



Corporate Supervision Department  
Company Law Division

Before Tahir Mahmood – Commissioner (Company Law Division)

*In the matter of*

**Faisal Latif, Chartered Accountant - Auditor of Petrosin Ravi Industries Limited**

Number and date of notice: EMD/242/I/113/11-349 dated November 20, 2012  
Date of hearings: June 22, 2015  
Present: Mr. Faisal Latif, Mr. Imran Shafique

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. Faisal Latif, Chartered Accountant, (the "respondent") engagement partner in respect of audit of annual audited financial statements (the "Accounts") of Petrosin Ravi Industries Limited (the "Company") for the year ended June 30, 2010. The proceedings were initiated through show cause notice ("SCN") dated November 20, 2012 issued 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 the examination of the Accounts of the Company revealed that Tariq Ayub Anwar & Co. Chartered Accountants (the "Auditor") audited the accounts of the Company for the year ended June 30, 2010 and the respondent being the engagement partner gave an unmodified opinion thereon. It was observed that:

- i. The comparative figures of 'trade debtors' of Rs74,758,508 for the year 2009 were reclassified as 'other receivables from associated undertakings' of Rs71,131,623 and 'trade debtors' of Rs3,626,885; and
- ii. Disclosure of transactions with related parties given under note 28 did not reconcile with the balances appearing in the Accounts with respect to associated undertakings.

In response to the queries raised by the Commission on the aforesaid issues, the Company failed to satisfy the observations with documentary evidence. An inspection was ordered on October 4, 2011 under section 231 of the Ordinance to inspect the record, books of accounts, papers and statutory record of the Company. After having carried out the inspection, the inspection team of the Commission reported as under:



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- i. The Company was not able to provide proper justification with regard to the reclassification of the transaction with the associated undertaking. The only submission made was that the reclassification has been made on advice of the auditors and that the balances which are outstanding were usually classified as 'debtors' otherwise they were classified as 'due from associated undertaking'.
- ii. The balances of the ledger accounts of the related parties did not reconcile with those reported in the Accounts of the Company.
- iii. Sale of scrap by Petrosin Gas Pakistan (Pvt.) Limited amounting to Rs16,243,755 was not disclosed in note 28 on 'Transactions with related party'.

The inspection team also reported that following disclosures as required under the Fifth Schedule to the Ordinance and Accounting and the Financial Reporting Standard for MSEs and SSEs (the "AFRS") were not made:

- i. Names of trade debtors-related parties required under clause 5B(ii) of Fifth Schedule;
- ii. The interest receivable from the associated undertaking amounting to Rs190,668/- disclosing names of the associated undertaking as required under clause 5B(ii) of Fifth Schedule;
- iii. Disclosure on remuneration of directors and the chief executive as required under part III, para 3 (i) of Fifth Schedule;
- iv. The disclosure required for the 'revaluation of assets' as required under para 3.40 of AFRS; and
- v. Nature, amount and reasons for reclassification of comparative figures as required under para 1.11 of AFRS.

3. The Accounts of the Company for the year ended June 30, 2009 were also audited by the same auditor with the respondent being the engagement partners. The balances due from related parties were not disclosed in the Accounts for the year ended June 30, 2009 and proper disclosure regarding reasons for reclassification were not given in the Accounts for the year ended June 30, 2010. The auditor did not point out the facts regarding non-disclosure of balances due from related parties in the Accounts for the year ended June 30, 2009 and also failed to highlight the reclassification of such balances in its audit report for the year ended June 30, 2010 along with other non-compliances with disclosure requirements of AFRS and the Fifth Schedule. Consequently, the SCN was issued to the respondent under section 260 read with sections 255 and 476 of the Ordinance.



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4. In response to the SCN, the respondent vide letter dated November 30, 2012 submitted that Tariq Ayub, Anwar & Co., Chartered Accountants was dissolved and the partners of the firm were restrained by the Court from doing business under the name and style of the firm. He further submitted that the cases of rendition of accounts, defamation and illegal operations of dissolved firm were pending in the Court. He requested for extension in time to receive certified copy of the Court's order and opinion of his legal advisor. However, the respondent did not provide any update in respect of the court case. The case was fixed for hearing on April 8, 2015, however, the respondent requested for rescheduling of the hearing due to his engagements in cases on Income Tax Appellate Tribunal. Later on the case was fixed for hearing on June 16, 2015, which after a rescheduling was finally held on June 22, 2015. The respondent appeared before the undersigned on the appointed date and made verbal and written submissions. A brief of his submissions with reference to the contents of the SCN is given below:

- Reclassification of trade debtors of Rs74 Million as at June 30, 2009, to Rs3.6 million and Rs71 million of 'trade debtors' and 'other receivable from associated undertaking' respectively discloses the nature, amount and reason of reclassification as it was done to correct the wrong by the management. The Commission should appreciate the better and correct presentation.
- Sale of Rs16,243,755 of material pipes and SS plates was carried out by the Company but the amount was wrongly deposited by the Company's clients into bank accounts of other related companies. The clients namely Malik Saeed and Raja Fazal-ur-Rehman deposited Rs10,564,775 into account no. 365-1-1 of Petrosin Gas Pakistan (Pvt.) Limited while another client namely Ghazi Steel Works Gujranwala deposited Rs5,678,980 into account no. 336-2 of Petrosin CNG (Pvt.) Limited, both with MCB Bank.
- This amount was reflected in ledger accounts of associated undertakings as well as in annual Accounts of the Company under note 28 to the Accounts 'transactions with associated undertakings'. Copies of bank deposit slips, gate passes and slips of weights of materials enclosed.
- Requirements of para 5 (B) (ii) of the Fifth Schedule have been fulfilled. Names of the trade debtors, related parties are disclosed in note 28. Those particulars and their balances as at June 30, 2010 are as follows:



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(Rupees)

Petrosin CNG (Pvt.) Ltd	34,236,696
Petrosin Gas Pakistan (Pvt.) Ltd	4,770,377
Petro sin Engineering (Pvt.) Ltd	21,248,982
Kohinoor Oil Mills Ltd	154,057
<b>TOTAL</b>	<b>60,410,112</b>

There was no transaction carried out with Kohinoor Oil Mills Ltd. during the year.

- The 'interest receivable, from associated undertakings comprise following parties and are properly disclosed in note 28:

(Rupees)

Petrosin Gas Pakistan (Pvt.) Ltd	104,507
Petrosin Edible Oil (Pvt.) Ltd	54,833
Petrosin CNG (Pvt.) Ltd	31,327
<b>TOTAL</b>	<b>190,668</b>

- No remuneration was paid to any of the director or chief executive. Basis of revaluation of assets are properly disclosed in accounts. These were valued by independent valuer on March 28, 2006 and copy of the report is enclosed.
- It is management who prepares and presents the Accounts in accordance with the law. The Commission has no *locus standi* in these cases for auditors and is vehemently denied. The Commission should have raised these issues with management who is responsible for preparation and presentation of the Accounts.
- I would like to attach auditing technical release # 20 of the Institute of Chartered Accountants of Pakistan applicable to the audit report of year ended June 30, 2010 clearly stating that infraction of laws or regulations, the financial implications of which is not material to the financial statements, do not require the modifications to the auditors' opinion. Being member of the ICAP, the same requirements were followed.
- In this regard it is stated that being the engagement partner for the audit report of the Company for the year ended June 30, 2010, I have nothing to do with the inadequate explanation of management given to the Commission. If the management failed to get the



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ledgers of related parties reconciled with those of appearing in the Accounts. Ledgers were reconciled at the time of audit. I have compiled audit report in accordance with section 255 (3) (d) and section 260 (1) of the Ordinance.

5. Before proceeding further, it is necessary to advert to the following relevant provisions of Ordinance, AFRS and International Standards on Auditing ("ISA").

Para A6 and 12 of ISA 710 – "Comparative Information Corresponding Figures and Comparative Financial Statements" state as under:

*12. If the auditor obtains audit evidence that a material misstatement exists in the prior period financial statements on which an unmodified opinion has been previously issued, and the corresponding figures have not been properly restated or appropriate disclosures have not been made, the auditor shall express a qualified opinion or an adverse opinion in the auditor's report on the current period financial statements, modified with respect to the corresponding figures included therein. (Ref: Para. A6)*

*A6. When the prior period financial statements that are misstated have not been amended and an auditor's report has not been reissued, but the corresponding figures have been properly restated or appropriate disclosures have been made in the current period financial statements, the auditor's report may include an Emphasis of Matter paragraph describing the circumstances and referring to where relevant disclosures that fully describe the matter that can be found in the financial statements (see ISA 706).*

Para 5 B of the Fifth Schedule to the Ordinance, as applicable at the relevant time states as under:

*5(B). A company which is not a Small-Sized Company shall, in the case of clauses (iii), (iv) and (viii) of sub-head 5 (A) above, also state the following particulars, namely: -*

- (i) the aggregate amount due by directors and chief executive and executives of the company and any of them severally or jointly with any other person; and*
- (ii) aggregate amount due by related parties, other than in clause (i) of subhead 5(B) above; names to be specified in each case.*

Para 1.11 and 3.40 of AFRS for Medium Sized Entities state as under:

*1.11. Unless the standard permits or requires otherwise, comparative information with respect to the previous period shall be disclosed for all numerical information in the financial statements. Comparative information shall be included in narrative and descriptive information when it is relevant to an understanding of the current period's financial statements. When the presentation or classification of items in the financial statements is amended, comparative amounts shall be reclassified unless the reclassification is impracticable. When comparative amounts are reclassified, an entity shall disclose the nature,*



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amount and reason of the reclassification. When it is impracticable to reclassify comparative amounts, an entity shall disclose the reason for not reclassifying the amounts and the nature of the adjustments.

3.40 When items of property, plant and equipment are stated at revalued amounts, the following shall be disclosed:

- (a) the basis used to revalue the assets;
- (b) the effective date of the revaluation; and
- (c) whether an independent valuer was involved.

Section 255 of the Ordinance prescribes powers and duties of the auditors and sub-section (3) specifically prescribes the mandatory contents of the audit report.

