IN THE HIGH COURT OF JUDICATURE AT HYDERABAD
FOR THE STATE OF TELANGANA AND
THE STATE OF ANDHRA PRADESH

****

Referred Case No.2 OF 2011

Between:

The Institute of Chartered Accountants of India,
ICAI Bhawan,
P.B.No.7100, I.P.Marg, New Delhi

... Petitioner.

And

Shri Mukesh Gang,
Chartered Accountant,
Flat No.102, Seshu Villa, 1-2-593/7,
Gagan Mahal Colony, Hyderabad.

... Respondent.

JUDGMENT PRONOUNCED ON 26.09.2016

THE HON'BLE THE ACTING CHIEF JUSTICE RAMESH RANGANATHAN

THE HON'BLE SRI JUSTICE M.SATYANARAYANA MURTHY

1. Whether Reporters of Local newspapers may be allowed to see the Judgments? No

2. Whether the copies of judgment may be marked to Law Reporters/Journals Yes

3. Whether Their Ladyship/Lordship wish to see the fair copy of the Judgment? Yes

*** THE HON'BLE THE ACTING CHIEF JUSTICE RAMESH RANGANATHAN**

A N D

THE HON'BLE SRI JUSTICE M.SATYANARAYANA MURTHY

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The Institute of Chartered Accountants of India,
ICAI Bhawan,
P.B.No.7100, I.P.Marg, New Delhi

....Petitioner

v.

$ Shri Mukesh Gang,
Chartered Accountant,
Flat No.102, Seshu Villa, 1-2-593/7,
Gagan Mahal Colony, Hyderabad.

.... Respondent

! Counsel for the Petitioner : Sri C.V.Rajeeva Reddy.

Counsel for Respondents: Sri Ashok Anand Kumar

<Gist :

>Head Note:

? Cases referred:

1. AIR 1958 SC 72
2. AIR 1987 SC 71
3. AIR 1998 SC 74
4. LAWS (APH)-2014-1-93
5. AIR 1953 Mad 79
6. 1977 MPLJ 722
7. AIR 2011 Cal 233
8. AIR 1998 SC 283
9. (2003) 129 TAXMAN 80 (Guj.)

10. 2002 (8) SCC 715
11. AIR 1965 SC 1818
12. AIR 1957 Cal 33
13. AIR 1984 SC 110
14. AIR 2000 SC 3344
15. AIR 2006 SC 3475
16. AIR 1930 PC 144
17. AIR 1966 SC 1734
18. I.L.R.39 Cal. 245
19. AIR 1977 SC 1712
20. AIR 1956 SC 593
21. (2012) 8 SCC 148
22. AIR 1961 SC 234
23. (1987) 9 NSWLR 310
24. (1887) 36 Ch.D. 787
25. (1932) Acct LR 38
26. (1895) 2 Ch. 673
27. (1896) 2 Ch. 279
28. AIR 1968 SC 1104
29. (2007) 12 SCC 210
30. AIR 1956 Calcutta 414
31. AIR 1996 AP 254
32. (1911) 1 CH 426
33. (1899) 2 Ch.392
34. (1872) L.R. 5 H.L. 480
35. (1892) 3 Ch. 577
36. (1905) 2 KB 532
37. (1994) 2 Cal L J 456
38. AIR 1956 Hyd 205
39. AIR 2007 Cal 29
40. 2000 (56) DRJ 671
41. 2000 (57) DRJ 27
42. (1992) 4 SCC 54
43. AIR 1996 Bom 227
44. AIR 1956 Calcutta 414
45. AIR 1996 AP 254
46. (1912) 1 KB 302
47. (2000) 7 Supreme Court Cases 264
48. (2004) 5 Supreme Court Cases 689
49. (2002) 3 Supreme Court Cases 667
50. (2008) 8 SCC 205
51. 2002 (5) ALT 162 (D.B.)
52. 1998 (4) ALT 803
53. (2010) 3 Supreme Court Cases 556
54. (2006) 7 Supreme Court Cases 558

THE HON'BLE THE ACTING CHIEF JUSTICE RAMESH RANGANATHAN
AND
THE HON'BLE SRI JUSTICE M.SATYANARAYANA MURTHY

R.C.No.2 OF 2011

ORDER: *(Per Hon'ble Sri Justice M.Satyanarayana Murthy)*

The Institute of Chartered Accountants of India, a premier institute established under the Chartered Accountants Act, 1949 to regulate the profession of Chartered Accountants in India, has, by virtue of the power conferred under Section 21 (5) of the Chartered Accountants Act, 1949 (hereinafter, for short, referred to as "the Act"), made this reference to this Court for passing an appropriate order against the respondent including imposition of penalty/punishment. The respondent, a Chartered Accountant, established a firm by name M/s M.Gang & Co, which was appointed as a Statutory Auditor of Ritesh Polyster Limited (hereinafter, for short, referred to as the "Company"). The General Manager, Securities and Exchange Board of India (hereinafter, for short, referred to as "SEBI") addressed a letter to the President, Institute of Chartered Accountants of India (hereinafter, for short, referred to as "the Institute") stating that it had conducted an investigation in the primary market and secondary market transactions in the scrip of the company which had come out with a public issue in 1995. During the course of investigation, it was found that the respondent, as the statutory auditor of the company, had given a certificate dated 09.06.1995 certifying that the entire promoters' contribution had been received by the company. The certificate of the Auditor is as under:

> "We the statutory Auditors of Ritesh Polysters Limited, Secunderabad, hereby certify and confirm that as per the books of accounts maintained by the company, the company has received

Rs.225 lakhs (Rupees Two crores twenty five lakhs only) as share application money towards 15,00,000/- equity shares of Rs.10/- each at a premium of Rs.5/- per share from the promoters, directors, their friends and associates as on 9th June 1995.

.....The details of promotes contribution of Rs.225 lakhs (Rupees two hundered and twenty five lakhs only), as per the books of accounts maintained by the company is as follows:

Name of the Share Holder	No. of shares	Amount
Ritesh Exports Ltd.	6,00,000	90,00,000
Surender Kumar Agarwal	5,22,500	78,37,500
Roop Rekha Agarwal	2,37,500	35,62,500
Deepak Agarwal	70,000	10,50,000
Ritesh Agarwal	70,000	10,50,000

It was further noticed by the SEBI that promoters contribution, only to the extent of Rs.35 lakhs, was received by the company and not Rs.225 lakhs as certified by the Auditor. The cheques issued against the balance amount had bounced. However, shares worth Rs.225 lakhs were allotted to the promoters by the company. The respondent was asked about the basis on which he gave the certificate regarding receipt of promoters' contribution in full and, in reply, the respondent had submitted that he had verified the bank book maintained by the Company, wherein they had shown receipt of the above cheques, he did not expect that the cheques issued by the promoters would bounce, and he had issued the certificate keeping in view the track record and reputation of the promoters.

Dissatisfied with the reply submitted by the respondent, SEBI concluded that the respondent/Auditors, without actually verifying the bank statements regarding realisation of the cheques, had given a false certificate regarding receipt of promoters contribution, in full, by Ritesh Polysters Limited. The respondent was held guilty of professional misconduct, and to have abetted the promoters in the fraudulent activity by issuing a false certificate, as he could have issued the certificate with the remark that "***subject to realisation of the Cheques deposited***". Instead of doing so, the respondent had issued certificate as if the entire contribution of the promoters was received.

It is also specifically stated, in the report of SEBI, that the amount, towards promoters' contribution, said to have been brought in by two of the promoters i.e Sri Deepak Agarwal and Sri Ritesh Agarwal on 09.06.1995, was actually advanced to them by the company i.e Ritesh Polyster Limited itself. SEBI also observed that the contribution of Rs.10,50,000/- by each of these two promoters was actually routed through the account of M/s Pratha Investments, owned by the respondent's wife and run by the respondent herself. Thus, the respondent had failed to take due care while issuing the certificate, and had failed to comply with the requirement of the SEBI Circular and, while issuing the certificate, the respondent did not disclose transfer of money from M/s Pratha Investments to the promoters Sri Deepak Agarwal and Sri Ritesh Agarwal.

On receipt of the above said letter from SEBI, the Institute addressed letter dated 28.07.2005 to the respondent alleging that the amount received towards contribution was only Rs.35 lakhs, but

the respondent had certified that Rs.225 lakhs was received by the company towards promoters contribution, and the cheques issued against the balance amount had bounced. However, shares for Rs.225 lakhs were allotted to the promoters by the company. The respondent was called upon to disclose the name(s) of the member (s), answerable to the charge of misconduct, as per Regulation 12 (6) of the Chartered Accounts Regulations, 1988 (for short, hereinafter referred to as "Regulations"), and to forward the letter to him/them with a request to submit his/their written statement (s) in his/their defence, in triplicate, as required under Regulation 12(7) read with Regulation 13 of the Regulations specifying the manner in which they had to submit their defence.

In response to the letter dated 28.07.2005 of the Institute, the respondent submitted his reply dated 05.08.2005 admitting that he, as the Proprietor of M/s M.Gang & Company, had issued the certificate dated 09.06.1995 stating that the promoters contribution of Rs.225 lakhs was received as per the books of accounts maintained by the Company. The certificate was issued, after verifying the "Share Application Account maintained in the General Ledger of the Company (Xerox enclosed)", the bank book showing receipt of the payments (in the form of cheques deposited) into State Bank of Mysore, and the bank deposit slip counterfoils duly bearing the bank acknowledgements of the cheques deposited. The certificate was issued, on the basis of the documentary evidence produced before him on the date of issue of the certificate, in the belief that the cheques deposited would not bounce, keeping in view the past track record of the promoters. The respondent, however, admitted that he should have issued the certificate with the remark

"subject to realisation of the cheques deposited", and stated that, while it was an omission on his part, it was not done with any malafide intention, and he did not receive any financial benefit in this connection.

It was also stated by the respondent, in his reply, that he had no reason to verify the source of money received from Deepak Agarwal and Ritesh Agarwal towards promoters contribution to equity in the company, and that M/s. Pratha Investments was not a firm either owned or run by him (he failed to state that it was owned by his wife). He admitted that there was a professional lapse on his part in not issuing the certificate with the caption "cheques are subject to realisation", and requested that the lapse on his part be ignored, since it was not done wilfully, no monetary benefit was received by him, it was not intended to cheat or misguide the investors, and he did not aid or abet the promoters in any fraudulent activity.

Being dissatisfied with the explanation submitted by the respondent, the Institute initiated disciplinary proceedings and constituted a disciplinary committee consisting of Ved Jain- President, O.P.Vaish - the Government Nominee and J. Venkateswarlu - Member. The disciplinary committee framed charges and, after following the procedure prescribed under the Act and the Regulations, found the respondent guilty of misconduct under Clause (7) of Part I of the Second Schedule read with Sections 21 and 22 of the Chartered Accountants Act, 1949.

The disciplinary committee forwarded its report to the Council to take appropriate action and, accordingly, the Council of the Institute accepted the findings of the disciplinary committee and

recommended that this Court impose the punishment of removal of his name from the Register of Members, for a period of 3 years, on the respondent, after following the procedure prescribed under the Act and the Regulations.

During hearing, Sri C.V. Rajeeva Reddy, learned counsel for the Institute, while stating the facts of the case, contended that the misconduct attributed against the respondent is serious in nature, and is against public interest, since M/s Ritesh Polyster Limited had invited applications, for allotment of shares to the public, for several crores of rupees, but only Rs.35,00,000/- was received by the Company towards promoters contribution, as against Rs.225 lakhs. Though the promoters did not contribute the amount, they were allotted shares for Rs.225 Lakhs. The certificate issued by the respondent made the public believe that the promoters had contributed Rs.225 lakhs to the share capital of the company, and the respondent was liable for a severe punishment. Learned Counsel has placed reliance on several judgments, which we will discuss at the appropriate stage.

Sri Ashok Anand Kumar, learned counsel for the respondent, raised several contentions, which are as follows:

(a) The Institute did not comply with the procedure contemplated under Regulation 16 (2) and (5). On this ground alone the disciplinary proceedings are vitiated, and are liable to be set aside.

(b) The scope of the proceedings, in a reference under Section 21 (5) and (6) of the Chartered Accountants Act, is wider and this Court can reappraise the entire material to come to an independent conclusion regarding the misconduct

attributed to the respondent, since this Court is exercising disciplinary jurisdiction.

(c) The nature of the proceedings before this Court are quasi judicial and quasi criminal in nature, and the standard of proof as required in criminal prosecutions is to be applied to these disciplinary proceedings.

(d) The power to impose punishment is conferred only on this Court. As the Statute does not prescribe guidelines regarding the manner of its exercise, such power should be exercised, and the reference should be disposed of, following principles of natural justice.

(e) The standard of proof applicable to professional misconduct of legal practitioners can be applied to the misconduct attributed to the respondent who is a professional Chartered Accountant.

(f) In order to accept the findings and to impose penalty, this Court would be required to conclude that the act of the respondent is wilful, deliberate or that it amounts to culpable negligence. Otherwise it would not fall within the definition of gross negligence.

(g) The act, allegedly performed by the respondent, would not fall 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.

(h) As the admissions of the respondent were not of his volition, such admissions cannot be taken into consideration to conclude that the respondent is guilty of professional misconduct.

(i) The delay in conclusion of the proceedings before the disciplinary authority, and the Council, would require this Court to take a lenient view in view of the law declared by various courts.

While placing reliance on several judgments, which we will refer to at the appropriate stage in the order, he requested this Court to exonerate the respondent for the alleged acts of misconduct, after finding him not guilty.

The points which arise for consideration are as follows:

(1) Whether in a reference made to this Court, and in exercise of the powers conferred by Section 21 (5) and (6) of the Chartered Accountants Act, 1949, the High Court can re-appreciate the evidence on record, and re-examine the conclusions arrived at by the Institute?

(2) Whether the Institute has violated Regulations 16 (2) and 16 (5) of the Regulations and, if so, whether the entire proceedings are vitiated?

(3) Whether these disciplinary proceedings are quasi- judicial and quasi criminal in nature and, if so, what is the standard of proof applicable to such disciplinary proceedings against a professional?

(4) Whether the act attributed to the respondent, of having issued a certificate confirming receipt of contribution of Rs.225.00 lakhs from the promoters, amounts to gross negligence; if so, whether such an act would fall within the ambit of Clause (7) of Part 1 of the Second Schedule

read with Sections 21 and 22 of the Chartered Accountants Act, 1949?

(5) Whether the alleged act committed by the respondent is wilful and deliberate or amounts to culpable negligence constituting "gross negligence"?

(6) Whether the admission made by the respondent is sufficient to conclude that he is guilty of misconduct?

(7) Whether delay in conclusion of the proceedings would require the respondent to be exonerated or to reduce the punishment recommended by the Institute?

POINT No.1:

This reference is made by the Institute under Section 21 (5) of the Act recommending that the penalty/punishment be imposed on the respondent i.e. for removal of his name from the Register of Members for a period of 3 years after recording a finding of misconduct on his part. Learned counsel for the respondent contended that it is the duty of the Court, while exercising disciplinary jurisdiction, to re-appreciate the entire material on record, and this Court can come to a different conclusion setting aside the findings recorded by the Council of the Institute. The jurisdiction of this Court is wide, and is akin to exercise of jurisdiction on the original side. He would request this Court to reappraise the entire evidence, and come to an independent conclusion based on the material available on record. In support of his contentions, he has placed reliance on the judgments of the Apex Court in "**Council of the Institute of Chartered Accountants v. B.Mukherjea**[1]", "**Institute of Chartered Accountants of India**

[1] AIR 1958 SC 72

v. L.K.Ratna.[2]" and "**Institute of Chartered Accountants of India v. M/s Price Waterhouse**[3]". Sri C.V.Rajeeva Reddy, learned counsel for the Institute, did not dispute the aforesaid submissions regarding the scope of an enquiry in a reference under Section 21 (5) of the Act. He has also placed reliance on the same judgment of the Apex Court in **Council of the Institute of Chartered Accountants v. B. Mukherjea** (referred supra).

