



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department- I

Adjudication Division

ORDER	
Name of Company:	M/s. Ittefaq Iron Industries Limited
Number and Date of Show Cause Notice (SCN):	CSD/ARN/587/2019-336 dated June 21, 2024
Name(s) of Respondent(s):	(i) M/s. Sarwars Chartered Accountants; and (ii) Mr. Rashid Sarwar.
Date(s) of Hearing(s):	(i) September 09, 2024; (ii) September 19, 2024; (iii) September 26, 2024; (iv) November 27, 2024; and (v) December 09, 2024
Case represented by:	Mr. Rashid Sarwar, Partner (as the Authorized Representative.)
Provisions of law involved:	Section 249 of the Companies Act, 2017 read with Section 253 thereof.
Date of the Order:	May 22, 2025

This Order shall dispose of proceedings initiated through the Show Cause Notice No. CSD/ARN/587/2019-336 dated June 21, 2024 ("SCN") by the Securities and Exchange Commission of Pakistan (the "Commission") against M/s. Sarwars Chartered Accountants (the "Audit Firm") and Mr. Rashid Sarwar, Engagement Partner-M/s. Sarwars Chartered Accountants (the "Auditor/Engagement Partner") of M/s. Ittefaq Iron Industries Limited (the "Company"), hereinafter collectively referred to as the "Respondents", issued under Section 249 of the Companies Act, 2017 (the "Act") read with Section 253 thereof.

2. Brief facts of the matter are that the examination of the Annual Audited Financial Statements of the Company for the year ended June 30, 2022 (the "Accounts") revealed that the audit for the said accounts was carried by the Audit Firm and the Auditor, being the engagement partner, performed the audit activity of the Company. Furthermore, it was also revealed the Company had credited the prior year's tax refund accepted by the Tax Authorities amounting to Rs. 86,382,542 (note 38) in the 'taxation (expense)' and correspondingly debited the tax recoverable amount (note 29.1). This treatment, as a residual impact, resulted in overstating the tax recoverable amount in the previous year as well as the profit after tax for the Financial year (FY) 2022.

3. The Commission vide letter dated January 27, 2023 sought from the Audit Firm a year-wise computational difference of tax provisions for previous years as stated in the financial statements and as assessed by the tax department which, during the year 2022, had resulted in reversal of previous year's tax by Rs. 86,328,542. In response, the Audit Firm, instead of providing requisite computation, through letter dated February 28, 2023 informed that the Federal Board of Revenue ("FBR") had approved advanced income tax refund amounting to Rs. 86,328,542 vide order dated January 18, 2022 passed by Deputy Commissioner-Inland Revenue under Section 170(3) of the Income Tax Ordinance, 2001 (the "Ordinance") and also furnished the copy of the said order to substantiate its claim.

4. In order to further probe the matter, the Commission vide letter dated March 16, 2023 sought the rationale for adjustment of aforesaid refund in the profit and loss accounts (prior year tax) against taxation along with detailed background of the case. However, in response, the Auditor preferred not to furnish the requisite information.

5. Perusal of the assessment orders for the FY 2020 and 2021 furnished by Audit Firm and the Company vide letters dated February 28, 2023 and April 8, 2023 revealed that the tax department had acknowledged a tax refund for the tax years 2020 and 2021 to the extent of Rs. 86,328,542 as under:

Admitted advance income tax for the FY 2020	Rs. 63,846,240
Admitted advance Income tax for the FY 2021	Rs. 22,482,302
Total	<u>Rs. 86,328,542</u>

However, review of the Accounts transpired that the Company, instead of adjusting opening balance of income tax recoverable (note 29.1) equivalent to acknowledged tax refund of Rs. 86,328,542, had further increased the income tax recoverable balance by adjusting prior year tax with the said amount (note 38). The Company, therefore, *prima facie*, misstated the Accounts by booking incorrect tax adjustment therein; which resulted in overstatement of income tax recoverable amount (note 29.1) and profit after tax amount.

