

# **Code of Ethics**

**Practical case studies & Important  
clauses of First & Second Schedules to  
CA Act, 1949**

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# Code of Ethics

## Why ?

Essential for commanding the respect and confidence of the regulators and public at large.

Conduct of Members is regulated under the Chartered Accountants Act, 1949 and the regulations framed thereunder.

# Code of Ethics

## What is the Code?

Essentially a set of professional ethical principles & standards, regulating the relationship of CAs with clients, employers, employees, fellow members of the group and the general public.

# Code of Ethics

- ICAI published the Code of Ethics for the first time in 1963, comprising of ethical principles and commentary on the clauses of First and Second schedules to the CA Act, 1949 .
- The Code has been revised 12 times so far and the latest i.e. 12<sup>th</sup> Edition has been released in 2019-20.

# Code of Ethics - Domestic Laws

- Compliance with Accounting & Auditing Standards, Guidance notes and other documents issued by ICAI
- Compliance with applicable laws (to the auditee) viz., Companies Act, I.T Act, B.R Act etc.

# **MISCONDUCT under CA Act**

## **(Chapter V)**

Omissions & Commissions and  
Unethical practices.

## **Professional or other misconduct defined (Sec.22)**

The expression “Professional or other misconduct” shall be deemed to include any act or omission provided in any of the schedules, but nothing in this section shall be construed to limit or abridge in any way the power conferred on the Director (Discipline) U/s.21(1) to inquire into the conduct of any member of the ICAI under any other circumstances.



## **Commonly observed Reasons / causes for filing complaint against members**

- Omissions and commissions noted in the Audit reports / certificates.
- Material mistakes / incorrect information in measurement, presentation / disclosure of Financial statements.
- Non-compliance with Accounting Standards / Auditing Standards.
- Non-compliance with other applicable laws – Eg: Banking Regulation Act, Co-operative Societies Act, MSMED Act.

# **Commonly observed Reasons / causes for filing complaint against members**

- FRRB findings.
- Complaints by Regulators like I.T Department, ROC, SEBI, Banks, RBI, SFIO, CBI, ED, GST Department, Co-operative Audit Department etc.
- Disputes among partners / Directors of the auditee.
- Disputes among the partners of professional firms.
- Other misconduct alleged by aggrieved parties, bringing disrepute to the profession.

# **First Schedule to the CA Act, 1949**

## **PART - I**

**Professional misconduct in relation to CAs in practice:**

**A Chartered Accountant in practice shall be deemed to be guilty of professional misconduct, if he:-**

# First Schedule (Part-I)

**CI 2:** *Pays or allows or agrees to pay or allow, directly or indirectly, any share, commission or brokerage in the fees or profits of his professional business, to any person other than a member of the Institute or a partner or a retired partner or the legal representative of a deceased partner, or a member of any other professional body or with such other persons having such qualifications as may be prescribed, for the purpose of rendering such professional services from time to time in or outside India.*

# First Schedule (Part-I)

(Clause 2 contd.,)

- ❑ Members can share fee with such members of other bodies as may be approved by the council (like CSs, Cost Accountants, Lawyers, Architects etc.)
- ❑ % of fee payable to Registrar of co-operative societies in certain states – permitted
- ❑ A legal representative of a partner (say widow) is entitled for share of profit and Goodwill when the Partnership Deed permits.

# First Schedule (Part -I)

**Cl 5:** *Secures, either through the services of a person who is not an employee of such chartered accountant or who is not his partner or by means which are not open to a chartered accountant, any professional business;*

- Work will follow due to the respect that he commands
- acts of partners / employees of the firm in securing the prof. work shall be subject to provisions of Cl. 6 & 7 of Part – I of First schedule.

# First Schedule (Part -I)

**CI 8:** *Accepts a position as auditor previously held by another chartered accountant or a certified auditor who has been issued certificate under the Restricted Certificate Rules, 1932 without first communicating with him in writing;*

# First Schedule (Part - I)

## Clause 8 (Contd..)

- Communication required for all types of audits.
- Grounds for Non-acceptance of audit to be stated clearly
- non-compliance with Sec.139 / 140 of Companies Act, 2013 read with Cl.9 of Part I of 1<sup>st</sup> schedule to CA Act 1949
- Non payment of undisputed audit fee by auditee, other than a sick unit.
- Fees pending due to non availability of Previous Auditor
- Course of action in case of change of auditor
- Duty of retiring auditor – to respond with correct information.
- Incoming auditor can act, after waiting for a reasonable time for a reply
- Positive evidence of delivery required - (a) RPAD (b) Personal delivery (c) Ack. by mail from retiring auditor's official mail ID (d) UDIN portal.
- Certificate of posting not a conclusive proof of communication.
- Premises found locked – New Guidance available.



# First Schedule (Part - I)

## Clause 8 (contd.,)

- Firm not found at the Registered address – New Guidance available
- Special audit under I.T Act / other Acts – Healthy practice to communicate with statutory Auditor.
- Communication in case of assignments by other professionals – healthy practice
- Lack of time in acceptance of Govt. Audits / Bank Audits
  - To make it clear in the acceptance that it is subject to prof. objections, if any from the previous auditor.