It is necessary to advert to the provisions of the Act, and the Regulations framed thereunder, for better appreciation of the scope of examination of disciplinary proceedings initiated against a professional Chartered Accountant.

Section 21 of the Act deals with the procedure in inquiries relating to misconduct of members of the Institute. Section 21 (5) and (6) read as under:

> Section 21 (5) of the Act: Where the misconduct in respect of which the Council has found any member of the Institute guilty is misconduct other than any such misconduct as is referred to in sub-section (4), it shall forward the case to the High Court with its recommendations thereon.
>
> Section 21 (6) of the Act: On receipt of any case under sub-section (4) or sub-section (5), the High Court shall fix a date for the hearing of the case and shall cause notice of the date so fixed to be given to the member of the Institute concerned, the Council and to the Central Government, and shall afford such member, the Council and the Central Government an opportunity of being heard, and may thereafter make any of the following orders, namely:-
>
> (a) direct that the proceedings be filed, or dismiss the complaint, as the case may be;
>
> (b) reprimand the member;
>
> (c) remove him from membership of the Institute either permanently or for such period as the High Court thinks fit;
>
> (d) refer the case to the Council for further inquiry and report."

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[2] AIR 1987 SC 71
[3] AIR 1998 SC 74

The power conferred on this Court, by Section 21 (6) of the Act, enables it to direct the proceedings to be filed, or to dismiss the complaint, as the case may be; reprimand the member; remove him from the membership of the Institute either permanently or for such period as it thinks fit; or to refer the case to the Council for further inquiry and report. The power conferred on this Court, in dealing with a reference made under Section 21 (5) of the Act, is unfettered and without any statutory restriction. In order to decide whether the complaint should be dismissed, or for any order to be passed imposing punishment on a member of the Institute, this Court must examine the entire material on record, come to an independent conclusion, and record a finding whether the member of the Institute is guilty of professional misconduct as defined in Section 22 of the Act.

Regulation 15 of the Regulations prescribes the procedure for an enquiry to be conducted before the Disciplinary Committee, and Regulation 16 prescribes the action to be taken on the report of the disciplinary committee. Neither of these provisions regulate the scope of an enquiry in a reference made to this Court under Section 21 (5) of the Act.

Even though a recommendation is made, recording a finding that the member of the Institute is guilty under Section 21 (5), the Act confers power on this Court to examine afresh whether the misconduct attributed to the member is established, and this Court can direct the complaint to be filed or dismiss it if it finds no material under Section 21 (6) of the Act. After examining the material on record, the Court must record its own conclusions/findings as to the misconduct attributed to the member

of the Institute. Depending upon the gravity of the misconduct proved against the member of the Institute, this Court is entitled to impose any punishment or penalty, including a punishment other than that recommended by the Institute.

Section 21 (1) of the Act deals with two categories of cases, in which the alleged misconduct of the members of the Institute can be enquired into, viz., based on the information received or complaint made to the Institute against the conduct of any member of the Institute i.e. a Chartered Accountant. The Council is, however, not bound to hold any enquiry straightaway. After examination of the complaint or information, if the Council finds that the facts alleged against the member, if proved, would render the member unfit, it may order an enquiry. If the disciplinary committee finds the member of the Institute guilty, it is required to submit a report to the Council. The Council is required to follow the procedure prescribed under Regulation 16, and if it finds that the matter falls exclusively within the ambit of Section 21 (5) of the Act, it should then refer the matter to this Court for a penalty to be imposed.

On a reference made by the Institute, this Court can exercise the power conferred under Section 21 (6) of the Act. In such a reference, the jurisdiction and powers of the High Court, while dealing with cases under sub-sections (2) (3) and (4) of Section 21 of the Act, are limited. The Calcutta High Court took the view that, even if a wider construction is put on the material words used in Sections 21 and 22, they would not be justified in passing any orders against the respondent in the proceedings, because the finding which had been referred to the High Court was only one, and that was that the respondent was guilty of professional

misconduct in the narrow sense of the term. In other words, the High Court was of the view that, if a wider construction is placed on the material words of the Section, it would be making out a new case on the reference, and the Court would not be justified in adopting such a course. The Apex Court, in **"Council of the Institute of Chartered Accountants v. B. Mukherjea"** (referred supra), held that the view of the Calcutta High Court was not well-founded. Section 21(2) lays down the procedure to be followed by the High Court when a finding, made by the Council, is referred to it under Section 21 (1). Notice, of the day fixed for the hearing of the reference, should be given to the parties specified in Section 21 (1), and an opportunity of being heard has to be afforded to them. Section 21 (3) then lays down that the High Court may either pass such final orders on the case as it thinks fit or refer it back for further inquiry by the Council, upon receipt of the finding after such inquiry, to deal with the case in the manner provided in sub-section (2), and to pass final orders thereon. It is clear that, in hearing a reference made under Section 21 (5), the High Court can examine the correctness of the findings recorded by the statutory bodies in that behalf. The High Court can even refer the matter back for further inquiry by the Council, and record a fresh finding. It is not as if the High Court is bound in every case to consider the merits of the finding as it has been recorded, and to either accept or reject the said finding. If, in a given case, it appears to the High Court that, on the facts alleged and proved, an alternative finding may be recorded, the High Court can as well send the case back to the Council with appropriate directions in this regard. The powers of the High Court, under Section 21 (3), are undoubtedly wide enough to enable it to

adopt any course which, in its opinion, will enable it to render justice to the parties.

In **Institute of Chartered Accountants of India v. L.K. Ratna** (referred supra) the Apex Court discussed the scope of an enquiry in a reference under Section 21 (5) of the Act, and held that it was apparent that, in the scheme incorporated in Section 21 of the Act, there were separate functionaries, the Disciplinary Committee, the Council and, in certain cases, the High Court. The controlling authority was the Council, which was only logical for the Council is the governing body of the Institute. When the Council receives information or a complaint alleging that a member of the Institute is guilty of misconduct, and it is *prima facie* of the opinion that there is substance in the allegations it refers the case to the Disciplinary Committee. The Disciplinary Committee plays a subordinate role. It conducts an inquiry into the allegations. Since the inquiry is into the allegations of misconduct by the member, it possesses the character of a quasi-judicial proceeding. The Disciplinary Committee, thereafter, submits a report of the result of the inquiry to the Council. The Disciplinary Committee is merely a Committee of the Institute, with its functions specifically limited by the provisions of the Act. As a subordinate body, it reports to the Council, the governing body. The report will contain a statement of the allegations, the defence entered by the member, a record of evidence and the conclusions upon that material. The conclusions are the conclusions of the Committee. They are only tentative. They cannot be regarded as 'findings'. The Disciplinary Committee is not vested by the Act with power to render any findings. It is the Council which is empowered to find whether the member is guilty of

misconduct. Both Section 21(2) and Section 21(3) are clear as to that. If, on receipt of the report, the Council finds that the member is not guilty of misconduct, Section 21(2) requires it to record its finding accordingly, and to direct that the proceedings shall be filed or the complaint shall be dismissed. If, on the other hand, the Council finds that the member is guilty of misconduct, Section 21(3) requires it to record a finding accordingly, and thereafter to proceed in the manner laid down in the succeeding sub-sections. The finding by the Council is the determinative decision as to the guilt of the member, and because it is determinative, the Act requires it to be recorded. A responsibility as grave as the determination that a member is guilty of misconduct, and recording of that finding, has been specifically assigned by the Act to the governing body, the Council. It is also apparent that it is only upon a finding being recorded by the Council that the Act moves forward to the final stage of penalisation. The recording of the finding by the Council is the jurisdictional springboard for the penalty proceeding which follows.

At this point it is necessary to advert to the nature of the power conferred on the Council. The Council is empowered to find a member guilty of misconduct. The penalty which follows is so harsh that it may result in the removal of a member's name from the Register for several years which would deprive him of the right to a certificate of practice. As is clear from Section 6(1) of the Act, he cannot practice without such a certificate. In the circumstances there is every reason to presume in favour of an opportunity being given to the member of being heard by the Council before it proceeds to pronounce upon his guilt. As seen, the finding by the

Council operates with finality in the proceeding, and it constitutes the foundation for the penalty imposed by the Council on him. The power to find and record whether a member is guilty of misconduct has been specifically entrusted by the Act to the entire Council itself and not to a few of its members who constitute the Disciplinary Committee. It is the character and complexion of the proceeding, considered in conjunction with the structure of power constituted by the Act, which leads to the conclusion that the member is entitled to a hearing by the Council before it can find him guilty.

In **Institute of Chartered Accountants of India v. M/s Price Waterhouse** (referred supra) the Apex Court held that a combined reading of the relevant provisions in Section 21 and Regulation 16 did indicate that recording of a finding of guilt or non-guilt by the Council was mandatory to take further action or to dismiss the complaint or for further process. The Council was required to consider independently the explanation submitted by the member and the evidence adduced in the enquiry before the Disciplinary Committee, and the report of the Disciplinary Committee. It provided an in-built mechanism under which the Council itself was required to examine the case of the professional or other misconduct of a member of the Institute or associate member, taking the aid of the report submitted by the Disciplinary Committee, the evidence adduced before the Committee, and the explanation offered by the delinquent member. The entire material constitutes the record of the proceeding before the Council to reach a finding whether or not the delinquent member had committed professional or other misconduct. Otherwise, the primacy accorded to the report of the Disciplinary Committee would attain finality,

denuding the Council of the power of discipline over the members of the Institute, and that would have a deleterious effect on the maintenance of discipline among the members or associate members of the Institute.

The Division Bench of this Court in "**Council of the Institute of Chartered Accountants of India v. G.Pattabhi Rama Charya**[4]" held that, in exercise of the jurisdiction under Section 21 of the Act, the High Court would take action against the Member only if it accepts the finding recorded by the Council and not otherwise.

The Division Bench of the Madras High Court in "**M.S.Krishnaswami v. The Council of the Institute of Chartered Accountants of India**[5]" held as follows:

> "It was argued for the petitioner that whatever might have been the position where disciplinary action is taken in exercise of inherent jurisdiction, where such a jurisdiction is conferred by a Statute, the proceedings become impressed with the character of civil proceedings and Article 133 will apply to them. We are unable to agree with this contention. We fail to see how the right of appeal can depend on whether the order was passed in exercise of a jurisdiction which is conferred by, a Statute on the court. If there is a right of appeal only against orders passed in civil proceedings, the determination of this right must depend on the nature of the jurisdiction that is exercised and not on the source of authority which confers that jurisdiction. In fact the decision in -- 'Bir Kishore Roy v. Emperor', 4 Pat L J 423, is with reference to an order passed under the special jurisdiction conferred by the Legal Practitioners Act and the court held that the appeal to the Privy Council was incompetent whether the disciplinary jurisdiction was exercised under the clauses of the Letters Patent or under a Statute."

In "**Council of the Institute of Chartered Accountants of India v. C.H.Padliya**[6]" the Madhya Pradesh High Court, after following the principles laid down in **Council of the Institute of**

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[4] LAWS (APH)-2014-1-93
[5] AIR 1953 Mad 79
[6] 1977 MPLJ 722

Chartered Accountants v. B. Mukherjea, held that the powers of the High Court under sub-section (6) of section 21 of the Act in hearing a reference under sub-section (5) thereof, and the provisions of Regulation 36 read with Part II of the Second Schedule to the Act and their application to the facts of the case was wider; the High Court may direct the proceedings to be filed or dismiss the complaint, reprimand the member or remove him from membership of the Institute either permanently or for such period; the High Court is also empowered, under Section 21(7) of the Act, to transfer the case subject to such other conditions, if any, as it thought fit to impose, to another High Court if it appeared to it that the transfer of a pending case will promote the ends of justice or tend to the general convenience of the parties; the powers in a reference under Section 21 (5) of the Act are wider; and the Court can come to any independent conclusion based on the material notwithstanding the findings recorded by the Council and the recommendations made for imposing penalty or punishment.

In "**The Council of the Institute of Chartered Accountants of India v. Shri Dilip Kumar De**[7]" the High Court of Calcutta, while deciding the case of misconduct of a Chartered Accountant, considered the scope of a reference, and the powers vested in the Court in a reference made to it. The Calcutta High Court concluded that the powers of the High Court are wider in view of the scheme for disposal of cases relating to misconduct, and it was apparent that, even in cases of misconduct of a lesser degree specified in the First Schedule to the Act, once a member was found guilty by the Council, based on an enquiry by the Disciplinary Committee, the

[7] AIR 2011 Cal 233

law did not authorize the Council to totally exonerate such a person, and at least a penalty in the form of "reprimand" must be imposed as provided in Sub-section (4) of Section 21 of the Act. If the member is found to be not guilty on enquiry, even in cases of misconduct specified in the Second Schedule to the Act, the law did not require approval of such finding by the High Court, and the Council itself was authorized to drop the proceedings or dismiss the complaint on such finding. But when a member has been found guilty of the graver misconducts mentioned in the Second Schedule, it is absurd to suggest that the Council may even decide not to recommend the minimum punishment of reprimand provided for the misconduct mentioned in the first schedule. The scheme of the Act permis dropping of proceedings or dismissal of the complaint only on a finding that the member is not guilty and not otherwise. Therefore, the order referred to in Clause (a) of sub-section (6) of Section 21 can be passed only if the finding of guilt recorded by the Council is set aside by the High Court. Thus, the High Court is vested with a wider power even to disagree with the findings recorded by the Council.

The Apex Court in "**P.D.Gupta v. Ram Murti**[8]", discussed the scope of the jurisdiction of the High Court to interfere with the finding recorded by the Bar Council of India and other statutory bodies, and held that the Bar Council of India and the State Bar Councils are statutory bodies. These bodies perform varying functions under the Act and the Rules framed thereunder. The Bar Council of India has laid down standards of professional conduct for the members. The Code of conduct, in the circumstances, can never

[8] AIR 1998 SC 283

be exhaustive. The Bar Council of India and the State Bar Councils are representatives' bodies of the Advocates on their rolls, and are charged with the responsibility of maintaining discipline amongst members, and to punish those who go astray from the path of rectitude set out for them. When the disciplinary committee has considered all the relevant circumstances, and has come to the conclusion that the advocate is guilty of misconduct, there is no reason to take a different view. The Supreme Court also found no ground to interfere with the punishment awarded to Sri P.D. Gupta.

In "**Council of the Institute of Chartered Accountants of India v. P.C. Parekh**[9]" the Gujarat High Court, while examining the scope of interference by the High Court with the findings recorded by the disciplinary committee, held that the High Court has been entrusted an important function in the context of the behaviour of the members of this noble profession in the disciplinary matters which come up before it. It has wide powers extending to removal from membership of the institute either permanently or for a specified period. It may direct the proceedings to be filed or dismiss the complaint. This enables the Court to examine the nature of misconduct alleged, and the facts and circumstances brought on record in connection therewith against the delinquent. There is a serious responsibility on the Court, a duty to itself, to the profession, and to the whole of the community to be careful not to accredit any person as worthy of the public confidence who cannot establish his right to that credential. However, when an important statutory body like the Council finds a member of the institute guilty of misconduct, and forwards the case to the High Court with

[9] (2003) 129 TAXMAN 80 (Guj.)

its recommendation under Section 21(5) of the Act, its findings, based on the material on record, would ordinarily not be disturbed unless found to be unjust, unwarranted or contrary to law.