6. The Commission, considering the fact that the Company carried forward the impact of aforesaid material misstatement in the financial statement for the year ended June 30, 2023 ("FS2023"), again took up the matter with the Auditor vide letter dated March 11, 2024 and also shared the computation as tabulated below; highlighting the impact of said material misstatement:

<u>Computation of overstated amount of Income Tax Recoverable</u>			
Refund Acknowledged by FBR based on Tax years 2020 & 2021 assessment			86,328,542
<u>Add: Net Advance tax for FY 2022</u>			
Advance Income tax/deduction during the year	103,225,890		
Provision during the year	(151,479,367)		
Workers' Welfare Fund	(5,884,250)	(54,137,727)	
Income Tax recoverable as of June 30, 2022			32,190,815
<u>Add: Net Advance tax for FY 2023</u>			
Advance Income tax/deduction during the year	170,425,554		
Provision during the year	(103,555,670)	66,869,884	
Income Tax recoverable as of June 30, 2023			99,060,699
Income Tax recoverable as of June 30, 2023 as per financial Statements 2023			295,793,400
Overstated amount required to be adjusted against prior year tax			196,732,701

7. In response, the Audit Firm vide letter received on March 21, 2024 asserted that *Rs. 196.732 million in the FS2023 is verifiable and relates to the earlier years (Note 29.1) and is the advance tax paid for that year under Sections 153, 148, 147, 235 and 231 of the Ordinance. Furthermore, said advance tax remains unadjusted and paid advance/recoverable from the tax officer of the circle of assessment of the Company.*

8. It is however noted that the opening balance of income tax recoverable for FY 2022 i.e., Rs. 196,732,701, as claimed by the Auditor, is prior to adjusting Rs. 86,328,542 i.e. the refund approved

by the tax authorities. Accordingly, the Company should have adjusted the allowed refund of Rs. 86,328,542 against the prior years' tax expenses instead of further enhancing the balance of recoverable income tax by the said amount. The aforesaid error of accounting treatment by the Company in adjusting income tax recoverable amount resulted in overstatement of profit by Rs. 196.732 million and accordingly, the Company was required to rectify/adjust its Accounts by Rs. 196.732 million.

9. In view of the aforesaid, the Accounts and FS2023 of the Company, *prima-facie*, do not present a true and fair view on account of the following material misstatements:

- (i) Overstatement of Profit after tax (for the FY 2022 only) by Rs. 196.732 million and accordingly Earning Per Share (EPS) by Rs. 1.36.
- (ii) Overstatement of Income Tax recoverable balance by Rs. 196.732 million.
- (iii) Overstatement of Un-appropriated Profit balance by Rs. 196.732 million.

The aforesaid misstatements are, *prima-facie*, contrary to the requirements prescribed in paragraph 15 of International Accounting Standard – 1, 'Presentation of Financial Statements' (IAS-1), which are reproduced for the purposes of reference, as under:

Para 15 of IAS-1:

"Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework. The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation."

10. Furthermore, International Standards on Auditing ("ISA") 705 requires that the auditor shall express an adverse opinion if the nature of the matter giving rise to the modification relates to whether the financial statements are materially misstated, or there is an inability to obtain sufficient appropriate audit evidence. Paragraphs 6 and 22 of ISA 705 are reproduced as under:

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

- (a) The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or*
- (b) The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.*

22. If there is a material misstatement of the financial statements that relates to qualitative disclosures, the auditor shall include in the Basis for Opinion section an explanation of how the disclosures are misstated."

11. It was transpired from the foregoing that the Respondents, *prima-facie*, failed to discharge their duty by not bringing out the aforesaid material facts in their Audit Report in respect of the Accounts and FS2023, contrary to the requirements of Sections 249(3) and 249(4) read with Section 253 of the Act.