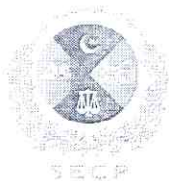
Section 260 of the Ordinance states as under:

“(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.”

6. I have analyzed the facts of the case, the relevant provisions of the Ordinance, requirements of AFRS and ISA and the arguments put forth by the respondent. I have observed that as per requirements of the Ordinance, AFRS and ISA quoted in the preceding paragraphs, the respondent being auditor of the Company was required to highlight the non-compliances by the Company in its report on the Accounts of the Company for the year ended June 30, 2010, in view of the following:

- a) ISA in general and ISA 550 in specific put in place special requirements for the auditor to exercise higher level of professional diligence and skepticism in respect of audit of related parties’ transactions given the inherent higher risk involved in such transactions. Due to this very reason, financial reporting framework in Pakistan like many other jurisdictions



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establishes specific accounting and disclosure requirements for related party relationships, transactions and balances to enable users of the financial statements to understand their nature and actual or potential effects on the financial statements. As set out by ISA 550, *planning and performing the audit with professional skepticism as required by ISA 200 is therefore particularly important in this context, given the potential for undisclosed related party relationships and transactions.*

- b) The Company failed to separately disclose the balances due from related parties in the Accounts for the year ended June 30, 2009 and when those were restated as comparative figures in the Accounts for the year ended June 30, 2010, no explanation was provided in the Accounts in this regard as per requirements of Para 1.11 of AFRS quoted above. Restating the figures to correctly disclose the comparative figures of balances due from related parties along with reasons for reclassification was the responsibility of the Company's management. Although they restated the comparative figures but did not provide reasons or explanation, which was necessary for proper understanding of the users. In terms of applicable ISA, it was auditor's responsibility to highlight the aforesaid restatement of related parties' balances and reasons thereof in his report to members. The auditor in view of requirements of Para 12 and A6 of the ISA 710 was required to highlight the matters in his report. The respondent's failure to do so renders him liable for the violation. It must be noted that all transactions with related parties and related disclosures should be considered material due to the nature of such transactions that involved higher risk. Materiality threshold for related parties transactions are, therefore, set lower by the ISAs.
- c) The Company failed to follow the complete disclosure requirement of the Fifth Schedule as name wise details of balances due from related parties was not disclosed in the Accounts. Moreover, name wise detail of interest due from each party was also not disclosed. Auditor failed to highlight the non-compliance.
- d) As reported by the inspection team, the Company does not have a clear distinction of balances pertaining to 'transactions with the associated undertakings' and 'the trade debtors' due to which there is often intermingling of balances at the time of presenting the figures in the annual account which in turn affects the accurate reporting of figures in the Accounts. This only leaves the auditor with a higher level of responsibility while reporting on the Accounts with reference to restatement of related parties' balances.



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- e) In respect of non-disclosure of sale of scrap amounting to Rs16,243,755 by Petrosin Gas Pakistan (Pvt.) Limited under the related parties' transactions, it has been submitted by the respondent that this sale was actually of material pipes and SS plates and was carried out by the Company. However, it was wrongly credited by the customers into bank accounts of Petrosin Gas Pakistan (Pvt.) Limited and Petrosin CNG (Pvt.) Limited. Copies of the documents provided include journal vouchers, bank deposit slips, gate passes etc. It appears that the customers wrongly deposited the amounts in the bank accounts of related parties and later on the entries were passed to transfer these funds to the Company by the related parties. It, however, shows lack of controls on the part of the Company. For all sales made by the Company the amounts should have been received by the Company instead of its related parties. It, however, appears that the auditor obtained documents to satisfy himself with regard to these sales by the Company in this particular instance. However, such special transactions were not separately disclosed in the Accounts for proper understanding of the users.
- f) In respect of revaluation of fixed assets, complete disclosures including the basis used to revalue the assets, the effective date and independent valuer were not given.
- g) Even otherwise, if modification to auditors' opinion, as claimed by the respondent in the context of ICAP's TR # 20, was not required in his view, it was his responsibility to highlight the issues and restatement of balances due from related parties in comparative figures in his report, as stated above.

7. 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 in the hope 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





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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. The responsibility of the auditor further increases when it comes to the audit of related parties transactions. 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.

8. For the foregoing reasons, I am of the view that the respondent failed to bring out the material facts about restatement of comparative figures of related parties' balances and other non-compliances and, therefore, is liable to penalty under section 260 of the Ordinance. Accordingly, I hereby impose a fine of Rs10,000/- (Rupees ten thousand only) under sub-section (1) of section 260 of the Ordinance on the respondent.

The respondent is directed to deposit the aforesaid fine in the designated bank account maintained in the name of Securities and Exchange Commission of Pakistan with MCB Bank Limited within thirty days from the receipt of this Order and furnish receipted vouchers for information and record, failing which proceedings under the Land Revenue Act, 1967 will be initiated which may result in the attachment and sale of movable and immovable property.

  
Tahir Mahmood

Commissioner (Company Law Division)

**Announced:**

August 12, 2015

Islamabad