The Gujarat High Court further held that the Council is one such representative body charged with the responsibility of ensuring discipline and ethical conduct amongst its members, and to impose appropriate punishment on members who are found to have indulged in conduct which lowers the esteem of the professionals as a class. Adopting the aforesaid approach, it was not possible to find any infirmity, either on facts or in law, in the reasoning and the findings recorded by the Disciplinary Committee and the petitioner Council in holding the respondent as being guilty of "other misconduct" under Section 21 read with Section 22 of the Act.

In "**West Bengal Electricity Regulatory Commission v. CESC Ltd.**[10]" the Apex Court held as follows:

> ***"that the appellate power of the High Court statutorily is not hedged in by any restriction, but in our opinion, the High Court merely because it has unrestricted appellate power, should not interfere with the considered order of the Commission unless it is satisfied that the order of the Commission is perverse, not based on evidence or on misreading of evidence, keeping in mind the fact that the Commission is an expert body.....***
>
> ***.....Further, in regard to the exercise of appellate power against the orders of expert Tribunals, on facts, the Appellate Court which is not an expert forum should be doubly careful while interfering with such expert forum's findings on facts....."***

In view of the law declared by the Apex Court and various High Courts, more particularly in **Council of the Institute of**

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[10] 2002 (8) SCC 715

Chartered Accountants v. B. Mukherjea (referred supra), the powers of the High Court, in a reference under Section 21 (5) of the Act, are wide and the Court can exercise its jurisdiction to render justice to the parties before it. We are in agreement with the submission of Sri Ashok Anand Kumar, learned counsel for the respondent, that the powers of this Court, in a reference under Section 21 (5) of the Act, are wide, and this Court is empowered to pass any of the orders contemplated under Section 21 (6) of the Act. Accordingly, the point is answered.

POINT No.2:

During the course of hearing, Sri Ashok Anand Kumar, learned counsel for the respondent, pointed out that the Institute and the disciplinary committee failed to comply with Regulation 16 (2) and (5) of the Regulations; they also failed to record evidence of the witnessess on behalf of the Institute, and they did not afford any opportunity to the respondent to adduce evidence; and, therefore, the enquiry conducted by the disciplinary committee, as confirmed by the Council, is vitiated by illegalities. Whereas, Sri C.V. Rajeeva Reddy, learned counsel for the Institute, contended that, in the absence of a prescribed procedure to be followed by the disciplinary committee, the Institute can adopt its own procedure and, accordingly, they followed a fair procedure, and recorded their findings mostly based on the admissions made by the respondent in the questionnaire. Therefore, on this ground, the disciplinary proceedings cannot be set at naught.

It is apposite to extract Regulation Nos.16 (2) and (5) for better appreciation.

Regulation 16:

(1) .....

(2) Where the finding of the Disciplinary Committee is that the respondent is guilty of professional and or other misconduct, a copy of the report of the Disciplinary Committee shall be furnished to the respondent and he shall be given the opportunity of making a representation in writing to the Council.

(3) .....

(4) .....

(5) The finding of the Council shall be communicated to the complainant and the respondent.

Clause (2) of Regulation 16 obligated the Disciplinary Committee to furnish a copy of its report to the respondent to enable him to submit a representation in writing to the Council. Though the learned counsel for the respondent pointed out non-compliance, he did not bring any material to our notice regarding non-compliance of Regulation No. 16 (2) of the Regulations. On the other hand, the material on record discloses that the Disciplinary Committee, after completion of enquiry, addressed letter dated 24.08.2009 enclosing a copy of the report, in compliance with Regulation No.16 (2) of Regulations. Thus, the Disciplinary Committee has complied with the mandatory requirement specified under Regulation No.16 (2) of the Regulations.

Similarly, Regulation No.16 (5) of Regulations obligated the Council to communicate the finding to the complainant and the respondent. In compliance with Regulation No.16 (5), the Council submitted the decision extracting from the Minutes of the 300th meeting of the Council held from 24th to 26th November, 2010 at New Delhi. Therefore, the Institute complied with both Regulation Nos.16 (2) and (5) of the Regulations, which are mandatory.

The respondent did not complain about non-compliance of any mandatory provisions, which caused him prejudice, either before the Council or the Disciplinary Committee. For the first time before us is a such contention urged. In view of the material available on record, regarding compliance with Regulation Nos.16 (2) and (5) of the Regulations, we are satisfied that the proceedings are not vitiated.

One of the contentions urged by Sri Ashok Anand Kumar, learned counsel for the respondent, is that no evidence was recorded following the rules of evidence but, based on admission of the respondent, a finding was recorded. Undoubtedly, there is no specific procedure prescribed to be followed by the Disciplinary Committee to record its finding. The strict rules of evidence, under the Indian Evidence Act, and the elaborate procedure prescribed under the Code of Civil Procedure or the Criminal Procedure Code, are not applicable to proceedings before the Disciplinary Committee of the Institute except for a few provisions of the Code of Civil Procedure as stipulated under Section 21 (8) of the Act. There is nothing in the Act, or in the Regulations, which disables the Committee from evolving its own procedure in conducting an enquiry into the misconduct alleged to have been committed by a member of the Institute. A questionnaire was sent, during the enquiry, eliciting answers from the respondent on 29.11.2008 at 10.10 a.m. in the office of the Institute at Chennai, and an opportunity was given to the respondent to explain the circumstances in which the certificate was issued by him. During questioning, the President of the Committee put a specific question

"***What do you want to say in your defence?***", then the respondent gave the following answer:

> ***"I gave a certificate on 9th June, 1995 and on that date the cheques were deposited and because the cheques could not cleared on that day and subsequently I appeared before the SEBI they told me that you should have subsequently withdrawn the certificate if you had come to know that the cheques are not cleared. I told them that that is the work of Merchant Bank and they are monitoring the day to day movement of the funds. I cannot go and monitor the day to day movement of the funds in their Company and based on their track record whatever cheques they have earlier deposited got cleared that is only one time that Rs.37 lacs cheques not cleared. That was the only plea which I took before the SEBI and I also taking before the Disciplinary Committee."***

Similarly several questions were put to the respondent who answered all the questions put to him. As questions were put to him, nothing prevented the respondent from explaining the circumstances in which he issued the certificate. He, however, did not give any satisfactory explanation to the questions. The respondent also did not express his desire to examine any witness on his behalf before the Committee. The question of cross examination of any witness would arise only if a witness is examined in chief in the first place. Therefore, the Committee recorded a finding that the respondent was guilty of professional misconduct. The evidentiary value of admissions of the respondent will be decided at an appropriate stage in the later part of this order.

The Disciplinary Committee has been conferred the power to enquire into the matter. In causing such an enquiry, the provisions of the CPC are applicable only to the limited extent specified in Section 21 (8) of the Act i.e. summoning and enforcing the attendance of any person and examining him on oath; the discovery

and production of any document; and receiving evidence on affidavit. While the Disciplinary Committee is required to follow the procedure prescribed under Section 21 (8) of the Act, it cannot exercise the powers of a Civil Court.

After considering the entire material on record, we are satisfied that the Disciplinary Committee, and the Council, have not violated any of the Regulations, more particularly Regulation 16 (2) and (5) thereof. Therefore, this point is held against the respondent and in favour of the petitioner.

POINT No.3:

Sri S. Ashok Anand Kumar, learned counsel for the respondent, would contend that the proceedings, before the Committee and the Council, are quasi-judicial and quasi-criminal in nature. The initial onus will always lie on the Institute to prove the guilt of the respondent beyond reasonable doubt and the principle of appreciation, i.e. preponderance of probabilities, applicable to Civil Cases cannot be applied to quasi-criminal cases i.e. disciplinary proceedings before the authorities.

The phrase "Quasi-criminal" mean a lawsuit or equity proceeding that has some, but not all, ***of the qualities of a criminal prosecution***. It may appear either in a Common law or a Civil law jurisdiction. It refers to ***"a court's right to punish for actions or omissions as if they were criminal."*** The origins of the phrase comes from the Latin word, *quasi*, meaning somewhat, sort-of, alike or akin to criminal law, as in Quasi-contract. The word "Quasi" is used "to indicate that one subject resembles another, with which it is compared, in certain characteristics, but there are intrinsic and material differences

between them. During a civil or equity trial, a court may act as if it were a criminal case to punish a person for contempt of court. In some cases, a court may impose asset forfeiture or another penalty. For example, a court has the right to punish actions or omissions of a party in a child support case as if they were a criminal, penalizing the parent with a sentence of jail term. Quasi-criminal proceedings include a wide variety of matters, including prosecution for a violation of the law or ordinance, psychiatric matters, motor vehicle law, status offences, family court actions, and equity proceedings such as a Writ.

In criminal cases, generally, Courts try cases following the prescribed procedure, and impose punishment either of a sentence or a fine or both, but in disciplinary proceedings, more particularly under the Act, the punishment which may be imposed is not a jail term or fine like any other criminal proceeding. The punishment which may be imposed under Section 21 of the Act, if the respondent is found guilty of misconduct, cannot be equated to a sentence or a fine imposed on a person being found guilty in a criminal prosecution. The standard of proof required in criminal cases and civil cases also vary.

In "**S.A.L.Narayan Row and another v. Ishwarlal Bhagwandas**[11]" the Supreme Court held that, generally speaking, a proceeding is a civil proceeding only if it relates to a civil right whether resting on common law or created by statute. The nature of the proceeding depends not upon the nature of the tribunal which is invested with the authority to grant relief, but upon the nature of the right violated, and the appropriate relief which may be claimed.

[11] AIR 1965 SC 1818

A civil proceeding is, therefore, one in which a person seeks to enforce, by appropriate relief, the alleged infringement of his civil rights against another person or the State, and which if the claim is proved would result in the declaration, express or implied, of the right claimed and relief such as payment of debt, damages, compensation, delivery of specific property, enforcement of personal rights, determination of status etc. There is thus a marked difference between Civil Proceeding and Criminal Proceeding.

If the principles laid down in **S.A.L. Narayan Row and another v. Ishwarlal Bhagwandas** (referred supra) is applied to the facts of the present case, the proceedings before this Court, before the Council and Committee are not criminal proceedings, and the rules of evidence applicable to criminal cases cannot be applied to the disciplinary proceedings initiated against the respondent.

Sri S. Ashok Anand Kumar, Learned counsel for the respondent, contends that the proceedings instituted against the respondent are quasi-criminal in nature and, consequently, this Court should insist on proof of misconduct beyond reasonable doubt like in criminal prosecution. He has placed reliance on a Division Bench judgment of the Madhya Pradesh High Court in **Council of the Institute of Chartered Accountants of India v. C.H. Padliya** (referred supra), wherein it is held as follows:

> "It may be convenient at this stage to consider the question as to on whom the onus of proof lies in the present case. The guide line and the clue to answer this question lies upon the nature and character of the proceedings initiated against the respondent Chartered Accountant. The scheme, intendment and object of section 21 referred to earlier when read with the use of the expressions "complaint", "guilty of any professional or other misconduct", "Disciplinary Committee", "inquiry and the nature of the punishment provided to be imposed by the Council or the High

> Court as the case may be against a member who is found to be guilty of any professional or other misconduct" would indicate and ***leave no doubt in our minds that the proceeding initiated against a member in inquiries relating to misconduct is akin to though not in fact a criminal prosecution***. At every stage, the statute provides for a reasonable opportunity of being heard to the delinquent member of the Institute against whom disciplinary proceedings have been initiated. Principles of natural justice must be followed by the Inquiry Authority, the Council as well as the High Court and the evidence has to be recorded by the Disciplinary Committee. The Council and the Disciplinary Committee are empowered with the same powers as are vested in the Civil Court for summoning and enforcing the attendance of any person and examining him on oath, the discovery and production of any document, and receiving evidence on affidavit. The member against whom a complaint is lodged or a charge is framed is permitted to lead his own evidence to vindicate his stand about the charge. Where no prima facie case has been made out, the Council itself may ignore the information or complaint but it has to refer the matter to the Disciplinary Committee, if in its opinion, there is a prima facie case against the member. The proceeding is undoubtedly quasi-judicial in character. In our considered opinion it is a quasi-judicial and quasi-criminal in character which is akin to criminal prosecution, though not exactly a criminal prosecution. It is akin to the proceedings of professional misconduct against a legal practitioner under the Legal Practitioners Act."

It was further held that the standard of proof that ought to be applied to cases arising under the Legal Practitioners Act is the same proof which is required for conviction on a criminal charge. The charge must be proved beyond reasonable doubt. Therefore, a charge that is required to be proved, against a professional for his misconduct, is like in a criminal prosecution.

He also relied on **Council of the Institute of Chartered Accountants of India v. G.Pattabhi Rama Charya** wherein a Division Bench of this Court, relying on the judgment of the Calcutta High Court in "**S. Ganesan v. A.K. Josceiyne**[12]", held that

[12] AIR 1957 Cal 33

Professional misconduct on the part of the person exercising one of the technical professions cannot fairly or reasonably be found, merely on a finding of a bare non-performance of a duty or some default in performing it. The charge is not one of inefficiency, but of misconduct and in an allegation of misconduct, imputation of a certain mental condition is always involved. It would be impossible for any professional man to exercise his profession if he was to be held guilty of misconduct simply because he had not, in a given case, been able to do all that was required in the circumstances or had misconceived his duty or failed to perform a part of it. I think the test must always be whether in addition to the failure to do the duty, partial or entire which had happened, there had also been a failure to act honestly and reasonably.

In **S. Ganesan v. A.K. Josceiyne** (referred supra) the Calcutta High Court held that **mental condition of the professional is to be established** to hold him guilty of misconduct. The Supreme Court in "**Pandurang Dattatraya Khandekar v. The Bar Council of Maharashtra, Bombay**[13]" and "**H.V. Panchaksharappa v. K.G. Eshwar**[14]", considered a charge of professional misconduct against Advocate under the Advocates Act.

It is not in dispute that, even in disciplinary proceedings, there should be some evidence to prove the charge. Although the charges in a departmental proceedings are not required to be proved like a criminal trial, i.e., beyond reasonable doubt, the enquiry officer should, after analysing the evidence on record, determine whether, on the preponderance of probabilities, the charge is proved. While doing so, he cannot take into consideration irrelevant

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[13] AIR 1984 SC 110
[14] AIR 2000 SC 3344

facts, and refuse to consider relevant facts, and shift the burden of proof on to the charged officer. The Enquiry Officer cannot also reject relevant testimony of witnesses on the basis of surmises and conjectures. A charge in a departmental proceedings, as held in "**M.V.Bijlani v. Union of India and Ors.**[15]", is not required to be proved beyond reasonable doubt like in a criminal trial, but should be proved on a preponderance of probabilities.

In "**A, a pleader v. The Judges of the High Court of Madras**[16]" the Privy Council held that the evidence should be carefully taken and judged according to the ordinary standards of proof.