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12. Relevant provisions of Sections 249 and 253 of the Act are reproduced for ease of reference as under:

“249.— Duties of auditors.—(3) *The auditor shall make out a report to the members of the company on the accounts and books of accounts of the company and on every financial statements and on every other document forming part of such statements including notes, statements or schedules appended thereto, which are to be laid before the company in general meeting and the report shall state—*

- a). *whether or not they have obtained all the information and explanations which to the best of their knowledge and belief were necessary for the purposes of the audit and if not, the details thereof and the effect of such information on the financial statements;*
- b). *whether or not in their opinion proper books of accounts as required by this Act have been kept by the company;*
- c). *whether or not in their opinion the statement of financial position and profit and loss account and other comprehensive income or the income and expenditure account and the cash flows have been drawn up in conformity with the requirements of accounting and reporting standards as notified under this Act and are in agreement with the books of accounts and returns;*
- d). *whether or not in their opinion and to the best of their information and according to the explanations given to them, the said accounts give the information required by this Act in the manner so required and give a true and fair view—*
 - i). *In the case of the statement of financial position, of the state of affairs of the company as at the end of the financial year;*
 - ii). *in the case of the profit and loss account and other comprehensive income or the income and expenditure account, of the profit or loss and other comprehensive income or surplus or deficit, as the case may be, for its financial year; and*
 - iii). *in the case of statement of cash flows, of the generation and utilisation of the cash and cash equivalents of the company for its financial year;*
- e). *.....*

(4) Where any of the matters referred to in sub-section (2) or (3) is answered in the negative or with a qualification, the report shall state the reason for such answer along with the factual position to the best of the auditor's information. (emphasis added).

253.— Penalty for non-compliance with provisions by auditors.—(1) *If any auditor's report or review report is made, or any document of the company is signed or authenticated otherwise than in conformity with the requirements of section 131, sections 249 and 251 or is otherwise untrue or fails to bring out material facts about the affairs of the company or the matters to which it purports to relate, the auditor concerned and the person, if any, other than the auditor who signs the report or signs or authenticates the document, and in the case of a firm all partners of the firm, shall be liable to a penalty of level 2 on standard scale.”*

13. Accordingly, cognizance in the matter was taken by issuing SCN to the Respondents requiring them to show the cause in writing as to why a penal action as prescribed under Section 253 of the Act may not be taken against them for non-compliance of the requirements of Section 249 of the Act. In response to SCN, the Audit Firm vide letter dated July 23, 2024, *inter alia*, stated that:

"In this respect it may be noted that the advance tax claimed includes verified and unverified amounts of refunds. To bring the facts to your knowledge the claim of the Taxpayer in 2020 was Rs. 140,127,688/- after deduction provisions of Rs. 33,942,084/- and in T.Y 2021 was Rs. 196,732,701/-, out of these refunds the FBR acknowledge refunds amounting to Rs. 63,846,240/- and Rs. 22,482,302/- relating to T.Y 2020 and 2021 respectively. The FBR acknowledge the total amount of Rs. 86,328,542/- out of 196,732,701/- for issuance/ adjustment of advance tax liability to apply for exemption certificate for further deductions.

After above calculation for the above year Rs. 110,404,159/- would still remain unverified and available for future adjustments or deductions. The Taxpayer can claim this tax as many times to the satisfaction of Taxpayer. Your honour cannot enforce the Taxpayer to write off this advance tax. The Taxpayer has correctly declared.

Furthermore, with adjustment of Rs. 86,328,542/- the effects on the financial statements would as below

As mentioned in audited accounts Note 29.1

	2023 (Rs.)	2022(Rs.)
At beginning of the year	228,923,516	196,732,701
Add: Advance income tax/deductions during the year	170,425,554	103,225,890
	399,349,070	299,958,591
Less: Provision for taxation		
- Current year	103,555,670	151,479,367
-Prior periods	-	86,328,542
	-103,555,670	-65,150,825
Less: Workers' welfare fund	-	5,884,250
At end of the year (Refunds outstanding)	295,793,400	228,923,516

If adjustment of the said refunds amounting to Rs. 86,328,542/- would not have been taken, the effects would be as under;

Income tax recoverable (Refunds)

At beginning of the year	142,594,974	196,732,701
Add: Advance income tax/deductions during the year	170,425,554	103,225,890
	313,020,528	299,958,591
Less: Provision for taxation		
- Current year	103,555,670	151,479,367
	-103,555,670	148,479,224
Less: Workers' welfare fund	-	5,884,250
At end of the year (Refunds outstanding)	209,464,858	142,594,974

The tax office has the authority to apply Section 170(3) of the Ordinance and cannot force taxpayer to declare the same.

