and integrity at their end.

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9. For the foregoing reasons, I am of the view that the respondent in his audit reports to members on Company's Accounts for the years ended June 30, 2013, 2014 and 2015 failed to appropriately modify his opinion and, hence, has not discharged his duties under the law. However, considering the acquiescence of default by the respondent, his assurance for future compliance and in view of the fact that the Company is a small private limited concern, instead of imposing fine, I hereby conclude the proceedings with a stern warning to the respondent

**Abid Hussain**  
Executive Director (CSD)

**Announced:**  
April 12, 2016  
Islamabad