A Constitution of the Supreme Court, in "**Gulabchand v. Kudilal**[17]", after adverting to the law laid down in "**Jarat Kumari Dassi v. Bissessur**[18]" and referring to the definitions of "proved, disproved and not proved" contained in Section 3 of the Indian Evidence Act, held as follows:

> ".....It is apparent from the above definitions that the Indian Evidence Act applies the same standard of proof in all civil cases. It makes no difference between cases in which charges of fraudulent or criminal character are made and cases in which such charges are not made. But this is not to say that the Court will not, while striking the balance of probability, keep in mind the presumption of honesty or innocence or the nature of the crime or fraud charged. ***In our opinion, Woodroffe, J., was wrong in insisting that such charges must be proved clearly and beyond reasonable doubt***....."

In view of the law laid down by the Constitution Bench of the Apex Court, in "**Gulabchand v. Kudilal**" (referred supra), and the Judgment of the Privy Council in "**A, a pleader v. The Judges of**

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[15] AIR 2006 SC 3475
[16] AIR 1930 PC 144
[17] AIR 1966 SC 1734
[18] I.L.R.39 Cal. 245

the High Court of Madras" (referred supra), it must be held that the standard of proof required to establish a charge, in a disciplinary proceedings, is on a preponderance of probabilities, and cannot be equated with the standard of proof in a criminal prosecution, wherein a charge is required to be proved beyond reasonable doubt. Accordingly, this point is decided.

POINT No.6:

After investigation by SEBI, in compliance with Section 11 (3) of SEBI Act, a questionnaire was sent to the respondent calling upon him to give answers. Accordingly, he gave the following answer to Question No.10.

> ***"Based on the bank book of the Company, wherein they had shown all the cheques to have been received. I had given the certificate. I did not expect cheques issued by the promoters of the Company will bounce, keeping in view of the track record and reputation of the Company."***

Similarly, to the notice issued by the Assistant Secretary of the Institute dated 10.12.2003, the respondent submitted his explanation by his letter dated 29.02.2004 as follows:

> ***"We have issued a certificate dated 9th June 1995 stating that Promoters Contribution of Rs.225 lakhs has been received as per the books of Accountants Maintained by the Company. This certificate was issued after verifying the "Share Application Account maintained in the General Ledger of the Company (Xerox Enclosed), the bank book showing receipt of the payments (in the form of Cheques deposited) into the State Bank of Mysore & State Bank of Mysore And the bank deposit slip counterfoils duly bearing the bank acknowledgments of the cheques deposited.***
>
> ***As alleged by SEBI as to why we have not verified the Bank Statement Regarding Realization of the cheques we once again reiterate that as upto 9th June 1995 no cheques of***

the promoters had bounced and hence we had no reason to believe that any cheques issued by the promoters could bounce.

As you will be aware that the certificate issued by us clearly states as under:- "We the Statutory Auditors of Ritesh Polyesters Limited, Secunderabad, hereby certify and confirm that as per books of Accounts maintained by the Company the Company has received Rs.2,25,000.00 as share application money from promoters, directors, their friends and Associates as on 9th June 1995." Hence it has been wrongly alleged by SEBI that we have given a false certificate and aided and abetted the Promoters in fraudulent activities by giving a false certificate.

It has been wrongly alleged by SEBI that Promoters Contribution only Rs.35 Lakhs was received as on 9th June 1995. As a matter of fact Rs.153.2 lakhs was received and only the following cheques of the two promoters has bounced viz. 1. Surender Kumar Agarwal Rs.44.40 lakhs & 2. Roop Rekha Agarwal Rs.27.40 lakhs. This money was also subsequently received by the Company."

Later, for the notice issued by the Assistant Secretary of the Institute dated 28.07.2005, the respondent submitted his his explanation dated 05.08.2005 as under:-

"As alleged by you that I should have qualified my certificate with a remark "Subject to realisation of the Cheques deposited", I agree that this was an omission on my part but I depose under oath that this was not done with any malified intention nor have I received any Financial benefit in connection with the above.

The above paragraph is based on the facts as on the date of issue of the certificate.

As on the date of issue of the certificate I had no reason to verify the source of money received from Deepak Agarwal & Ritesh Agarwal as their contribution towards promoters contribution to Equity in the Company.

The above explanation is based on the belief I had on the date of issue of the certificate.

As regards the M/s Pratha Investments I categorically affirm that M/s. Pratha Investments is not a firm owned by me and is neither run by me.

The above affirmation is based on facts.

Finally I admit that there has been professional lapse on my part in not qualifying my certificate with the caption "Cheques are subject to realisation". I request the Office bearers to kindly neglect the lapse on my part as the same has not been done wilfully and no monetary benefit has been received by me. In view of the above I once again state that I have not acted with any prejudicial interest to cheat or misguide any investor nor have I aided & abetted the Promoters in any Fraudulent Activities."

In the enquiry held by the Committee, on 29.11.2008 at 10.10 a.m. at the office of the Institute at Chennai, the respondent was examined and, for the question put to him by the President "***What do you want to say in your defence***?", he gave the following answer:

"I gave a certificate on 9th June, 1995 and on that date the cheques were deposited and because the cheques could not cleared on that day and subsequently I appeared before the SEBI they told me that you should have subsequently withdrawn the certificate if you had come to know that the cheques are not cleared. I told them that that is the work of Merchant Bank and they are monitoring the day to day movement of the funds. I cannot go and monitor the day to day movement of the funds in their Company and based on their track record whatever cheques they have earlier deposited got cleared that is only one time that Rs.37 lacs cheques not cleared. That was the only plea which I took before the SEBI and I also taking before the Disciplinary Committee."

Both during investigation by SEBI, and in the enquiry by the Committee, there are clear and unequivocal admissions by the respondent regarding his professional lapse in issuing a certificate certifying that the Promoters had contributed Rs.2,25,00,000/- for allotment of shares, and to have confirmed receipt of money towards 15,00,000 equity shares of Rs.10/- each at a premium of Rs.5/- per share. He also admitted to have issued a certificate without

qualifying it as "***subject to realisation of the Cheques deposited***." These admissions suffice to show the lapses on the part of the respondent.

Though the amount received towards the capital contribution of the promoters was only Rs.35,00,000/-, the respondent had certified that Rs.2,25,00,000/- was received by the company towards promoters contribution, though the cheques issued against the balance amount were dishonoured on presentation.

Admission is a statement, [oral or documentary or contained in electronic form], which suggests an inference as to any fact in issue or relevant fact, and which is made by any of the persons, and under the circumstances, mentioned in the Evidence Act. Admissions are not conclusive proof of the facts admitted, but may operate as estoppel under Section 31 of the Evidence Act.

According to Section 58 of the Evidence Act no fact need be proved in any proceeding which the parties thereto or their agents agree to admit at the hearing or which, before the hearing, they agree to admit by any writing under their hands, or which by any rule or pleading in force at the time they are deemed to have admitted by their pleadings and the Court may, in its discretion, require the facts admitted to be proved otherwise than by such admission. Therefore, an admission in writing need not be proved, more so as the strict rules of the Evidence Act are not applicable to disciplinary proceedings. The admissions, extracted above, are made by the respondent in writing and they need not therefore be proved by examining any witness.

The Disciplinary Committee, based on the admission made by the respondent both before the SEBI in writing and before the Committee, concluded that the respondent had committed a grave

irregularity in issuing the certificate and held him guilty. These findings of the Disciplinary Committee was accepted by the Council also. Sri C.V. Rajeeva Reddy, learned counsel for the Institute, has contended that the admission made by the respondent is sufficient to conclude that he was grossly negligent in issuing the certificate dated 09.06.1995 certifying that the entire promoters' contribution had been received by the company.

The relevant portion of the certificate issued by the respondent is as under:

> "We the statutory Auditors of Ritesh Polysters Limited, Secunderabad, hereby certify and confirm that as per the books of accounts maintained by the company, the company has received Rs.225 lakhs (Rupees Two crores twenty five lakhs only) as share application money towards 15,00,000/- equity shares of Rs.10/- each at a premium of Rs.5/- per share from the promoters, directors, their friends and associates as on 9th June 1995."

The respondent certified that an amount of Rs.2,25,00,000/- was received by the company towards promoters contribution, though the amount received towards promoters contribution was only Rs.35,00,000/- and the cheques issued against the balance amount had bounced. However, shares worth Rs.2,25,00,000/- was allotted to the promoters by the company. On being asked by SEBI of the basis on which he had given the certificate regarding receipt of promoters' contribution in full, the respondent replied that he had verified the bank book maintained by the Company, wherein they had shown receipt of the above cheques, he did not expect that the cheques issued by the promoters would bounce, and he had issued the certificate keeping in view the track record of the promoters.

Admissions are of two types, one is judicial admission and another is evidentiary admission. Admissions are not conclusive proof, but the admissions estop the person who made such admission. When a judicial admission is made in the pleadings or in any document regarding a particular fact in issue, such fact need not be proved by adducing evidence in view of Section 58 of the Indian Evidence Act. It is settled law that admission is the best piece of evidence. The Supreme Court, in "**Sita Ram Bhau Patil Vs. Ramachandra Nago Patil[19]"**, held:-

> *"Admission is the best piece of substantive evidence that an opposite party can rely upon, though not conclusive, is decisive of the matter, unless successfully withdrawn or proved erroneous. Admission may in certain circumstances, operate as an estoppel. The question which is needed to be considered is what weight is to be attached to an admission and for that purpose it is necessary to find out as to whether it is clear, unambiguous and a relevant piece of evidence, and further it is proved in accordance with the provisions of the Evidence Act. It would be appropriate that an opportunity is given to the person under cross-examination to tender his explanation and clear the point on the question of admission."*
>
> *In view of the above, the law on the admissions can be summarised to the effect that admission made by a party though not conclusive, is a decisive factor in a case unless the other party successfully withdraws the same or proves it to be erroneous. Even if the admission is not conclusive it may operate as an estoppel. Law requires that an opportunity be given to the person who has made admission under cross-examination to tender his explanation and clarify the point on the question of admission. Failure of a party to prove its defence does not amount to admission, nor it can reverse or discharge the burden of proof of the Plaintiff."*

In another decision "**Nagubai Ammal and others Vs. B. Shama Rao[20]"** the Supreme Court held:-

> *"Admission made by a party is admissible and best evidence, unless it is proved that it had been made under a mistaken belief. While deciding the said case reliance has been*

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[19] AIR 1977 SC 1712
[20] AIR 1956 SC 593

placed upon the judgment in Slatterie v. Pooley *(1840) 6 M & W 664, wherein it had been observed "What a party himself admits to be true, may reasonably be presumed to be so."*

In "**Union of India (UOI) v. Ibrahim Uddin**[21]" the Supreme Court observed that admission are the best piece of evidence and can be relied on by the Courts in deciding any issue. In "**Amba Lal v. Union of India**[22]" the Constitution Bench of the Supreme Court held that for a decision to be based on admission, it must be in writing; and the admission is more satisfactory if a body entrusted with statutory functions takes necessary precautions when its decision is mainly to depend upon such admission.

If the above principle, laid down by the Supreme Court, is applied to the facts of the present case, the admissions made by the respondent, which are extracted in the earlier paragraphs, suffice to conclude that there is a clear professional lapse on the respondent's part as he failed to issue a qualified certificate that receipt of the amount was subject to realisation of the cheques. In view of the law declared by the Supreme Court in the decisions referred supra, we have no hesitation to hold that admission is the best piece of evidence since the respondent failed to explain under what circumstances such admission was made. Accordingly, the point is held in favour of the Institute, and against the respondent.

POINT Nos: 4, 5 and 7:

The genesis, for the Institute to conduct an enquiry against the respondent, is the investigation report of SEBI in relation to the certificate attached to the prospectus, wherein the respondent had certified that the promoters had contributed Rs.225 lakhs towards

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[21] (2012) 8 SCC 148
[22] AIR 1961 SC 234

their share capital, and 15,00,000 shares were allotted to the promoters and their friends, though an amount of Rs.35,00,000/- alone was received towards contribution from the promoters. The fact that the respondent had issued the certificate, certifying that an amount of Rs.225 lakhs was received by Ritesh Polysters Limited, is not in dispute.

Ritesh Polysters Limited (for short, hereinafter referred to as "Company") is a company originally incorporated as Srinath Synthetics Private Limited on 2nd September, 1988, and was renamed as Ritesh Polysters Private Limited on 21.04.1993. The said company was converted into a Public Limited Company on 07.05.1993 in terms of the special resolution dated 01.03.1993, and its registered office was located at 604, Swapnalok Complex, Sarojini Devi Road, Secunderabad. The authorised capital of Ritesh Polysters Private Limited, prior to the public issue on 12.06.1995, was 7,25,00,000/- (72,50,000 shares of Rs.10/- each). Its issued and paid up capital was only Rs.2,49,60,000/- (24,96,000 shares of Rs.10/- each). After its conversion as a Public Limited Company, the company proposed to issue 45,00,000 shares to the public inviting a share capital of Rs. 6,75,00,000 from the public at large, fixing the value of a share at Rs.10/- each with a premium of Rs.5/- per share. The net offer to the public was 30,00,000 shares for Rs.4,50,00,000/- at Rs.10/- per share with a premium of Rs.5/- per share. 15,00,000 shares were reserved for the promoters amounting to Rs.2,25,00,000/-, and several shares were reserved for preferential allotment. The Company issued a notification inviting contribution from the public for allotment of shares; the issue opened on 12.06.1995, the earliest closing was on 16.06.1995, and

the final closing was on 22.06.1995. The Central Bank of India, Merchant Banking Division, Mumbai, and Rajshree Fiscal Services Limited, Mumbai were the lead managers to the issue, whereas Sriven Corporate Services Private Limited, Hyderabad, Dhanalakshmi Bank of India, Abids Road, Hyderabad, and Bhagwandas Gordhandas Financial Private Limited, Mumbai were the Co-Managers to the issue. The respondent, M/s Gang and Company, was the statutory Auditor.

After the public issue, SEBI conducted investigation and found that, as per the prospectus dated 30.03.1995, 15,00,000 shares were reserved for promoters, their relatives and friends on a firm allotment basis at Rs.10/- per share with a premium of Rs.5/- per share; the total contribution, by the promoters, was Rs.2,25,00,000/- which was required to be credited before the opening of public issue; and the respondent had certified receipt of the same. SEBI addressed a letter dated 28.06.2000 to the Company to furnish details of the promoters contribution. In response thereto, vide letter dated 05.07.2000, the Company submitted details of the promoters contribution as follows:

Name of the Promoter	Cheque No.	Contribution	Date	Drawn on
Ritesh Exports Ltd	441810	400000	8/6/95	State Bank of Patiala
	441811	450000	8/6/95	State Bank of Patiala
	441812	450000	8/6/95	State Bank of Patiala
	441813	450000	8/6/95	State Bank of Patiala
	441814	450000	8/6/95	State Bank of Patiala
	441815	450000	9/6/95	State Bank of Patiala
	441816	450000	9/6/95	State Bank of Patiala
	441817	450000	9/6/95	State Bank of Patiala
	441818	450000	9/6/95	State Bank of Patiala
	441819	450000	9/6/95	State Bank of Patiala
	441820	450000	9/6/95	State Bank of Patiala
	441821	450000	9/6/95	State Bank of Patiala
	441822	450000	9/6/95	State Bank of Patiala
	441823	50000	9/6/95	State Bank of Patiala

Sh.Surender Kumar Agarwal	508981	300000	9/6/95	State Bank of Patiala
	508984	450000	9/6/95	State Bank of Patiala
	508985	450000	9/6/95	State Bank of Patiala
	508986	390000	9/6/95	State Bank of Patiala
	508987	390000	9/6/95	State Bank of Patiala
	508988	450000	9/6/95	State Bank of Patiala
	508989	450000	9/6/95	State Bank of Patiala
	508990	300000	9/6/95	State Bank of Patiala
	508991	390000	9/6/95	State Bank of Patiala
	508992	390000	9/6/95	State Bank of Patiala
	508993	390000	9/6/95	State Bank of Patiala
	508994	390000	9/6/95	State Bank of Patiala
	508995	450000	9/6/95	State Bank of Patiala
	508982	200000	9/6/95	State Bank of Patiala
	508983	550000	9/6/95	State Bank of Patiala
Smt. Roop Rekha Agarwal	417280	2739500	9/6/95	State Bank of Patiala
Sh.Ritesh Agarwal	819066	150000	9/6/95	State Bank of Patiala
	819067	100000	9/6/95	State Bank of Patiala
	819073	450000	9/6/95	State Bank of Patiala
	819074	300000	9/6/95	State Bank of Patiala
	819075	50000	9/6/95	State Bank of Patiala
Sh. Deepak Agarwal	818144	150000	9/6/95	State Bank of Patiala
	818145	150000	9/6/95	State Bank of Patiala
	818149	700000	9/6/95	State Bank of Patiala
	818150	50000	9/6/95	State Bank of Patiala

Again SEBI, vide letter dated 30.08.2000, requested State Bank of Patialia, R.P. Road Branch, Secunderabad to furnish details regarding realisation of the cheques mentioned above. By its letter 05.09.2000, State Bank of Patiala informed that the cheques were returned unpaid, and the details of the unpaid cheques were as follows.