Your good-self has calculated the amount at Rs. 196,732,701/- and consider it to be materially misstated and having adverse effects on the financial statement that the amount pertains to opening advance tax for the year ended June 30, 2022. The effect of the said adjustment should be Rs. 86,328,742/- in the financial statements for the year ended June

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30, 2022, and also has same impact on opening balance for the year ended June 30, 2023. The transaction was approved by the management and it is also below the materiality level calculated by the Audit firm. Furthermore, to select the materiality parameters are subjective matters and truly depends on auditor's judgment with respect to audit risks, control risk and past history of client.

Your good-self also ignored the relevant provisions of IAS 37 (Provisions, Contingent Liabilities and Contingent Assets and ISA 705 and misinterpreted the implications of the said adjustment on the audit report and audit opinion widely ignoring the materiality levels and pervasive effect of the said adjustment on the financial statements. However, the same adjustment was made part of the summary of uncorrected misstatements duly signed by the client. It is submitted that advance adjustments have correctly declared, the effect of adjustments thus stands explained as above."

14. In order to provide opportunity of personal representation to the Respondents, hearings in the matter were fixed for September 09, 2024 and September 19, 2024 where the Respondents did not prefer to attend. Later, another hearing in the matter was fixed for September 26, 2024; when the Auditor himself as Respondent No. (ii) and on behalf of the Audit Firm-Respondent No. (i), as its Authorized Representative (the **"Authorized Representative"**) appeared. During the course of hearing, the Authorized Representative reiterated the written response to SCN submitted vide letter dated July 23, 2024 and stated that the material misstatement was below the threshold of material assessment; therefore, a qualified report was not issued and the Board of Directors (BOD) of the Company was duly informed about the same. Moreover, the said misstatement will be revised in financial statements for the year 2024 ("FS2024").

15. Subsequent to the hearing, the Audit Firm vide letter dated October 17, 2024 submitted the published page of FS2024 of the Company relating to restatement of income tax refunds and a summary of uncorrected misstatements for the period ended June 30, 2022, duly signed by the management on the letter head of the Company, which was claimed to be duly communicated by the Auditor to the BOD.

16. In order to conclude the matter, the Respondents were provided with another opportunity and hearing in the matter was fixed for November 27, 2024 which was not attended by the Respondents. Later, in order to meet the ends of justice, another hearing in the matter was fixed for December 09, 2024 with a clear advice that no further requests for adjournments of hearing opportunities will be allowed and in the case of non-appearance the order shall be passed on the basis of record available with this office. Despite the same, the Respondents failed to appear.

17. I have gone through the relevant provisions of Section 249 of the Act, considered the facts of the case, the record available with the Commission along with the written and verbal submissions of the Respondents. I have also perused Section 253 of the Act which stipulates penal action for contravention of the aforesaid provision of law. The relevant paras of IAS 1 and ISA 705 have also been perused to establish a clear canvas of Auditor's responsibilities in the instant matter. It is observed that the auditors being the frontline watchdog are required to give a report on the financial statements and books of accounts of the company after conducting the audit in accordance with the prescribed procedures and requirements of the Act, the accounting as well as the auditing standards. The shareholders are the ultimate stakeholders to whom the auditors are responsible to express their opinion by reporting if the financial statements are drawn up in conformity with the accounting and

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reporting standards and are in agreement with the books of account, and they must keep this fact in mind while auditing the books of accounts and reporting thereon. The duties and responsibilities of an auditor under Section 249 of the Act, appointed by the shareholders can best be understood if role of an auditor is looked at in the overall scheme of the company law where the audited financial statements sit at the heart of overall reporting to stakeholders. It is pertinent to observe that in the case of a listed company, the general public also contributes towards the equity of the company. Such persons do not have any direct control over the affairs of the company and access to the books of accounts and have no other option except to place their trust upon the auditor. Hence it is utmost to exercise due diligence in performing their duties and discharging their responsibilities. Any lapse in exercising due care and diligence, may injure such trust and confidence of the shareholders and other stakeholders of the Company.

