

To,

5<sup>th</sup> March, 2016

**Shri H. S. Mahadeva Prasad,  
Minister for Co-Operation and Sugar,  
Government of Karnataka.**

### **MEMORANDUM**

The Karnataka State Chartered Accountants Association (R) (in short '**KSCAA**') is an association of Chartered Accountants, registered under the Karnataka Societies Registration Act in the year 1957. KSCAA is primarily formed for the welfare of Chartered Accountants and represents before various regulatory authorities to resolve the professional problems faced by chartered accountants.

We do hereby submit a Memorandum to rationalize appointment and audit process in Co-Operative Sector. This Memorandum is being submitted to your goodself in view of various phone calls and communications received from Chartered Accountants practicing in the State of Karnataka.

- We are an Association formed by the Karnataka State Chartered Accountants and known as "**Karnataka State Chartered Accountants Association**". Being an association we need to look into the grievances, hear difficulties faced by the Chartered Accountants in Karnataka. Chartered Accountants are trained in the line of Auditing and specialised mainly in the line of Audit and Taxation. About three year back, by making an amendment to the Karnataka Co-operative Societies Act, the Auditing of Co-operative Societies situated in Karnataka were permitted to be audited by **Chartered Accountants**. In recent development by making one more amendment to the Karnataka Co-operative Societies Act, the Co-operatives were also authorized to get the accounts audited by **Cost Accountants**, i.e. those who are qualified from the **Institute of Cost and Accountants of India**. These Cost Accountants are specialised in the area of Costing and not in Auditing.

- Allowing Non-Chartered Accountants for audit of Financial Statement which involve expression of opinion on true and fair view of financial position is detrimental to the main objective of audit of Financial Statements and adversely affect the quality of audit in Co-Operative sector. Further, it also causes injustice to our fraternity and for the reasons detailed in following paragraphs.
- Primarily, the Institute of Chartered Accountants of India is formed in 1949 by an Act of Parliament by The Chartered Accountants Act, 1949 with specific objective Audit of Financial Statement and expression of opinion on financial position of an organization. On the other hand, the Institute of Cost Accountants of India has been set in 1959 by The Cost and Works Accountants Act, 1959 for the promotion of Cost Accountancy which main involve certification of facts. **These two Institutes are formed with specified objectives, Chartered Accountants are exclusively dealing with financial audit and Cost Accountants are exclusively dealing with Cost Audits.**
- The requirements of the audit require the auditor to give a true and fair view on the accounts of the auditee which can be given only by persons having a high degree of training and competence in accounting. This level of knowledge in accounting is possessed only by chartered accountants acquired by virtue of their tough training and stringent qualifying requirements. The syllabus prescribed for the various examinations of the CA Institute is of a very high order and the same is constantly updated to be in tune with the times through the constitution of Review Committees. In fact, CA exams are one of the toughest exams of the world.
- The Central Government through 97<sup>th</sup> Constitutional Amendment has emphasized the audit of co-operative sector by Chartered Accountants due to their training and extent of knowledge in the field of audit of Financial Statements and capability in assessing the financial condition.
- The Cost Accountants are experts in the field of Cost Audit whereas the Chartered Accountants are specialised and experts in the field of Financial

Audits and at present all Financial Audits are required to be conducted only by Chartered Accountants.

- Considering the fact that the reporting under audit requires a thorough knowledge of the principles of accounting and auditing and the procedures thereof and also a thorough knowledge of the various applicable statutes, including income tax Act, with an independent professional who possesses an approach with integrity, impartiality and objectivity, all statutes have reposed the responsibility of conducting such audit exclusively on the chartered accountants.
- In many judicial pronouncements it is clearly held that the financial audit is exclusive domain of Chartered Accountants.

Even the Apex Court has put its seal of approval by upholding the constitutional validity of section 44AB in *T.D. Venkata Rao v Union of India* [1999] 237 ITR 315 (SC). The Apex Court has made the following significant observations:

*‘Chartered Accountants, by reason of their training have special aptitude in the matter of audits. It is reasonable that they, who form a class by themselves..... There is no material on record and indeed in our view, there cannot be that an income-tax practitioner has the same expertise as chartered accountants in the matter of accounts.’*

There are several High Court judgments as well, like **Sarma (A.S.) v. Union of India** [1989] 175 ITR 254 (AP); **Mohan Trading Company v. Union of India** [1985] 156 ITR 134 (MP); **Nataraj (T.S.) v. Union of India** [1985] 155 ITR 81(Kar.); **Sathya Moorthy (R.) v. Union of India** [1991] 189 ITR 491 (Mad.); **Rajkot Engineering Association v. Union of India** [1986] 162 ITR 28 (Guj.,) which have clarified that audit is the exclusive domain of Chartered Accountants.