Name of the Promoter	Cheque No.	Date	Amount
Sh.Surender Kumar	508990 508983	9/6/95	3,00,000
	508985 508988-89	9/6/95	5,50,000
	508995 508986-87	9/6/95	4,50,000
	508991-94	9/6/95	9,00,000
		9/6/95	4,50,000
		9/6/95	7,80,000
		9/6/95	15,60,000
Smt.Roop Rekha Agarwal	417280	9/6/95	27,39,500
	Total amount unpaid		77,29,500

On receipt of the above details from State Bank of Patiala, SEBI again addressed a letter to Company to clarify how the promoters had contributed money for allotment of 15,00,000 shares. By letter dated 17.06.2002, the Company submitted that three cheques worth Rs.71,79,500/- were returned unpaid for

certain reasons, but the company received the amount thereafter on different dates during 1995-96. From the details furnished by Company, it came to light that cheques worth Rs.49,90,000/-, issued by Sh.Surendra Agarwal towards promoters contribution, had bounced. Against this an amount of Rs.44,65,000/- was stated to have been brought on different dates between 14.06.1995 and 26.03.1996. Similarly, Ms.Roop Rekha Agarwal had issued a cheque for Rs.27,39,500/- towards promoters contribution, which was also dishonoured by the payee bank. Against this an amount of Rs.27,67,750/- was stated to have been brought on different dates between 02.08.1995 and 31.01.1996. Thus, the Company is stated to have received Rs.31,50,000/- as "investments before 01.06.1995" from Ritesh Exports Limited, Rs.18,97,500/- from Sh.Surendra Kumar Agarwal and Rs.8,23,000/- from Smt.Roop Rekha Agarwal, but the certificate issued by the respondent herein, annexed to the prospectus, is silent about the said investments. Entries were made in the accounts to justify the difference between the contribution amount received as shown in the prospectus and the actual cheques received from the promoters, which were honoured by the bank. In fact, no cheque for Rs.31,50,000/- was received from Ritesh Exports Limited. Similarly, no cheques were received for Rs.18,97,500/- from Sh.Surendra Kumar Agarwal or for Rs.8,23,000/- from Smt.Roop Rekha Agarwal before 01.06.1995. The promoters, thus, failed to contribute Rs.58,70,500/-prior 01.06.1995. Added to that is the shortfall in contribution on account of the bounced cheques. The following amounts were shown to have been received by the Company, one day prior to the opening of the issue i.e. 11.06.1995.

Ritesh Exports Limited	Rs.58.50 lakhs
Sh.Surendra Kumar Agarwal	Rs.13.00 lakhs
Sh.Deepak Agarwal	Rs.10.50 lakhs
Shri. Ritesh Agarwal	Rs.10.50 lakhs
Total	Rs.92.50 lakhs

It was also shown that Ritesh Exports Limited had brought Rs.22,00,000/- as promoters contribution on 08.06.1995, and Rs.36,50,000/- on 09.06.1995, by way of an Overdraft facility from the bank. From the bank statements of the Company it was evident that, on 09.06.1995, they had transferred Rs.36,50,000/- back to Ritesh Exports Limited. Thus, the Company had shown that Rs.58,50,000/- was received as promoters contribution from Ritesh Exports out of which Rs.36,50,000/- was, in fact, transferred back to them by the Company. In effect, Ritesh Exports Ltd had contributed only Rs.22,00,000/-. While Shri Deepak Agarwal and Sh.Ritesh Agarwal had allegedly contributed Rs.10,50,000/- each towards promoters contribution on 09.06.1995, the bank statements showed that the Company had advanced Rs.10,50,000/- each to these two persons, having routed it through the account of M/s.Pratha Investments. In short, the Company itself gave Rs.22,00,000/- to M/s.Pratha Investments, which, in turn, paid Rs.10,50,000/- each to Shri Deepak Agarwal and Shri Ritesh Agarwal on the same day i.e. 09.06.1995. Subsequently, Shri Deepak Agarwal and Shri Ritesh Agarwal gave this money back to the Company as promoters contribution. The payments made by the promoters were only book entries, and no amount was actually paid by the promoters towards their contribution to the capital of the Company.

SEBI addressed a letter to Shri Lohia to submit the bank statement of Shri Surendra Kumar Agarwal to find out the truth regarding the alleged contribution made by Shri Surendra Kumar Agarwal, but to no avail. The investigation by SEBI disclosed that only Rs.22,00,000/- was received from Ritesh Exports and Rs.13,00,000/- from Shri Surendra Kumar Agarwal, as promoters contribution, one day prior to the issue, instead of the Rs.2,25,00,000/- shown to have been received by the company in the certificate issued by the respondent. It is evident that the company had allotted shares worth Rs.2,25,00,000/- to the promoters when it has actually received only Rs.35,00,000/-.

In the prospectus of the company, it is specifically mentioned that the amount mentioned in D above will be brought in by the promoters before the date of opening of the public issue, and the same shall be certified with a certificate from the Auditors. Later, the Auditor issued a certificate certifying that the promoters had contributed Rs.2,25,00,000/- furnishing the following details indicating the allotment of shares proportionate to their contribution.

Name of the Share Holder	No.of shares	Amount
Ritesh Exports Ltd.	6,00,000	90,00,000
Surender Kumar Agarwal	5,22,500	78,37,500
Roop Rekha Agarwal	2,37,500	35,62,500
Deepak Agarwal	70,000	10,50,000
Ritesh Agarwal	70,000	10,50,000

According to SEBI, the contribution actually received by the Company was only Rs.35,00,000/-, despite which the promoters were allotted 15,00,000 shares worth Rs.2,25,00,000/- and the statutory Auditor, i.e respondent herein, had certified that

Rs.2,25,00,000/- was received by the Company before the public issue. The certificate, issued by the respondent, is evidently false and, consequently, SEBI addressed a letter to the Institute to take appropriate action against the statutory Auditor, i.e the respondent herein.

On receipt of the letter from SEBI, the Institute followed the prescribed procedure, framed charges, initiated proceedings and constituted a Disciplinary Committee. The Disciplinary Committee, in turn, after following the prescribed procedure, submitted its report which was accepted by the Institute after affording a reasonable opportunity of being heard to the respondent, and on recording a finding that the respondent was guilty of professional misconduct. The Institute has proposed imposition of the penalty of removal from the Register of Members for a period of 3 years i.e. suspension from practice for a period of three (3) years, and has referred the matter to this Court under Section 21 (5) and (6) of the Chartered Accounts Act, 1949.

The basis for the Institute to initiate proceedings is the investigation report of the SEBI and, during investigation, a lot of material was collected from Rajashree Fiscal Services Limited, State Bank of Patiala and the Company. The respondent submitted his explanations vide letters dated 29.02.2004 and 05.08.2005 that it was merely a professional lapse on his part in not qualifying the certificate with the caption “cheques are subject to realisation”. While admitting his professional lapse in issuing such a certificate, the respondent contended that he did not indulge in any fraudulent transactions, and requested that his professional lapse be ignored, and all further proceedings be dropped.

In this context it is necessary to note that SEBI issued a circular directing companies to annex a certificate, either from a Chartered Accountant or a Company Secretary in practice, to the effect that the promoters contribution, including premium, had been brought in its entirety, in advance before the public issue opened; the certificate should be forwarded to SEBI at least one day prior to the date of opening of the issue; and the certificate should be accompanied by a list of names and addresses of friends, relatives and associates who have contributed to the promoters quota, along with the amount of subscription made by each of them. It is in compliance with the circular instructions issued by SEBI, that the respondent issued the certificate certifying that the promoters contribution of Rs.2,25,00,000/- was received, without qualifying that it was subject to realisation of the cheques.

The main contention of Sri C.V. Rajeeva Reddy, learned counsel for the Institute, is that the duty of the Auditor is to verify each and every account, and certify the truth or otherwise in the entries made in the accounts; the respondent failed to discharge his duties as a Statutory Auditor of the company; he had issued a certificate to the effect that the company had received Rs.2,25,00,000/- before opening of the public issue, and before contribution was invited from the public for allotment of shares; and, thereby, the respondent was guilty of gross negligence in issuing the certificate.

Per contra, Sri Ashok Anand Kumar, learned counsel for the respondent, would contend that the respondent had no intention to defraud either SEBI or the public at large while issuing the certificate; he bonafidely believed that the cheques would be

realised; when the negligence attributed to the respondent is not culpable, intentional or planned, he cannot be found guilty of gross negligence under Section 21 (7) read with Section 22 of the Act; mere negligence is not sufficient to take action against the respondent for professional misconduct, unless it is proved that it is intentional and planned; in the present case, there is no material to establish that the respondent was grossly negligent in discharging his duties; and he cannot, therefore, be found guilty of the misconduct defined under Section 22 of the Act. Learned Counsel would request this Court to exonerate the respondent of the charges.

It is not only the duty of the Auditor to verify whether the promoters contribution was actually received, but also to ensure that the company had received the money due towards promoters capital contribution, before issuing the certificate. In "**Alexander v. Cambridge Credit Corporation**[23]" the test of common sense was applied to find out whether the relevant act or omission was a cause. "Common sense" is, however, an uncertain guide. One person's common sense may be another's nonsense. In "**Leeds Estate Building and Investment Company v. Shepherd**[24]" and "**In Re The Westminster Road Construction & Engineering Co Ltd**[25]" the issue of inflated profit figures in audited accounts, and payment of tax on the inflated profit figures fell for consideration, and it was held that the auditors were liable to the company towards dividends, cost of recovering the excess tax, and any tax not recovered.

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[23] (1987) 9 NSWLR 310
[24] (1887) 36 Ch.D. 787
[25] (1932) Acct LR 38

"**In Re London General Bank (No. 2)**[26]" a similar question regarding the Auditor's liability came up for consideration, and the Court concluded that, although it was not the duty of the Auditors of a company appointed under the Companies Act, 1879 to consider whether its business is prudently or imprudently conducted, it is their duty to consider and report to the shareholders whether the balance-sheet exhibits a correct view of the state of the company's affairs, and the true financial position of the company at the time of the audit. They must ascertain this by examining the books of the company, and must take reasonable care that what they certify as to the company's financial position is true. And except in very special cases it is their duty to place before the shareholders the necessary information as to the true financial position of the company, and not merely to indicate the means of acquiring it.

Similarly "**In Re Kingston Cotton Mills Co. (No. 2)**[27]", the Court held that, where an officer of a company has committed a breach of his duty to the company, the direct consequence of which has been a misapplication of its assets, for which he could be made responsible in an action, such breach of duty is a "misfeasance" for which he may be summarily proceeded against under the Companies Act, and it is not necessary that an action should be brought. The Auditors relied on certificates, wilfully false, given by J., one of the directors who was also the manager, as to the value of the stock-in-trade. Dividends were paid for some years on the footing that the balance-sheets were correct; but if the stock-in-trade had been stated at its true values it would have appeared that there were no profits out of which dividend could be declared. If the

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[26] (1895) 2 Ch. 673
[27] (1896) 2 Ch. 279

Auditors had verified the books, and had added to the stock-in-trade, at the beginning of the year, the amounts purchased during the year, and deducted the amounts sold, they would have seen that the stock-in-trade at the end of the year was so large as to call for an explanation, but they did not do so. That, it being no part of the duty of the Auditors to take stock, they were justified in relying on the certificates of the manager, a person of acknowledged competence and high reputation, and were not bound to check his certificates in the absence of anything to raise suspicion, and that they were not liable for the dividends wrongfully paid. An Auditor is not bound to be suspicious where there are no circumstances to arouse suspicion, and he is only bound to exercise a reasonable amount of care and skill. The real controversy was about the guilt of the Auditors due to breach of their duty to the company. To decide the question, it was necessary to consider what their duty was; whether they had performed, it and in what aspect they failed to perform it? The duties of the Auditor was considered by the Chancery Division in "**In Re London and General Bank (No.2)** (referred supra).

Relying on the above said judgments of the Chancery Division, the Supreme Court, in "**Institute of Chartered Accountants of India v. P.K.Mukherji**[28]", held:-

> "It is not possible for us to accept this argument. Respondent No. 1 owed a duty to all the subscribers of the Provident Fund who were in the position of beneficiaries. It is not correct to say that respondent No. 1 owed a duty only to the Company which had appointed him to perform the auditing. The contributors to the Provident Fund had a beneficial interest in the Fund and the primary object of auditing the Fund was to appraise

[28] AIR 1968 SC 1104

them of the true financial position of the accounts and investments made from time to time. Respondent No. 1 therefore owed a duty to the contributors to the Provident Fund for making a true report to them of the financial position. In other words, the auditing was intended for protection of the beneficiaries and the Auditor was expected to examine the accounts maintained by the trustees with a view to inform the beneficiaries of the true financial position. The Auditor is, in such a case, under a clear duty towards the beneficiaries "to probe into the transactions" and to report on their true character. In our opinion, the legal position of the Auditor in the present case is similar to that of the Auditor under the Indian Companies Act, 1956. In such a case the audit is intended for the protection of the shareholders and the Auditor is expected to examine the accounts maintained by the Directors with a view to inform the shareholders of the true financial position of the Company. The Directors occupy a fiduciary position in relation to the shareholders and in auditing the accounts maintained by the Directors the Auditor acts in the interest of the shareholders who are in the position of beneficiaries. In London Oil Storage Co. Ltd. v. Seear, Hasluck & Co., (Dicksee on Auditing., 17th Edn., p. 632.) Lord Alverstone stated as follows :

"He must exercise such reasonable care as would satisfy a man that the accounts are genuine, assuming that there is nothing to arouse his suspicion of honesty and if he does that he fulfils his duty; if his suspicion is aroused, his duty is to 'probe the thing to the bottom' and tell the directors of it and get what information he can."

It was therefore no defence for respondent No. 1 in this case to say that he had disclosed the irregularity to the Company by this letter dated May 25, 1955. On the contrary it was a breach of duty on his part not to have made a disclosure thereof to the beneficiaries of the Provident Fund in the statement of accounts for the year 1954 which he signed on June 30. 1955."