18. It is further observed that computation of the advance tax for Tax Years 2020 and 2021 when analyzed revealed that the Company in FY 2020 claimed advance tax of Rs. 136.55 million out of which Rs. 19.15 million was unverified/rejected by the tax authority. This resulted in a balance of admitted advance tax amounting to Rs. 117.39 million. Similarly, the Company in FY 2021 claimed advance tax of Rs. 143.08 million out of which Rs. 15.19 million was unverified/rejected by the tax authority; resulted in a balance of admitted advance tax amounting to Rs. 127.88 million. Accordingly, the total balance of admitted advance tax for both years was Rs. 245.28 million as against the advance tax of Rs. 279.63 million. In addition to the above, the Company had prior year adjustments for short provisioning amounting to Rs. 37.73 million (Rs. 18.80 million for FY 2020 and Rs. 18.93 million for FY 2021). Moreover, as per the financial statements for FY 2020 and 2021, the Company recorded advance tax of Rs. 274.06 million, which exceeded the admitted advance tax by Rs. 28.78 million; thus, representing the excess advance tax recorded in the books.

19. Furthermore, it was observed that prior year tax adjustment of Rs. 66.51 million (sum of excess advance tax recorded in FS and the prior years short provisioning i.e., Rs 28.783 + 37.73 million) was not reflected in the Accounts and whereas the actual credit adjustment of Rs. 86.328 million, as approved by the FBR, relating to FY 2020 and 2021 was erroneously booked in the Accounts; resulting in an overstatement of profit by Rs. 152.84 million in FY 2022 (Rs. 66.51+86.328 million). Additionally, for computing actual overstatement of profit, the opening balance of advance tax of Rs. 43.09 million from 2020 and a prior year adjustment of Rs. 0.80 million made during FY 2022 had also been accounted for, leading to a total overstatement of profit of Rs. 196.732 million in the Accounts, which required appropriate adjustment for accurate financial reporting and compliance. The said computation tabulated below for reference;

Computation of Excess advance Tax being recorded in the Books									
Tax year	Advance tax claimed	Unverified / rejected	Admitted Advance Tax	Prov. As per FS	Tax Assessed	Adjustment 2016/ refund rejected	Prior year adj. for short prov.	Advance Tax as per FS	Excess advance tax recorded in FS
	(a)	(b)	c=(a-b)	(d)	e	(f)	(g)=[(e+f)-d]	(h)	i=(h-c)
2020	136,547,616	19,154,507	117,393,109	34,744,194	50,776,869	2,770,000	18,802,675	130,982,205	13,589,096
2021	143,078,706	15,193,905	127,884,801	86,473,693	101,155,116	4,247,383	18,928,806	143,078,706	15,193,905
Sub-total	279,626,322	34,348,412	245,277,910	121,217,887	151,931,985	7,017,383	37,731,481	274,060,911	28,783,001

Adjustment of prior year tax that should have been recorded in Accounts-2022 (g+i)	66,514,482
Actual credit adjustment made against prior year in the Accounts 2022	86,328,542
Profit for FY 2022 is overstated by	152,843,024
Opening balance-Tax Recoverable of 2020	43,087,567
Add: Prior year adjustment made during 2020	802,110
	196,732,701

20. In the instant matter, the Respondents failed to disclose the nature and impact of a material misstatement in their audit report on the Accounts. As the Company, in its Accounts, instead of adjusting the opening balance of income tax recoverable by the amount of tax refund of Rs. 86,328,542, erroneously recognized the same as current year income by crediting it to the profit and loss account under the head 'taxation' and concurrently, debited the same amount to the income tax recoverable balance. This accounting treatment was fundamentally incorrect and resulted in the double recognition of the same tax refund: *(i) first, as part of the opening balance of income tax recoverable, and (ii) second, as income during the year.* As a consequence, the Company materially overstated its profit after tax and income tax recoverable balance by Rs. 196.732 million in FY 2022 as computed above. The misstatement was also carried forward to the FS2023. However, the Auditor did not include/highlight any qualification, emphasis of matter or adverse opinion in the audit report.

