



Corporate Supervision Department
Company Law Division

Before Mr. Tahir Mahmood – Commissioner (Company Law Division)

In the matter of

**M/s FR Merchant & Co. Chartered Accountants
Auditor of Titan Cement Industries Limited**

Number and date of notice: EMD/242/K/681/2013-1263 dated December 30, 2014
Date of hearing: September 10, 2015
Present: Mr. Waqas Yameen - Authorized Representative

ORDER

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

This order shall dispose of the proceeding initiated against FR Merchant & Co. Chartered Accountants ("respondent") through show cause notice (the "SCN") dated December 30, 2014 under the provisions of Section 260 read with Section 255 and 476 of the Companies Ordinance 1984 (the "Ordinance").

2. The facts leading to this case, briefly stated, are that, the examination of the annual audited accounts for the year ended June 30, 2013 & 2014 (the "Accounts") of Titan Cement Industries Limited (the "Company") revealed that, respondent being the auditor of the Company have prepared the audit report (the "Report") to the members of the Company which was not in conformity with the requirements of Section 255 & 260 of the Ordinance.

3. The accumulated losses of the Company stood at Rs. 17.695 million in 2014, the Company was incorporated in 2005 with the principal activity of manufacturing and marketing of cement, however, they have not yet started its production activities. The directors' report is silent about the uncertainty over the entity's ability to continue as going concern.

4. Para 19 of International Standard on Auditing (ISA) 570 (Going Concern) states that:
"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 doubts 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 matter set out in paragraph 18.*

Para 20 of ISA 570 (Going Concern) states that:

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 705.6 The auditor shall state in the auditor's report



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that there is a material uncertainty that may cast significant doubt about the entity's ability to continue as a going concern.

5. The respondent while making out their report to the members neither stated the aforementioned facts nor did he express a qualified opinion/adverse opinion as appropriate with specific reference to the fact of uncertainty with regard to going concern as required by the ISA. The audit reports on the aforesaid accounts were prima facie, not in accordance with the requirements of Section 255 of the Ordinance and ISA and failed to bring out material facts about the affairs of the Company. Therefore, SCN was issued to the respondent for *prima facie*, contravention of Section 260 of the Ordinance.

6. The reply to SCN was submitted by the respondent vide letter dated February 2, 2015. The seriatim reply is summarized below.

- The Company maintains a going concern status. The Company has ability to continue as going concern also they have disclosed in the directors report that the company has not started its production activities yet due to economic and political instability of the country and severe law and order issues as well. The Company has sustained losses but its equity is still positive and despite the willingness to commence the operation, directors unable to do so due to economic and political instability of the country in general and province (Baluchistan) in particular.
- The Company has positive equity of Rs. 12.404 million and has working capital of Rs. 834,180.

7. In order to provide opportunity of personal hearing; the case was fixed before the undersigned on September 10, 2015. Mr. Waqas Yameen appeared and maintained the same plea as per written submissions. He also submitted ICAP selected opinions Volume No. XIX, regarding auditors report on going concern assumption, extract of opinion is stated as follows;

The going concern assessment by management is required where the company ceases its operations or does not commence its operations, both due to adverse economic conditions. Although the company has sufficient liquid assets to settle its liabilities without incurring losses, ceasing or not starting operations are an indication that a material uncertainty is present. In both these cases, the auditors' responsibility is to obtain sufficient appropriate audit evidence and to conclude whether there is material uncertainty or not. In case where auditor's conclusion is different from the management assessment, appropriate reference in the opinion is required as illustrated in ISA 570.

8. Before proceeding with the order, it is appropriate to quote the provisions of Section 255(3) of the Ordinance stipulating duties of auditors. It requires that the auditor shall make a report to the members of the company on the accounts and books of account of the company and



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on every balance sheet and profit and loss account and on every other document forming part of the balance sheet and profit and loss account, including notes, statements or schedules appended thereto, which are laid before the Company in general meeting during their tenure of office, and the report shall state:

(d) whether or not in their opinion and to the best of their information and according to the explanations given to them, the said accounts give the information required by this Ordinance in the manner so required and give a true and fair view in the case of the balance-sheet, of the state of the company's affairs as at the end of its financial year; in the case of the profit and loss account or the income and expenditure account, of the profit or loss or surplus or deficit, as the case may be, for its financial year; and in the case of the statement of changes in financial position or sources and application of funds of a listed company, of the changes in the financial position or the sources and application of funds for its financial year;

9. Furthermore, the provisions of Section 255(4) requires that where any of the aforesaid matters is answered in the negative or with a qualification, the report shall state the reason for such answer along with the factual position to the best of the auditors' information.

10. In terms of the Commission's notification SRO 154 (I)/2015 dated February 19, 2015, the powers to adjudicate cases under section 255 & 260 have been delegated to the Commissioner (Company Law Division).

11. I have analyzed the facts of the case, relevant provisions of the Ordinance, arguments put forth by the respondent in writing during the hearing and observed that the provisions of Section 255 are very clear and the spirit of the aforesaid provisions is that, the primary responsibility of the auditor is to opine on the Accounts of the Company after obtaining all the relevant and necessary information which is essential to form an opinion.

12. Reverting to the argument put forth by the auditor, in view of the aforesaid provisions of the Ordinance and ISA the respondent stance that the Company maintains a going concern status is not tenable. As per ISA 570 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. The auditor needs to evaluate management's assessment of the entity's ability to continue as a going concern. Based on the audit evidence obtained, the auditor needs to 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. When material uncertainty exists the auditor has to express a qualified opinion or adverse opinion, as appropriate, in accordance with ISA 705



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13. Section 305 of the Ordinance stipulates that a company may be wound up by Court if the company does not commence its business within a year from its incorporation. In the instant case the respondent has expressed an unqualified opinion despite lapse of 10 years since incorporation the company has not yet started its production activities. The company is exposed to the risk of being wound up if the Commission or a creditors so desires. This risk is exaggerated by the fact that the directors report does not indicate any plan for commencement of business nor does it disclose any efforts by the management to change the situation of the company. These indications cast significant doubt on the entity's ability to continue as going concern and makes it incumbent on the respondents to assess the management's assumption on going concern. The selected opinion volume No. XIX by ICAP Committee referred by the respondents itself requires the respondents to do the same as can be perused in the para reproduced below:

Although the company has sufficient liquid assets to settle its liabilities without incurring losses, ceasing or not starting operations are an indication that a material uncertainty is present. In both these cases, the auditors' responsibility is to obtain sufficient appropriate audit evidence and to conclude whether there is material uncertainty or not. In case where auditor's conclusion is different from the management assessment, appropriate reference in the opinion is required as illustrated in ISA 570.

14. For the foregoing reasons, I am of the firm opinion that the respondent failed to bring about material facts about the affairs of the Company and accordingly audit reports have not been made in conformity with Section 255 & 260 of the Ordinance and is liable for the penalty as prescribed by Section 260 of the Ordinance. Therefore, in exercise of the powers conferred by the aforesaid provisions of the Ordinance, I hereby impose a fine of Rs.10,000 (Rupees ten thousand only) on the respondent.

The respondent is hereby directed to deposit fine of Rs.10,000 (Rupees ten thousand only) 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.

Tahir Mahmood
Commissioner
Company Law Division

Announced:
October 1, 2015
Islamabad

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