# First Schedule (Part - I)

**Cl 9:** *Accepts an appointment as auditor of a company without first ascertaining from it whether the requirements of Section 225 of the Companies Act, 1956 (Sec.140 of 2013 Act), in respect of such appointment have been duly complied with;*

# First Schedule (Part - I)

## Clause 9 (contd.,)

- ❑ Procedural requirements to be diligently adhered to.
- ❑ To check whether Special notice was given at least 14 days before the general meeting.
- ❑ Notice to retiring auditor should be sent by RPAD.
- ❑ Replies received from the retiring auditor are sent to all the members of the company.

# First Schedule (Part - I)

## Clause 9 (contd.,)

- ❑ After satisfying that the requirements of the companies act have been complied with, the incoming auditor should first communicate with the retiring auditor as provided in clause 8 of Part I of First Schedule.
- ❑ Do not rely on the verbal assurance given by the company about the compliance of Companies Act requirements. Verify and collect the documentary evidence.

# First Schedule (Part - I)

**CI 11:** *Engages in any business or occupation other than the profession of chartered accountants unless permitted by the Council so to engage.*

# First Schedule (Part - I)

## Clause 11 (Contd..,)

### ■ **DIRECTOR/PROMOTER/ PROMOTER DIRECTOR**

- Permitted generally to be director simplicitor in any company.
- Permitted to be a promoter or signatory to the MOA & AOA of the Company.
- To be a director of the company irrespective of whether the objects include areas which do not fall within the scope of the profession of CA.

# First Schedule (Part - I)

## Clause 11 (Contd..,)

### ■ **PERMISSION GRANTED GENERALLY (By Council Resolution)**

- Employment under CA in practice/firm
- Private tutorships.
- Acting as surveyor/loss assessor under insurance act.
- Full/part time employment in business concerns provided one doesn't hold substantial interest.
- Full/part time employment in non- business concerns .
- Office of MD/Whole Time Director of body corporate, provided he/relatives doesn't hold substantial interest.
- Interest in family business concerns.

# First Schedule (Part - I)

## Clause 11 (Contd.,)

A CA in practice shall not engage in any other prof. / business except with the permission of council (Reg. 190A).

### Exceptions:

Permitted - Liquidator, Trustee, Executor, Administrator, Arbitrator, Receiver, Adviser or representative for costing etc., appointed by Govt. – provided the appointment is not on a salary cum full time basis.



# First Schedule (Part - I)

## Clause 11 (Contd..,)

### ❑ **Director – Simplicitor:**

- Means an ordinary Director (Not MD / WTD) required only to attend Board meetings and no remuneration except sitting fee
- No specific permission is required

### ❑ **Promoter Director:** No bar to be a promoter director and Simplicitor director.

### ❑ **Member in practice in a HUF doing business:**

- To prove that he was not actively engaged in the business of HUF
- Funds of HUF can be invested in business provided member is not actively engaged in the management of the said business.

# First Schedule

## Part IV

### Other Misconduct in relation to the Members of the Institute generally:

***A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he-***

*1: Is held guilty for any Civil or Criminal Court for an offence which is punishable with imprisonment for a term not exceeding six months.*

*2: In the opinion of the Council, brings disrepute to the profession or the institute as a result of his action whether or not related to his professional work.*

- Council is empowered to opine on any action of a member which brings the Institute or profession in disrepute as misconduct.

# Second Schedule

## Part I

### **Professional misconduct in relation to CAs in practice:**

*A chartered accountant in practice shall be deemed to be guilty of professional misconduct, if he –*

# Second Schedule (Part -I)

**CI 3:**      *Permits his name or the name of his firm to be used in connection with an estimate of earnings contingent upon future transactions in a manner which may lead to the belief that he vouches for the accuracy of the forecast;*

# Second Schedule (Part - I)

## Clause 3 (Contd..,)

- **Report on profit forecast and / or Financial forecast**
- Member should state the sources of information, basis of forecasts, major assumptions etc. but should not vouch for accuracy of the forecasts.
- Refer SAE 3400 – The Examination of prospective Financial Information (applicable for all reports issued on or after 1.4.2007)
- Refer to “Guidance Note on Reports in company prospectuses (Revised 2019)” issued in January 2019  
[Provides Guidance on compliance with Companies Act, 2013 and SEBI (issue of Capital & Disclosure Requirements) Regulations 2018]

## Second Schedule (Part - I)

**CI 4:** *expresses his opinion on financial statements of any business or enterprise in which he, his firm or a partner in his firm has a substantial interest;*

# Second Schedule (Part - I)

## Clause 4 (Contd..,)

### ■ **Substantial interest:**

- Shall have same meaning as is assigned thereto under Chartered Accountants Regulations, 1988
- 20% of voting power / shareholding
- Member, his firm or his partner or his relative has substantial interest
- "Financial Statements cover both reports and certificates usually given after examination of Accounts or Financial Statements
- Council decided not to permit:-
  - a CA employee to certify the Financial Statements of his employer company or a company under the same management, even though he holds COP.
  - accept the auditor-ship of a college, if he is working in the same college on part time basis.
  - accept the auditor-ship of a Trust, where his partner is a trustee or employee of the said Trust.