21. Additionally, the Respondents' justification regarding the materiality of the matter does not hold ground, as the amount was significant to influence the economic decisions of financial statement users, especially where it had a direct impact upon the EPS. Under International Standards on Auditing ("ISA") 320, 'Materiality in Planning and Performing an Audit', materiality is determined not only by numerical/quantum thresholds but also by the nature and context of the misstatement. Thus, failure to disclose the aforementioned material misstatements undermined the reliability of the financial statements.

22. It is also pertinent to observe that the Company has subsequently rectified the misstatement by restating the financial position of FY 2022 in FS2024 which reinforces the fact that the Accounts and FS2023 were not free from material misstatement. The restatement of financial statements is an evidence that the Accounts and FS2023 were not in compliance with the requirements of the law for which, in separate Adjudication proceedings, a penal action has been taken against the Company and its BOD on account of aforesaid material misstatement.

23. Furthermore, it is relevant to observe that the Respondents have not provided any evidence to establish the claim that the misstatement was duly communicated by them and the same was acknowledged and approved in the BOD meeting. No minutes of the BOD meeting and/or cover page have been submitted to substantiate their claim that the matter of misstatement was brought to the attention of the Company's BOD. It is also observed that the Respondents in terms of ISA 705 should have appropriately reported the overstatements in the Audit Report as the impact of the same had caused material misstatement of the financial position of the Company.


24. A wholistic guidance in the instant matter can be sought from a judgment passed by the Appellate Bench Registry ("ABR") of the Commission in the matter of *Ilyas Saeed & Co. Chartered Accountants vs. Director/HoD Adjudication-I* (Appeal No. 122 of 2021), where it was held that *"the statutory auditors have a fiduciary duty towards the stakeholders of a company and that an audit report also helps the regulator to carry out its oversight of the affairs of a company....The Bench has*

observed that Appellant has failed to discharge their duty with regard to accurately reflecting books and records of the Company in the auditor's report, therefore not carrying out their professional duties in a diligent, transparent and professional manner. It was stated that the Bench expects statutory auditors to be more vigilant while carrying out the statutory audit of a company.... it is established that the Appellant has failed to comply with the requirements of duty of auditors.... and it is clear that the Appellant did not adopt an attitude of professional skepticism. ---"

25. In light of the aforesaid, the contravention with the requirements of Section 249 has been established beyond doubt which attracts penal action in terms of Section 253 of the Act. I have also given due attention to the grounds presented by the Authorized Representative to the said non-compliance, however, none of the ground justifies the non-adherence with the provisions of the Act. I, therefore, hereby, in terms of powers conferred under Section 253 of the Act read with S.R.O. 1545(I)/2019 dated December 06, 2019, impose a penalty of **Rs.50,000/- (Rupees Fifty Thousand only)** on Auditor i.e., Respondent No.(ii)-Mr. Rashid Sarwar, and Warn the Audit Firm, i.e., Respondent No.(i)- M/s. Sarwars Chartered Accountants, on account of established default.

26. The Respondents are also advised to remain vigilant in ensuring meticulously compliance with applicable legal and regulatory requirements in future.

27. Respondent No. (ii), is, hereby, directed to deposit the aforesaid amount of penalty in the designated bank account maintained in the name of the Commission with MCB Bank Limited or United Bank Limited within thirty (30) days from the date of this Order and to furnish a receipted bank challan to the Commission forthwith. In case of failure to deposit the penalty, the proceedings under Section 485 of the Act will be initiated for recovery of the penalty/fines as arrears of land revenue pursuant to provision of Section 42B of the Securities and Exchange Commission of Pakistan Act, 1997.


1- 22-05-2025

(Sohail Qadri)
Director/ HOD
Adjudication Department-I

Announced:
Dated: May 22, 2025
Islamabad.