In "**Institute of Chartered Financial Analysts of India v. Council of the Institute of Chartered Accountants of India**[29]" the Apex Court, while considering the misconduct of a clerk, drew a distinction between a misconduct committed by an employee and professional misconduct and held that, in case of professional

[29] (2007) 12 SCC 210

misconduct, "***the person in the profession precisely knows what is expected of him.***"

The prospectus is a special document and it is the duty of the Auditor to issue a certificate, regarding receipt by the company of entire sums due towards promoters contribution, before shares are offered to the public at large. If a false certificate is issued by the Auditor, it would amount to his failure to discharge his statutory duties, as he must be presumed to be aware of the consequences that flow from such gross negligence of a false certification, as the invitation to the public, to subscribe to the shares of the company, is based on the false representation that the promotees had paid the entire amount due, towards their capital contribution, to the company.

The Chartered Accountant is a professional whose expertise in accountancy is acknowledged. He is a member of an expert body and of a premier institute in India. The certificate issued by an Auditor has its own impact on the public at large, as it is largely on the basis of this certificate that the general public subscribe to the shares of the company. Reckless certification by an Auditor, which has resulted in the public being misled into subscribing to the shares of the company in the public issue, would undoubtedly amount to gross negligence. Large sections of society rely on the certification by the Chartered Accountants for taking many vital decisions. It is imperative that utmost care and caution is exercised in issuing such certificates, and the objectivity, integrity, reliability and credibility of the information therein is ensured. Of late, several instances have come to light where, due to the erroneous/ambiguous advice tendered by Chartered Accountants,

borrowal accounts have had to face quick mortality resulting in huge losses for banks and financial institutions. To ensure public faith and protect gullible small investors from being cheated of their life savings, the Institute should ensure that its members possess competence of a high order, their character is above board, and their integrity beyond reproach. Chartered Accountants are responsible to the public for their actions, as heavy reliance is placed on their credibility by the general public consisting of investors, banks, financial institutions, governments etc. The Chartered Accountant's duty is not merely to his client, but extends to various segments of society, more particularly in the commercial field, on whose expertise, integrity and impartiality they rely on in taking various decisions.

Larger public interest would be served only if Chartered Accountants maintain high ethical standards apart from her standards of expertise in accountancy and related fields. In the rare instances where Auditors are found to lack integrity, objectivity, professional competence, and to have failed to exercise due care and caution in issuing certificates, larger public interest would be served only if they are sternly dealt with. The certificate issued by the auditor is, in this case, the basis for the general public subscribing to the shares of the company. The present case best illustrates how a false and misleading certification by the Auditors, has resulted in the general public being cheated into believing that the promoters of the company had invested Rs.2.25 crores in its capital, before the public at large were invited to invest in the share capital of the company.

Certification is a formal procedure by which an accredited or authorized person or agency assesses and verifies the attributes characteristics, quality, qualification or status of individuals or organisations, goods or services, procedures or processes, or events or situations, in accordance with established requirements or standards. Certification refers to the confirmation of certain characteristics of an object, person, or organisation. This confirmation is often, but not always, provided by some form of external review, education, assessment, or ***audit***. Certification means authenticity of a particular fact on verification, and is not a mere statement. Therefore certification by a statutory Auditor regarding contribution of the promoters and allotment of shares to them, without disclosing the true facts to the general public that the contribution had not been actually received, and that the cheques received from them was ***"subject to realisation of amount"***, amounts to misleading the general public to subscribe to the shares of the company in the public offer of a huge sum of Rs.4,50,00,000/- (Rupees four crores fifty lakhs).

As per Section 65 of the Companies Act, 1956, a statement included in a prospectus shall be deemed to be untrue, if the statement is misleading in the form and context in which it is included *inter alia* in the prospectus itself, or is contained in any report or memorandum appearing on the face thereof or by reference incorporated therein or issued therewith and where the omission from a prospectus of any matter is calculated to mislead, the prospectus shall be deemed, in respect of such omission, to be a prospectus in which an untrue statement is included. The liability accrues where any person subscribes for any shares or debentures

on the faith of the prospectus for any loss or damage he may have sustained by reason of an untrue statement included therein. A representation in the prospectus regarding contribution of the promoters, if found untrue, may well result in the general public being mislead into seeking allotment shares based on such misrepresentation. The certification by the statutory auditor has resulted in the general public, who reposed faith on his statement, being mislead into subscribing to the shares of the company placing faith on such a certificate.

The facts before us are that the respondent is a statutory auditor of Ritesh Polyster Limited, which was registered under the Companies Act as a private limited company and was later converted into a public company. The company invited subscription of capital from the public for allotment of shares by way of public issue, annexing a certificate from the statutory auditor regarding receipt of money towards the promoters contribution. The auditor confirmed receipt of Rs.2.25 crores, and allotment of 15,00,000 shares to the promoters, their friends and relatives. It is on the faith of the certification, and confirmation, that the public invested money in the company for allotment of shares. In fact, the company did not receive Rs.2,25,00,000/- but was only received Rs.35,00,000/- towards promoters contribution but still allotted 15,00,000 shares worth Rs.2,25,00,000/-. It is evident that it was a fraudulent invitation to subscribe to the share capital of the company, and the respondent cannot distance himself from the corporate fraud, since he certified and confirmed the alleged contribution by the promoters, more particularly the receipt of

Rs.2,25,00,000/-, though the actual amount received by the company, towards promoters contribution, was only Rs.35,00,000/-

As the certificate issued by him, as the statutory auditor of the company, regarding receipt of consideration of Rs.2.25 crores from the promoters towards subscription of share capital under the promoters quota, which forms the basis for inviting subscription from the public, has been found false, it amounts to gross negligence under the Act. In fact, such gross negligence was detected during investigation by the SEBI under Section 11 of the SEBI Act, and was the basis for the statement/complaint made by them to the Institute which eventually resulted in the Council recommending removal of the name of the respondent from the Register of Members for a period of three (3) years, i.e. suspension from practising as a Chartered Accountant, as the conduct of the respondent would fall within Section 21 (7) of the Act.

Section 22 of the Act defines professional misconduct. According to it, the expression ***"professional misconduct"*** shall be deemed to include any act or omission specified in any of the Schedules, but nothing in this Section shall be construed to limit or abridge in any way the power conferred or duty cast on the Council under sub-section (1) of Section 21 to inquire into the conduct of any member of the Institute under any other circumstances. Thus, the definition of professional misconduct is wider.

The Second Schedule, read with Section 21 (5) and 22 of the Act, prescribes several acts which would fall within the ambit of professional misconduct. They are:

(1) .....

(2) .....

(3) .....

(4) .....

(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 mis-statement 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;

(8) fails to obtain sufficient information to warrant the expression of an opinion or his exceptions are sufficiently material to negate the expression of an opinion;

(9) .....

(10).....

Part II of the Second Schedule specifically refers to professional misconduct, in relation to members of the Institute, generally requiring action by a High Court. Thereunder a member of the Institute, whether in practice or not, shall be deemed to be guilty of professional misconduct, if he contravenes any of the provisions of the Act or the regulations made thereunder; and is guilty of such other act or omission as may be specified by the Council in this behalf, by notification in the Gazette of India. The contravention, attributed to the respondent, is violation of Clause (7) of Part- I of Schedule II i.e. grossly negligent in the conduct of his professional duties.

As discussed above, the duty of a professional Auditor, among others, is to ascertain the truth, and disclose true facts to the public in the certificate of confirmation issued by him along with the prospectus. In the present case, the respondent confirmed and certified that the company has received Rs.2,25,00,000/- as share application money for allotment of 15,00,000 equity shares at

Rs.10/- per share at a premium of Rs.5/- per share from the promoters, directors, their friends and relatives as on 09.06.1995. The certification and confirmation by the respondent, that the company had received Rs.2,25,00,000/- from the promoters, without disclosing that cash, for such allotment, had not been received, amounts to failure to exercise due care and caution before certification. The minimum care which an auditor ought to have taken was to verify whether the promoters had sufficient balance in their account for the cheques, to be honoured on its presentation, besides certifying that the cheques were subject to realisation. It is not for him to blindly accept what the promoters inform him, as he owes a greater duty to the general public who, placing reliance on his certificate, had subscribed to the shares of the company. The action of the respondent is in dereliction of his statutory duty, and is nothing but gross negligence. The respondent, while answering questions put to him during investigation by SEBI, stated that he had issued a certificate based on the cheques received by the company and keeping in view the track record and reputation of the promoters of the company. The respondent, as a statutory Auditor, was not supposed to certify and confirm receipt of Rs.2,25,00,000/- towards promoters contribution based on the alleged reputation of the promoters, and it was his obligation to verify whether payment was actually received. Though he was required to verify receipt of payment for allotment of shares to the promoters, the respondent disowned his responsibility, and blindly certified and confirmed receipt of Rs.2,25,00,000/- towards promoters contribution. The respondent, as a statutory Auditor of the company, must be presumed to aware of his obligations to the general public who,

relying on his certification, had invested in the share capital of the company despite which he issued the certificate based on the alleged reputation of the promoters, a factor wholly irrelevant for issuing such a certificate.

Sri C.V. Rajeeva Reddy, learned counsel for the Institute, would contend that issue of such certificate directly attracts Clause (7) of Part I of the Second Schedule i.e. gross negligence of a member of the Institute in the conduct of his professional duties. He relied on several judgments of various High Courts, and the Supreme Court, in "**Deputy Secretary to the Government of India, Ministry of Finance (Department of Economic affairs), v. S.N.Das Gupta**[30]"; "**Council of the Institute of Chartered Accountants of India v. V.I.Oommen**[31]", "**Council of the Institute of Chartered Accountants of India v. Shri Gyan Prakash Agarwal**", (unreported judgment of the Delhi High Court in C.A. Reference No.1/2014 and CM No.3363/2014 dated 30.04.2015) and "**Chartered Accountants of India, Indraprastha Marg, New Delhi v. Shri S.Giridharan, Chartered Accountant**", (unreported judgment of High Court of Karnataka at Bengaluru in Civil Petition No.191 of 2012).

Sri Ashok Anand Kumar, learned counsel for the respondent, would submit that mere negligence does not constitute misconduct to hold a member guilty under Section 21 (5) read with clause (7) of Part I of Second Schedule, and it is only gross negligence in discharging his duties by a professional Chartered Accountant which attracts the penal clause; and, unless, the Court records a finding that the negligence held established amounts to gross

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[30] AIR 1956 Calcutta 414
[31] AIR 1996 AP 254

negligence, the respondent is not liable for any punishment. He has also placed reliance on several judgments of various Courts.

As seen from Clause (7) of Part I of Schedule II read with Section 21 (5) and 22 of the Act, mere negligence by itself would not constitute misconduct, as the word negligence is prefixed with the word "gross". What is gross negligence is a question required to be decided by us.

The Act does not define gross negligence, but it is defined in Black's Law Dictionary as follows:

Gross Negligence:

> "1.A lack of slight diligence or care. 2. A conscious, voluntary act or omission in reckless disregard of a legal duty and of the consequences to another party, who may typically recover exemplary damages. Also termed reckless negligence; wanton negligence; willful negligence; willful and wanton negligence; hazardous negligence, magna neglegentia. 3. See criminal negligence.
>
> "Negligence is gross if the precautions to be taken against harm are very simple, such as persons who are but poorly endowed with physical and mental capacities can easily take." H.L.A.Hart, "Negligence, Mens Rea and Criminal Responsibility," in Punishment and Responsibility 136, 149 (1968).
>
> "Gross Negligence. As it originally appeared, this was very great negligence, or the want of even slight or scant care. It has been described as a failure to exercise even that care which a careless person would use. Several courts, however, dissatisfied with a term so nebulous..... have construed gross negligence as requiring willful, wanton, or reckless misconduct, or such utter lack of all care as will be evidence thereof..... But it is still true that most courts consider that 'gross negligence' falls short of a reckless disregard of the consequences, and differs from ordinary negligence only in degree, and not in kind."

Similarly, in Law Lexicon by P.Ramanatha Aiyar the word gross negligence is defined as follows:

> Gross negligence, sometimes called 'wilful blindness' is the same thing as 'negligence', with the additional of a vituperative epithet.
>
> The term "gross neglect" means and involves a failure on the part of a person to take such reasonable precautions against the risk of an innocent person being deceived in the circumstances of the particular case.
>
> Gross negligence means some culpable default, not arising merely from want of foresight or mistake of judgment.
>
> Negligence marked by total or nearly total disregard for the rights of others and by total or nearly total indifference to the consequences of an act.

For an act of 'negligence' to constitute 'gross negligence', it must be in reckless disregard of a legal duty and of the consequences to another party, or wilful or voluntary or wanton omission. Negligence is the failure to take reasonable care as an ordinary prudent man, depending upon the circumstances of the case, would take.

As seen from the definition of gross negligence, even an act of omission, or reckless disregard of a legal duty, by a statutory Auditor amounts to gross negligence. In the present facts, the Auditor issued a certificate confirming receipt of Rs.2,25,00,000/- towards promoters contribution, and that 15,00,000 shares, at Rs.10/- per share with premium of Rs.5/-, was allotted though only Rs.35,00,000/- was actually received by the company towards promoters contribution, that too just one day prior to opening of the public issue. The certificate was issued by the respondent without even verifying actual receipt of cash for such allotment, and without qualifying the certificate to the effect that the consideration received was "subject to realisation of the cheque amount". This act of certification by the respondent amounts to gross negligence since he had voluntarily omitted to do so in reckless disregard of his

duty/obligation as the statutory auditor of the company. The certificate issued by the respondent, which was among the documents which formed the basis for inviting contribution from the public towards share capital of Rs.4,50,00,000/-, is a mis-statement in the prospectus which resulted in defrauding investors of the company, other stakeholders, and the public at large.

The words "gross negligence", in the context of the duty of the Directors of the Company, came up for consideration before the Chancery Division "**In Re Brazilian Rubber Plantations and Estates Limited[32]"** and, in the said case, a complaint was made regarding mis-statement by the Directors in the Prospectus which amounted to gross negligence. In **"Lagunas Nitrate Co. v. Lagunas Syndicate[33]"** the word "gross negligence" was defined as follows:

> "Negligence must be not the omission to take all possible care; it must be more blameable than that: it must be in a business sense culpable or gross." That proposition governs this case, and all the cases show that directors must exercise reasonable care and must use their own judgment and not that of others.

In the above decision, a prospectus was issued inviting subscription from the public and the public, who subscribed to the shares on the faith of the statement in the prospectus, had the same knowledge as the directors. All of them knew of the inflation in the price, but had no notice of the dishonesty of Meiter's report. He committed a great fraud, but how could the directors find that out? He had a good position in the city and had been abroad. In March,Hoffman was sent out, with a marked prospectus to report critically on the property, and in April he cabled "***very satisfactory***" and his letter, received on May 31,said "***get transfer through***", and the

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[32] (1911) 1 CH 426
[33] (1899) 2 Ch.392

board could not then repudiate or refuse to make further payments. Where a company is formed, as here, to carry out a particular contract, and they carry it out without knowledge of any wrong, they are not guilty of negligence. The principle of "**Overend & Gurney Co. v. Gibb**[34]" and "**In Re New Mashonaland Exploration Co**.[35]" applies, and the 1st case shows that the company in this case had notice from the prospectus of the increase in price. The Directors had acted based only on Meiter's report, they had given the statement in the prospectus inviting subscription of capital to the company. Therefore, no knowledge was attributable to the Directors, and they were found not guilty.