The relevant extracts of the aforesaid judgments are as follows :-

### **1. Approval by Apex Court for Chartered Accountants as specialists in audit**

The highest Court has put its seal of approval by upholding the constitutional validity of section 44AB in *T.D. Venkata Rao v Union of India* [1999] 237 ITR 315 (SC). The Apex Court has made the following significant observations:

*“Chartered Accountants, by reason of their training have special aptitude in the matter of audits. It is reasonable that they, who form a class by themselves, should be required to audit the accounts of businesses whose income (sic: turnover) exceeds Rs. 40 lakhs and professionals whose income (sic: gross receipts) exceeds Rs.10 lakhs in any given year. There is no material on record and indeed in our view, there cannot be that an income-tax practitioner has the same expertise as chartered accountants in the matter of accounts. For the same reasons the challenge under article 19 must fail, and it must be pointed out that these income-tax practitioners are still entitled to be authorised representatives of assessees.’*

**2. High Courts recognize the audit expertise of Chartered Accountants (i) Sarma(A.S.) v. Union of India [1989] 175 ITR 254 (AP)**

*“Income-tax practitioners and auditors cannot be considered on par with chartered accountants regarding expertise and excellence in audit. It is contended that the income-tax practitioners, advocates and chartered accountants are considered and treated alike under section 288 and, therefore, there is no logic for this differentiation. Section 288 enumerates the diverse categories of persons entitled to attend on behalf of the assessee before the hierarchy of authorities under the Act and apart from other persons income-tax practitioners, advocates and chartered accountants are mentioned. A glance at the list of persons set out in sub-section (2) of section 288 reveals that the persons who are expected to make an effective and genuine representation and having an over-view knowledge of the affairs of the assessee are authorised to represent without reference to any specialised proficiency in taxation or otherwise. It is patent that all those categories are lined up on an equal footing under section 288 for the purpose of representation of the case of the assessee and this equal eye should be confined to the purpose of representation only and it cannot be expected of advocates and income-tax practitioners with their background of education and academic attainment to give a good account of themselves in audit. Equally, chartered accountants cannot be credited with legal education. Chartered accountants constitute a distinct group and income-tax practitioners and advocates cannot be equated with them in so far as audit is concerned and as such section 44AB is not violative of article 14 of the Constitution.”*

**3. Mohan Trading Company v. Union of India [1985] 156 ITR 134 (MP)**

*"The chartered accountant, who do the work of audit, perform the function of an "accountant" on account of the special qualification they have for this purpose and the legal practitioners obviously do not belong to that category. It is, therefore, not a case where the legal practitioners, who are qualified to perform the duty of an "accountant", have been restrained from doing so. As for representation of the assessee before the assessing authority, the legal practitioner as well as the "accountant" appear for the assessee, since both are included in the category of persons entitled to represent the assessee as an "authorised representative" in accordance with s. 288 of the Act. It is for the purpose of s. 288 of the Act that a legal practitioner and an "accountant" are equals and not for the purpose of compulsory audit of the assessee's account, for which the "accountant" alone is qualified. Admittedly, there is no discrimination made between a legal practitioner and an "accountant" for the purpose of appearance as an "authorised representative" of the assessee in accordance with s. 288 of the Act. If a person clubbed with others in s. 288 possesses some further qualification enabling him to perform a function in addition to appearance as an "authorised representative" of the assessee, no discrimination can result from the disability of others for want of qualification to perform the addition function outside the ambit of s. 288 of the Act. The mere possibility of an "accountant" being preferred to a legal practitioner for the purpose of representing the assessee before the assessing authority is no ground to hold that there is any discrimination between them as equals under s. 288 of the Act."*

**4. Nataraj T.S. vs. Union of India [1985] 155 ITR 81(Kar.)**

*"Under the Chartered Accountants Act and the Chartered Accountants Regulations of 1964 framed there under, a person, to be enrolled as a chartered accountant, must possess the special qualifications prescribed by the regulations which require him to undergo an arduous and intensive training and then pass the various tough examinations that qualify him for enrolment as a chartered accountant. In that process, one of the qualifications acquired will be the special skill or knowledge in the audit of accounts which is both a science and an art. Any and every one cannot claim the qualifications and status of a chartered accountant. We can with certainty hold that a CA has the necessary qualification, skill and expertise to audit the accounts required to be filed under the Act. While this is the position of chartered accountants, we cannot hazard to say the same so far as the ITPs are concerned. The class of ITPs cannot compare*