# Second Schedule (Part - I)

## Clause 4 (Contd.,)

- Requirements of this clause are applicable to all attest functions
- Where the member is a Director, officer or employee in a company
- Sec.141(3)(b) of Companies Act, 2013 prohibits from auditing such company irrespective of holding substantial interest.



## Second Schedule (Part - I)

### Clause 4 (Contd..,)

- a Director / simplicitor cannot be the auditor of that company
- Sec. 141(3)(d)(i) of Cos Act disqualifies a person if he, his relative or partner holds any security or interest in the company or its subsidiary / holding / associate company (relative can hold security up to Rs.1,000/-).
- Sec.141(3)(c) of Cos Act, 2013 disqualifies a member from being auditor if he is a partner or who is in the employment, of an officer or employee of the company.
- Sec.141(3)(f) of Cos Act, 2013 disqualifies a person whose relative is a Director or is in the employment of the company as a Director or KMP
- "Relative" for this purpose would refer to the definition mentioned in AS-18.

## Second Schedule (Part - I)

### Clause 4 (Contd..,)

- Not to write books of A/c for clients
- Statutory Auditor not to be the Internal Auditor
- Internal Auditor not to be the Tax Auditor under I.T Act / GST Act.
- 2 years cooling off period after completion of tenure as Director
- Members to satisfy whether appointment is as per the statute
- Regulatory requirements and requirements of Trust deed / Articles.

## Second Schedule (Part - I)

**CI 5:** *fails to disclose a material fact known to him which is not disclosed in a financial statement, but disclosure of which is necessary in making such financial statement where he is concerned with that financial statement in a professional capacity;*

# Second Schedule (Part - I)

## Clause 5 (Contd..,)

- For Materiality, refer to SA 320 – “Materiality”
- Misstatements including omissions are expected be material, if they individually or in aggregate expected to influence the economic decisions of users taken on the basis of Financial Statements.
- Judgments about materiality are to be made in the light of surrounding circumstances, size / nature of miss-statement
- Financial statements cover both reports & certificates.

## Second Schedule (Part -I)

**Cl 6:** *Fails to report a material misstatement known to him to appear in a financial statement with which he is concerned in professional capacity.*

Observations made in Clause – 5 are equally applicable to this clause.

# Second Schedule (Part -I)

*Cl 7: Does not exercise due diligence, or is grossly negligent in the conduct of his professional duties.*

- Though simply worded, very vital clause which usually gets attracted whenever it is necessary to judge whether a member has honestly and reasonably discharged his duties.
- Diligence encompasses the responsibility to act in accordance with the requirements of an assignment carefully and thoroughly.

# Second Schedule (Part - I)

## Clause 7 (Contd..,)

### ■ What constitutes professional misconduct?

Professional misconduct on the part of a technical professional cannot be found merely on a finding of bare nonperformance of a duty or some default in performing it.

- Misconduct implies failure to act honestly and reasonably either according to the ordinary and natural standard or according to a particular profession.
- Term of fairly wide import but generally speaking it implies fairly serious cases of misconduct of gross negligence.
- Negligence per se would not amount to gross negligence

# Second Schedule (Part - I)

## Clause 7 (Contd..,)

- **Gross negligence – some instances**
  - Failure to verify securities
  - Failure to reconcile bank balances
  - Failure to check cash balances
  - Issuing a false certificate regarding maintenance of records



# Second Schedule (Part - I)

**CI 8:** *fails to obtain sufficient information which is necessary for expression of an opinion or its exceptions are sufficiently material to negate the expression of an opinion;*

- A member should not express an opinion before obtaining the required data and information.
- If a member did not get full information for expression of an unmodified opinion, the auditor should clearly express his disclaimer. Refer to SA 705 – Modifications to the opinion in the Independent Auditor's Report (Revised)

# Second Schedule (Part - I)

***CI 9: Fails to invite attention to any material departure from the generally accepted procedure of audit applicable to the circumstances;***

- What is generally accepted Audit procedure:
  - Audit should be performed in accordance with generally accepted procedures of audit applicable to circumstances / entity
  - Depend upon facts and circumstances of each case.
- Guidance is available from ICAI by way of Engagement and Quality Control Standards (SAs), Statements, GNs, GCs, Tech. Guides, practice manuals, studies and other papers.

# Second Schedule (Part - I)

## Clause 9 (contd.,)

- Audit of listed companies:
  - To have Peer Review certificate
- Firm Registration Number and Membership Nos. to be quoted on all reports.
- UDIN to be quoted – w.e.f. 01.07.2019

# **Second Schedule**

## **Part -II**

CI 4. *Defalcates or embezzles moneys received in his professional capacity.*

# Second Schedule

## Part III

### **Other Misconduct in relation to the Members of the Institute generally:**

*1. A member of the Institute, whether in practice or not, shall be deemed to be guilty of other misconduct, if he is held guilty by any civil or criminal court for an offence which is punishable with imprisonment for a term exceeding six months.*

**THANK YOU**