In the same judgment the Chancery Division observed that the **Director** ***could reasonably be expected to be an honest man and he is not liable for errors of judgment if he committed any***. Further, if Meiter's report was true, and the directors *bona fide* believed it to be true, the contract was a good bargain for the company. The promoters were making only a cash profit of 4000/- out of the 30,000/- and all the rest of the purchase price, 1,20,000/- in shares was paper. Was it therefore such an exorbitant price? Moreover, the prospectus was so framed and the contracts were so disclosed as to conceal the fact that Meiter was one of the sub-vendors.

In the same judgment, the duty and obligations of the Directors towards their company was highlighted, and it was laid down that so long as they act honestly they cannot be made responsible in damages unless guilty of gross negligence. There is admittedly a want of precision in this statement of a director's liability. In truth, one cannot say whether a man has been guilty of

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[34] (1872) L.R. 5 H.L. 480
[35] (1892) 3 Ch. 577

negligence, gross or otherwise, unless one can determine what is the extent of the duty which he is alleged to have neglected? A director's duty has been laid down as requiring him to act with such care as is reasonably to be expected from him, having regard to his knowledge and experience. Hence, he is not bound to bring any special qualifications to his office and when such reasonable care is taken as an ordinary prudent man is expected to take, in the same circumstances, the directors are not liable for such misstatement since they had acted merely on the report of Meiter.

In "**Forder v. Great Western Railway Company**[36]" the expression "wilful misconduct" has been defined as follows:

> "Wilful misconduct" in an owner's risk note is thus summarized by Johnson J in "Graham v. Belfast and Northen Counties Ry [(1901) 2 I.R. 13]" "Wilful misconduct in such a special condition means misconduct to which the will is party as contradistinguished from accident, and is far beyond any negligence, even gross or culpable negligence, and involves that a person wilfully misconducts himself who knows and appreciates that it is wrong conduct on his part in the existing circumstances to do, or to fail or omit to do (as the case may be), a particular thing, and yet intentionally does or fails or omits to do it, or persists in the act, failure, or omission regardless of consequences....."

The word "gross negligence", as defined in "**Forder v. Great Western Railway Company**" (referred supra), is negligence which is far beyond any negligence or culpable negligence. In the present case the respondent, as the statutory Auditor, was under an obligation to ascertain actual receipt of cash for allotment of shares and, instead, he issued the certificate without qualifying that receipt of Rs.2,25,00,000/- was by way of cheques and was subject to realisation. The respondent stated that he had issued the certificate

[36] (1905) 2 KB 532

without any qualification based on the track record and reputation of the promoters, though he was well aware that the certificate, was the basis on which contribution of capital was invited from the public at large. Such callousness of the respondent, in issuing the certificate, would undoubtedly amount to gross negligence or culpable negligence since the respondent as an Auditor could not be unaware of the consequences of such a mis-statement in the certificate issued by him.

Sri Ashok Anand Kumar, Learned counsel for the respondent, would contend that the act of the respondent, at best, amounts to negligence, but not gross negligence. He would draw the attention of this court to **Institute of Chartered Financial Analysts of India v. Council of the Institute of Chartered Accountants of India**. (referred supra), wherein the Supreme Court examined the word "misconduct" in paragraph No.28 relying a judgment of Calcutta High Court rendered in "**Probodh Kumar Bhowmick v. University of Calcutta**[37]" as follows:

> "Misconduct, inter alia, envisages breach of discipline, although it would not be possible to lay down exhaustively as to what would constitute conduct and indiscipline, which, however, wide enough to include wrongful omission or commission whether done or omitted to be done intentionally or unintentionally. It means, 'improper behaviour; intentional wrong doing on deliberate violation of a rule of standard or behaviour."

In "**The Institute of Chartered Accountants of India v. V.K. Madhava Rao**[38]" an identical question came up for consideration, and a Division Bench of this Court held that a statement, in the respondent's letter, that he had examined the books of accounts,

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[37] (1994) 2 Cal L J 456
[38] AIR 1956 Hyd 205

was certainly a deliberate mis-statement which was admitted by him in paragraph No. 7 of his written statement. In those circumstances, the Division Bench agreed that the Accountant was grossly negligent as he did not have sufficient material to give such a certificate, and had failed to obtain sufficient information.

In the above judgment, the charge against the accountant was that he had blindly certified the sales of the Deccan Chronicle without checking the books of accounts knowing fully well that the certificate was required for boosting up advertisement insertions. When persons intend to insert advertisements in newspapers, one of considerations, which weigh with them, in selecting a newspaper, is to enquire what its circulation or sales is, and advertise in a paper which has a wide circulation. But, based on the statement of the accountant advertisements were invited, which was false on the face of the record. Therefore, the Chartered Accountant was found guilty of misconduct i.e. the gross negligence in issuing the certificate as he had failed to take the elementary precaution of checking the facts contained in the accounts. He was deemed guilty of gross negligence, because the duty he owed was to all those who were likely to act to their detriment upon the strength of that statement, and whom he should have had in contemplation at the time when he made the statement. The principles laid down in the above judgment, in fact, supports the contention urged on behalf of the Institute.

Sri Ashok Anand Kumar, learned counsel for the respondent, contends that failure to rise to the expected level of efficiency, in discharging professional duties, cannot be regarded as misconduct, treating such failure as gross negligence in the discharge of duty; at

best, it is merely a failure of the respondent to qualify the certificate; in the facts of the present case, failure of the respondent to verify actual receipt of cash for allotment of shares is merely a failure to rise to the expected level of efficiency in the discharge of his professional duties; it does not amount to gross negligence; and is merely a bonafide mistake or error. In support of his contention, he placed reliance on the judgment of the Calcutta High Court in "**Council of the Institute of Chartered Accountants of India v. Somnath Basu**[39]". In the said judgment, the Calcutta High Court held that failure to rise to the expected level of efficiency in discharging professional duties cannot be regarded as misconduct treating such failure as a negligent act in the conduct of professional duties. It is not the case of the Institute that the respondent failed to rise to the expected standards of his professional duties, but that he had issued the certificate on the basis of the track record and reputation of the promoters, though, the sum of Rs.2,25,00,000/- which he had certified to have been received was, in fact, not received by the date of certification dated 09.06.1995 i.e. one day prior to opening of public issue. Issue of such a certificate is not an innocent omission, or failure to rise to the professional standards required of a Chartered Accountant, but amounts to gross negligence on the part of the respondent in the discharge of his duties as the statutory auditor of the company.

It is also contended that to impose penalty or punishment against a professional for his misconduct, the act of such professional must be deliberate and intentional. While an intentional omission would certainly amount to gross negligence,

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[39] AIR 2007 Cal 29

even failure to discharge the statutory obligation or duty imposed on an Auditor by a statute i.e. issuing certificate, without verifying actual receipt of consideration, amounts to gross negligence since such omission is in utter disregard of the statutory duty imposed on the respondent, and is not a simple professional lapse on his part. As noted hereinabove, it is based on this certificate that the company invited subscription from the general public for Rs.4,50,00,000/-, even without the promoters contributing Rs.2,25,00,000/- as mentioned in the prospectus, and yet they were allotted shares worth Rs.2,25,00,000/- on payment of merely 35 lakhs to the company.

The judgment of the Madhya Pradesh, in "**Council of the Institute of Chartered Accountants of India v. C.H.Padliya"** is merely of persuasive value and does not constitute a precedent binding on this court. In **"Institute of Chartered Accountants of India v. S.K. Jain**[40]" the Division Bench of the Delhi High Court, while dealing with misconduct under Section 22 of the Act, held as follows:

> ""Professional misconduct" has been defined in Section 22 of the Act. Intendment and object of the Act is to maintain standard of the profession at a high level, and consequently a code of conduct has been prescribed. Misconduct implies failure to act honestly and reasonable either according to the ordinary and normal standard, or according to the standard of a particular profession. Authenticity and sanctity is attached to certification done by a Chartered Accountant. Hallmark of the profession is the expertise possessed by its members, in the matters of accountancy and auditing amongst others. Correctness is a matter of rule in a certificate issued by a Chartered Accountant. He is supposed to have tested correctness of the figures certified. If he puts his signature, without proper verification, in any certificate, it certainly is a serious matter. Such conduct does not befit a Chartered

[40] 2000 (56) DRJ 671

> Accountant, and is unbecoming of him. In such a case, he fails to do what is the minimum required to be done by him. He does something in the pursuit of his profession which is not only unethical, but also disgraceful or dishonourable."

In "**Council of Institute of Chartered Accountants of India v. B. Ram Goel**[41]" the Delhi High Court defined the expression 'professional misconduct' as follows:

> ""Professional misconduct" has been defined in Section 22 of the Act. Intendment and object of the Act is to maintain standard of the profession at a high level, and consequently a code of conduct has been prescribed. Misconduct implies failure to act honestly and reasonably either according to the ordinary and natural standard, or according to the standard of a particular profession. Chartered Accountants' profession occupies a place of pride amongst various professions of the world. That makes observance of the professional duties and propriety more imperative. When conduct of a member of the profession is contrary to honesty, or opposed to good morals, or is unethical, it is misconduct-warranting consequences indicated in the Statute. An Auditor holds a position of trust. That is why disclosure of information has been made a ground for imputing misconduct. By betrayal of the trust, the conduct becomes one which is unbecoming of the professional."

In the aforesaid judgment, the Delhi High Court relied on **Pandurang Dattatraya Khandekar v. The Bar Council of Maharashtra, Bombay**, and held that the misconduct alleged against the Chartered Accountant was established, and imposed on him the punishment of reprimand.

In "**State of Punjab v. Ram Singh Ex.Constable**[42]" the Supreme Court relied upon the definition of "misconduct" as defined in Black's Law Dictionary, 6th Edition at page 999 and P.

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[41] 2000 (57) DRJ 27
[42] (1992) 4 SCC 54

Ramanatha Aiyar's Law Lexicon, Reprint Edition 1987 at page No.821, which are as follows:

> "Misconduct has been defined in Black's Law Dictionary, Sixth Edition at page 999 thus:
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> A transgression of some established and definite rule of action, a forbidden act, a dereliction from duty, unlawful behaviour, wilful in character, improper or wrong behaviour, its synonyms are misdemeanour, misdeed, misbehaviour, delinquency, impropriety, mismanagement, offence, but not negligence or carelessness.
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> Misconduct in office has been defined as:
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> Any unlawful behaviour by a public officer in relation to the duties of his office, wilful in character. The term embraces acts which the office holder had no right to perform, acts performed improperly, and failure to act in the face of an affirmative duty to act.
>
> P. Ramanatha Aiyar's the Law Lexicon, Reprint Edition 1987 at p. 821 'misconduct' defines thus:
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> The term misconduct implies a wrongful intention, and not a mere error of judgment. Misconduct is not necessarily the same thing as conduct involving moral turpitude. The word misconduct is a relative term, and has to be construed with reference to the subject-matter and the context wherein the term occurs, having regard to the scope of the Act or statute which is being construed. Misconduct literally means wrong conduct or improper conduct. In usual parlance,. misconduct means a transgression of some established and definite rule of action, where no discretion if left, except what necessity may demand and carelessness, negligence and unskillfulness are transgressions of some established, but indefinite, rule of action, where some discretion is necessarily left to the actor. Misconduct is a violation of definite law; carelessness or abuse of discretion under an indefinite law. Misconduct is a forbidden act; carelessness, a forbidden quality of an act, and is necessarily indefinite. Misconduct in office may be defined as unlawful behaviour or neglect by a public officer, by which the rights of a party have been affected."

In the aforesaid decision, the Supreme Court held that the conduct of a constable possessing a service revolver, found to be heavily drunk while roaming in the market on duty, and to have abused the medical officer at the time of medical examination, would amount to conduct unbecoming of a constable, and that meant that he was unsuitable to discharge his duties as a police constable.

In **Deputy Secretary to the Government of India, Ministry of Finance (Department of Economic affairs), v. S.N.Das Gupta** (referred supra) the Supreme Court, after considering the duties of

an auditor, held that the duty of an auditor is to make a report to the share-holders, but doubted if the Act intended that a report may be a mere certificate to the effect that the Auditor was satisfied as to the particular matters specified in Section 145(2) of Companies Act, 1913. Such a certificate conveyed nothing to the share-holders beyond an assurance that, in the opinion of the Auditor, the books of the company were in order, and the position of the company was as stated in the balance-sheet. Such an assurance could hardly serve the purpose of giving adequate information to the share-holders as to the state of the company's affairs, because most of the items in a balance-sheet are generally of an omnibus character - large sums being shown under a general or composite heading. Unless the composition of those sums is explained by the Auditor's report, and where the sums are 'sums of loans or liabilities, and the nature of the investment or of the debt is not fully explained, it is difficult to see how the share-holders are enlightened. Be that as it may, as to the general duty of the Auditor in regard to his report, it has been said that his duty is to give information and not merely means of information. In other words, he must communicate facts so that, on those facts, the shareholders may judge the position for themselves and not merely throw out hints which might put the shareholders on enquiry and induce them to take steps for ascertaining what the facts were or which might be missed by the share-holders altogether. When the facts are such as to cause a doubt in the mind of the Auditor as to the accuracy of certain entries in the balance-sheet or they are such that, if disclosed, they would show the balance-sheet in a different light, those facts must be conveyed to the share-holders. They cannot be suppressed, nor

can doubt or dissent be expressed, but the reasons therefor withheld. In India, the Act deals with the last matter in Sub-section (2A) of Section 145 which says that where any of the matters referred to in Sub-section (2) is answered in the negative or with a qualification, the report shall state the reasons for such answer.

The Supreme Court also held that the Auditor holds a position of trust and it is his bounden duty to honour that trust by being candid with the shareholders, and telling them frankly and fully everything with regard to the affairs of the company which has come to his knowledge and which it is material for the shareholders to know;if an Auditor does not do what it is his duty to do, it is no defence for him to say in a disciplinary proceeding, started under the Chartered Accountants Act, that he had told the shareholders that he had not done it. ***The lapse is constituted by his failure to perform a duty without which an audit is meaningless and it is not excused by giving information of the omission to the share-holders.*** The reason is that the object of the Act is to ensure in public interest that those who practise the profession of Auditors shall perform, in their actual practice, at least the essential duties of an audit and shall bring to bear on their work attention to matters to which their duty requires them to pay attention, and the examination of accounts involves thorough and exhaustive testing of every account in the general ledger. If such negligence would cause no damage to anyone, such negligence cannot be termed as gross negligence within the definition of Section 22 of the Act.

The law declared in the above judgment cannot be applied to the present facts of the case since the respondent, in utter disregard of his professional duties, issued a certificate containing a false

statement regarding receipt of Rs.2,25,00,000/- towards contribution by the promoters for allotment of 15,00,000 shares, though he was well aware that the promoters had all issued cheques just one day prior to opening of public issue, all of which were later dishonoured on presentation.

The word 'neglect' is defined both as a noun and as a verb in terms of failure or omission to discharge or perform a duty; but one cannot be charged with failure to perform a duty unless he knows, or ought to know, that there is a duty incumbent on him to be performed. However, the word may import something more than a mere omission, something more than a failure without fault; it may import an omission accompanied by some kind of culpability in the conduct of the person, and it embraces wilful as well as unintentional disregard of duty.

'Neglect of duty' means failure to perform or discharge a duty and covers positive official misdoing or official misconduct as well as negligence as held in "**Baburao Vishwanatah Mathpati. v. State of Maharashtra**[43]".