*themselves with the class of CAs. We are here concerned with the superior and special qualifications possessed and recognised by law and not with the individual and special attainments, if any, attained by an individual and not recognised by law. As pointed out by Cardozo J. in Stewart Dry Goods Co. v. Lewis (294 Us 550) quoted with approval by our Supreme Court in Kodar v. State of Kerala [1974] 34 STC 73, the “law builds on the probables only” and cannot possibly comprehend all conceivable situations at any rate in one measure, in any event at one time. What emerges from this discussion is that the ITPs who belong to a separate class cannot compare themselves with the class of chartered accountants that have special qualifications and expertise to do the job of audit more efficiently.”*

**5. Rajkot Engineering Association v. Union of India 11986j 162 ITR 28 (Guj.)**

*“It is, therefore, clear that unless a person has adequate academic and practical training, proficiency and expertise in relation to what is known as auditing, it would be difficult for him to perform his role and adopt measures so as to reach the well recognized standards in the profession. It is difficult for us to agree with the Learned Advocate General for the petitioners that the general role which is envisaged for the authorized representatives which a non-chartered accountant can assume and perform would be sufficient for reaching and maintaining the standards required for an auditor and more so for a tax auditor. The norms and distinctions which a person has to satisfy and achieve in the course of the academic and practical training for being qualified as a chartered accountant go a long way in conferment of proficiency and expertise which a lay person cannot achieve by merely having practical knowledge of the principles of accountancy.*

*“It, therefore, cannot be said that Parliament has, by selecting chartered accountant from amongst various representatives to act as tax auditors, given a preferential treatment to them vis-a-vis the other non-chartered accountants’ segment of authorized representatives. These two classes cannot be said to be similarly situate so as to make the classification and intelligible or for that matter as suspect classification without having reasonable nexus with the object of the Act.”*

**In sum and substance, all the above judgements emphasize only one point. If the activity is an AUDIT(whatever may be the nature of audit – Company Audit, Tax**

Audit or Cooperative Audit) then it is the exclusive domain of CHARTERED ACCOUNTANTS only.

Audit is not just filling up a questionnaire. Because of the rigorous training which involves an exclusive and exhaustive study of all the accounting and auditing standards, thoroughness in the knowledge of audit and unparalleled expertise, CA's possess the required skill set and expertise to form an independent opinion on the credibility of the books of accounts and other documents subjected to audit; only CA's can perform and deliver an effective audit. CA's are also trained to decipher the various management and employee frauds which others do not have an iota of experience. Thus, General public has placed total reliance on the report of the Chartered Accountants and no one else.

Neither a Cost Accountant nor any other person possess the required attributes mentioned above and therefore can never perform an effective audit. If at all such persons are allowed to audit then the quality of the audit would naturally suffer thereby the purpose of audit itself would get defeated. The resultant consequence would be catastrophic having the potency to impair the financial position of the auditee societies and the trust fabric is going to be damaged beyond repair.

Hence, considering all the above points we request you to kindly look in to the matter and recommend for suitable amendment in the Act.

We also request the Honourable Minister to look in to the following other matters in connection with Co-Operative audits:

1. Panel of auditor and auditing firm as per rule 29-B. The panel of auditors and auditing firms is to be revised and updated from time to time.
2. The appointment of auditors of Urban Co-operative banks need to done by the separate panel of auditors as in the case of DCC banks by NABARD. The autonomy given to management of co-operative banks to select the auditors would hamper the independence of auditors. Therefore similar to Section 98-U, auditor of Urban Banks is to be selected for the panel approved by a separate committee.

3. The rotation of auditors of co-operative societies to be extended to Four years instead of two years to ensure continuity and involvement of auditors.
4. A comprehensive system of audit reports is to be developed as applicable to different types of societies. A committee consisting of officials of department and Institute of Chartered Accountants of India need to be formed for this purpose.
5. For submission of audit reports a separate portal to be established like in Companies act, where the audit reports and accounts to be submitted by auditors electronically.
6. Fixation of audit fees:- The audit fee for Co-operative Societies fixed based on turnover or working capital needs to be revised upwards to meet the current trends.

We seek your approval to submit separate memorandum in detail with action plan and suggestions. We sincerely hope the Honorable Minister shall be kind enough to take up the matter with appropriate authorities.

Yours Sincerely,

**For Karnataka State Chartered Accountants Association (R),**

CA. Dileep Kumar T.M.  
President

CA. Raghavendra T. N.  
Secretary