The view expressed by the Court, in the above judgment, is that, in order to find the person guilty of neglect of duty, it must be culpable or wilful. Here the respondent is a statutory Auditor, on whom a duty or obligation is imposed to ensure that the certificate he issued, regarding receipt of promoters contribution, was based on a proper verification of the bank account of the promoters, and after ascertaining that there was sufficient balance in their bank account to ensure that the cheques would be honoured on presentation. The respondent failed to discharge his statutory

[43] AIR 1996 Bom 227

obligation or duty knowing the ill-consequences that flow from such failure, would certainly amounts to gross negligence.

In paragraph No.50 of the same judgment, the Division Bench of the High Court adverted to the meaning of 'gross negligence' to make a professional liable for misconduct. ***To fall within the ambit of misconduct under Section 22 of the Act, such negligence must be wilful, intentional, culpable or in flagrant disregard of duties***. Even if the definition in paragraph No.50 of the judgment is applied here, the respondent has acted in flagrant disregard of his duties as he has, without verifying the actual receipt of cash for allotment of shares to the promoters worth Rs.2,25,00,000/-, issued the certificate confirming receipt of such amount. Such an act of the respondent would amount to gross negligence as held by the Division Bench of the Calcutta High Court (referred supra).

Sri Ashok Anand Kumar, learned counsel for the respondent, has drawn our attention to "**The Council of Institute of Chartered Accountants of India v. Shrui K.Venkatacharyulu**" (unreported judgment of this Court in C.A. Referred Case No.123 of 2000 dated 03.09.2014) wherein the Division Bench of this Court held that misconduct can be attributed to a Chartered Accountant mostly when he has resorted to certain acts knowing fully well that the same is contrary to law. An opinion formed by him, which ultimately turns out to be not correct, cannot be treated as an act of misconduct. The law laid down by the Division Bench of this Court is that, in order to find a person guilty of professional misconduct, he must resort to certain acts knowing fully well that the same is contrary to law.

As discussed in the earlier paragraphs, the respondent issued the certificate without ascertaining whether the cheques would be honoured on presentation, or with the qualification that payment was by cheques and was subject to realisation. Issue of the certificate by the respondent amounts to gross negligence in the discharge of his profession duties as a statutory auditor, and he is liable for punishment under Section 21 (5) read with clause (7) of part I of Schedule II.

Refuting the contentions of the learned counsel for the respondent, Sri C.V. Rajeeva Reddy, learned counsel for the Institute, has placed reliance on four judgments viz., "**Deputy Secretary to the Government of India, Ministry of Finance (Department of Economic affairs), v. S.N.Das Gupta**[44]", "**Council of the Institute of Chartered Accountants of India v. V.I.Oommen and others**[45]", "**Council of the Institute of Chartered Accountants of India v. Shri Gyan Prakash Agarwal**", (unreported judgment of Delhi High Court in C.A. Reference No.1/2014 and CM No.3363/2014 dated 30.04.2015) and "**Chartered Accountants of India, Indraprastha Marg, New Delhi v. Shri S.Giridharan, Chartered Accountant**", (unreported judgment of High Court of Karnataka in Civil Petition No.191 of 2012) to contend that the respondent's failure to take reasonable care, and his failure to discharge his professional duties, amounts to gross negligence and he is liable for punishment on being found guilty of misconduct as defined under Section 22 of the Act. The consistent view expressed by various courts in the above judgments

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[44] AIR 1956 Calcutta 414
[45] AIR 1996 AP 254

is that failure to take reasonable care in discharging his professional duties amounts to misconduct.

The definition of Professional Misconduct, contained in Corpus Juris Secumdum at page No.740 (Vol.7), is as follows:

> "Professional misconduct may consist in betraying the confidence of a client, in attempting by any means to practise a fraud or impose on or deceive the court or the adverse party or his counsel, and in fact in any conduct which tends to bring reproach on the legal profession or to alienate the favourable opinion which the public should entertain concerning it."

Relying on the definition of "professional misconduct" as defined by Darling J., in "**A Solicitor ex p the Law Society, In re**[46]", the Supreme Court, in "**R.D.Saxena v. Balram Prasad Sharma**[47]", opined that an advocate must conduct himself at all times in a manner befitting his status as a member of a high and honourable profession. If he departs from such a standard, even in the context of recovering his fees, and behaves in a manner which is not fair, reasonable and according to law, he would be liable to disciplinary action. Exploitation of poor litigants is nothing but a common man loosing faith in the institute of judiciary.

Similarly, in "**Noratanmal Chouraria v. M.R.Murli**[48]", the Supreme Court considered the scope of professional misconduct, and concluded that improper behaviour, intentional wrongdoing or deliberate violation of a rule or standard of behaviour is nothing but transgression of a definite rule of action, which amounts to misconduct of a professional advocate.

In "**Baldev Singh Gandhi v. State of Punjab**[49]" the Apex Court examined the scope of misconduct and held that

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[46] (1912) 1 KB 302
[47] (2000) 7 Supreme Court Cases 264
[48] (2004) 5 Supreme Court Cases 689
[49] (2002) 3 Supreme Court Cases 667

"misconduct" has not been defined in the Act. The word "misconduct" is the antithesis of the word "conduct". Thus, ordinarily, the expression "misconduct" means wrong or improper conduct, unlawful behaviour, misfeasance, wrong conduct and misdemeanour etc. There being different meanings of the definition of misconduct, the Court should consider the expression "misconduct" with reference to the subject and the context wherein the said expression occurs. Thus, from the principles laid down in the above judgment, misconduct has to be considered in the facts and circumstances of the case, and is not a principle of universal application.

Coming back to the facts of the present case, it is evident that the allotment of shares of Rs.2.25 crores to the promoters was fraudulent, and without receipt of contribution from them and, on the basis of the cheques issued by the promoters just one day prior to opening of the public issue, the certificate was issued. The Statutory Auditor was obligated to ascertain whether the company had received the consideration of Rs.2.25 crores before certifying to the fact. As noted hereinabove, the promoters of the company resorted to jugglery of the figures in the books of accounts, transferring money from one person to another, or routing the money through M/s Pratha investment which was manned by the respondent, and belonged to his wife. The respondent has, in fact, assisted the promoters in playing fraud on the general public, in making them believe that the promoters had invested Rs.2.25 crores in the share capital of the company as promoters contribution, and thereby inducing the general public to subscribe to the share capital of the company for Rs.4.50 crores. It also appears that the

respondent was hand-in-glove with the promoters of the company, and the certificate was issued by him to induce the general public to subscribe to the public issue for allotment of shares. The respondent violated his obligations and duties as the statutory auditor of the company in issuing the certificate, and in aiding this corporate fraud. If such conduct is accepted merely as a professional lapse, it would certainly result in complete erosion in the high professional standards expected of Chartered Accountant members of the Institute, besides letting recalcitrant professionals go scot free. Unless Chartered Accountants, like the respondent, are sternly dealt with, under the provisions of the Act, it would also result in loss of public faith in the integrity, character and competence of the members of the Institute.

In view of the law declared by various courts referred to above, we shall now examine the specific acts or omissions attributed to the respondent which, we are satisfied, amounts to gross negligence on his part making him liable to be punished for misconduct under Section 22 of the Act. The specific omissions or commission attributed to the respondent are as follows:

(1) The respondent issued a certificate, being the statutory Auditor of Ritesh Polysters Limited, which formed the basis for issuing a notification inviting the general public to contribute to the share capital, without verifying actual receipt of cash of Rs.4.50 crores for allotment of 15,00,000 shares to the promoters worth Rs.2,25,00,000/-, and the cheques issued by the promoters bounced later.

(2) Respondent issued a certificate without qualifying that allotment of shares to the promoters was "subject to realisation of cheques."

(3) The respondent did not verify the individual bank accounts of the promoters to ascertain whether there was sufficient balance in their account to ensure that the cheques would be honoured, by the payee bank, on its presentation.

(4) Respondent failed to verify actual receipt of cash while allotting shares.

(5) Contribution of Rs.2,25,00,000/- as promoters contribution by Ritesh Exports was not examined, similarly routing of Rs.22,00,000/- through M/s Pratha Investments (owned by the wife of the respondent and being managed by the respondent himself) to the promoters Sri Deepak Agarwal and Sri Ritesh Agarwal, who allegedly contributed Rs.10,50,000/- each was also not examined. Thus, the said investment of Rs.22,00,000/- by Sri Deepak Agarwal and Sri Ritesh Agarwal was only a book entry without actual receipt of consideration. The company's money was divered and was brought back as contribution by the promoters.

We have adverted to the omissions or commissions of the respondent in the earlier paragraphs while discussing point No.6. The respondent has also, during investigation by SEBI and the enquiry by the Disciplinary Committee appointed by the Council, admitted issue of a certificate confirming receipt of promoters contribution to a tune of Rs.2,25,00,000/-, allotment of 15,00,000

shares without verifying actual receipt of cash for allotment of such shares to the promoters, and to have issued the certificate without qualifying that the allotment was subject to realisation of cheques.

On this corporate fraud coming to light, SEBI instituted proceedings against the directors of the company, and the matter went upto the Supreme Court in "**Ritesh Agarwal. v. Securities and Exchange Board of India.**[50]" The Supreme Court, while taking note of the corporate fraud played by the directors, exonerated Ritesh Agarwal and Deepak Agarwal on the ground that they were minors by the date of the public issue. Relying on "**BPL Limited v. Securities & Exchange Board of India"** and **"Videocon International Ltd. v. Securities & Exchange Board of India"** the Supreme Court held that, apart from the actions taken by the Board, the persons who undertook these fraudulent actions must also be held to be guilty of making a mis-representation, and commission of fraud not only before the prospective purchasers of the shares, but also before the statutory authority. The same, however, would itself not mean that a minor could be penalized for entering into a contract which per se was not enforceable. The Supreme Court permitted SEBI to take necessary action against Shri Surender Kumar Agarwal and Smt.Rooprekha Agarwal, while setting aside the order against Ritesh Agarwal and Deepak Agarwal who were minors by then. As the Supreme Court has directed that action be taken against certain promoters of the company for their active role in the corporate fraud, the Auditor, who certified and confirmed receipt of contribution from the promoters, cannot absolve himself of all blame and contend that the ambivalent

[50] (2008) 8 SCC 205

certificate issued by him was merely a professional lapse, and not gross-negligence on his part.

In the earlier paragraphs, we have elaborately discussed what amounts to gross negligence and professional misconduct with reference to the law declared by various Courts including the Supreme Court, Chancery Division etc., and have held that issue of the certificate, confirming receipt of Rs.2,25,00,000/- by the company towards promoters contribution just one day prior to opening of the public issue, without verifying actual receipt of consideration for such allotment of shares worth Rs.2,25,00,000/- (15,00,000 shares), is in violation of the respondent's professional duties as the Statutory Auditor of the company, and amounts to gross negligence and professional misconduct.

Sri Ashok Anand Kumar, Learned Counsel for the respondent, would contend that principles of natural justice were not followed, and sufficient opportunity was not afforded to the respondent. We must express our inability to agree as we have perused the records and are satisfied that reasonable opportunity was afforded to the respondent, at every stage, strictly adhering to the procedural provions of the Statute and the Regulations.

Sri Ashok Anand Kumar, Learned counsel for the respondent, would contend that the charges are vague, and do not afford any opportunity to the respondent to defend himself by filing an appropriate reply; and, on the strength of such vague charges, the respondent cannot be found guilty. He has placed reliance on a judgment of this Court in W.P.No.28 of 2003 dated 29.09.2010 wherein the Division Bench of this Court, while placing reliance on **M.V.Bijlani v. Union of India** (referred supra), held that, when an

appropriate charge is not framed or charges are vague, the employee cannot be found guilty of misconduct. This contention was neither urged before the Disciplinary Committee nor before the Council. On the other hand, the respondent appeared in person and defended himself. It is for the first time before this Court that this contention has been raised requesting this Court to exonerate him of the charges of misconduct. In any event, no prejudice has been caused to the delinquent thereby and, as held in "**UCO Bank and another v. M.Venuranganath**[51]" and "**C.Pattabhirama Sastry v. Bank of Baroda**[52]", no interference is called for where procedural violations, if any, have not caused any prejudice to the delinquent.

In "**Sarva Uttar Pradesh Gramin Bank v. Manoj Kumar Sinha**[53]" the Supreme Court observed that the respondent did not protest before the enquiry officer for not being permitted to cross-examine the witness, the enquiry proceedings were conducted in accordance with principles of natural justice, and the grievance was subsequently aired just to influence the proceedings in Court. In case the respondent felt genuinely aggrieved he would have raised the issue at the earliest possible stage.

In "**Om Prakash Mann v. Director of Education (Basic)**[54]", while deciding the case of misconduct of a Headmaster in a departmental enquiry, it was held that when the delinquent was called upon to submit a reply and no ground was taken by the delinquent that the charge sheet was vague or that he was unable to give an effective reply to the charges, and he had participated in the disciplinary proceedings without demur, he was estopped from later

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[51] 2002 (5) ALT 162 (D.B.)
[52] 1998 (4) ALT 803
[53] (2010) 3 Supreme Court Cases 556
[54] (2006) 7 Supreme Court Cases 558

raising such a plea of vagueness in the charges. The said judgment of the Supreme Court is a direct answer to the contention urged by the Learned Counsel for the respondent, and the respondent cannot claim that he should be exonerated on this ground.

Sri C.V. Rajeeva Reddy, learned counsel for the Institute, contended that an appropriate punishment, as recommended by the Council of the Institute, should be imposed and this Court, while exercising power under Section 21 (5) of the Act, should not take a lenient view against the statutory Auditor of the company who has indulged in a Corporate fraud to the detriment of the public at large. On the other hand, Sri Ashok Anand Kumar, Learned Counsel for the respondent, would submit that the incident took place in the year 1995, almost 21 years has since elapsed, and therefore a lenient view should be taken.

The professional misconduct attributed to the respondent is grave and serious in nature which affects public confidence, and their faith in the integrity and impartiality of the Chartered Accountants and the Institute of which they are members. A false certification by the respondent has enabled the promoters of the company to squander public money, on inducing the general public to subscribe to the share capital of the company. Taking a lenient view, or exonerating such professionals, would encourage others to indulge in similar acts, and completely erode the faith of the general public in the impartiality and integrity of the members of the Institute, and bring the Institute itself into disrepute.

The Council of the Institute has recommended removal of the name of the respondent from the Register of the Institute for a period of three (3) years i.e. suspending him from practicing as a

Chartered Accountant for a period of three (3) years. The recommendation of the Institute, regarding the nature of the punishment, is not binding on this Court and, in exercise of the wide powers conferred on it by the Act, this Court can impose a different punishment. In a similar situation, the Division Bench of this Court, in **Council of the Institute of Chartered Accountants of India v. V.I.Oommen** (referred supra), imposed a higher punishment than the one recommended by the Institute.

In the light of the above discussion, after anxious consideration of the matter, we find it appropriate that the respondent herein should be suspended from practising as a Chartered Accountant for a period of three years from 01.11.2016 to 31.10.2019.

Accordingly, the referred case is disposed of directing the respondent's membership with the Institute of Chartered Accountants of India shall stand suspended from 01.11.2016 to 31.10.2019, and, consequently, during that period he shall not practice or function as a Chartered Accountant. There shall be no order for costs.

Miscellaneous petitions, if any, pending shall stand closed.

RAMESH RANGANATHAN, ACJ

JUSTICE M.SATYANARAYANA MURTHY

26.09.2016.

Note:
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