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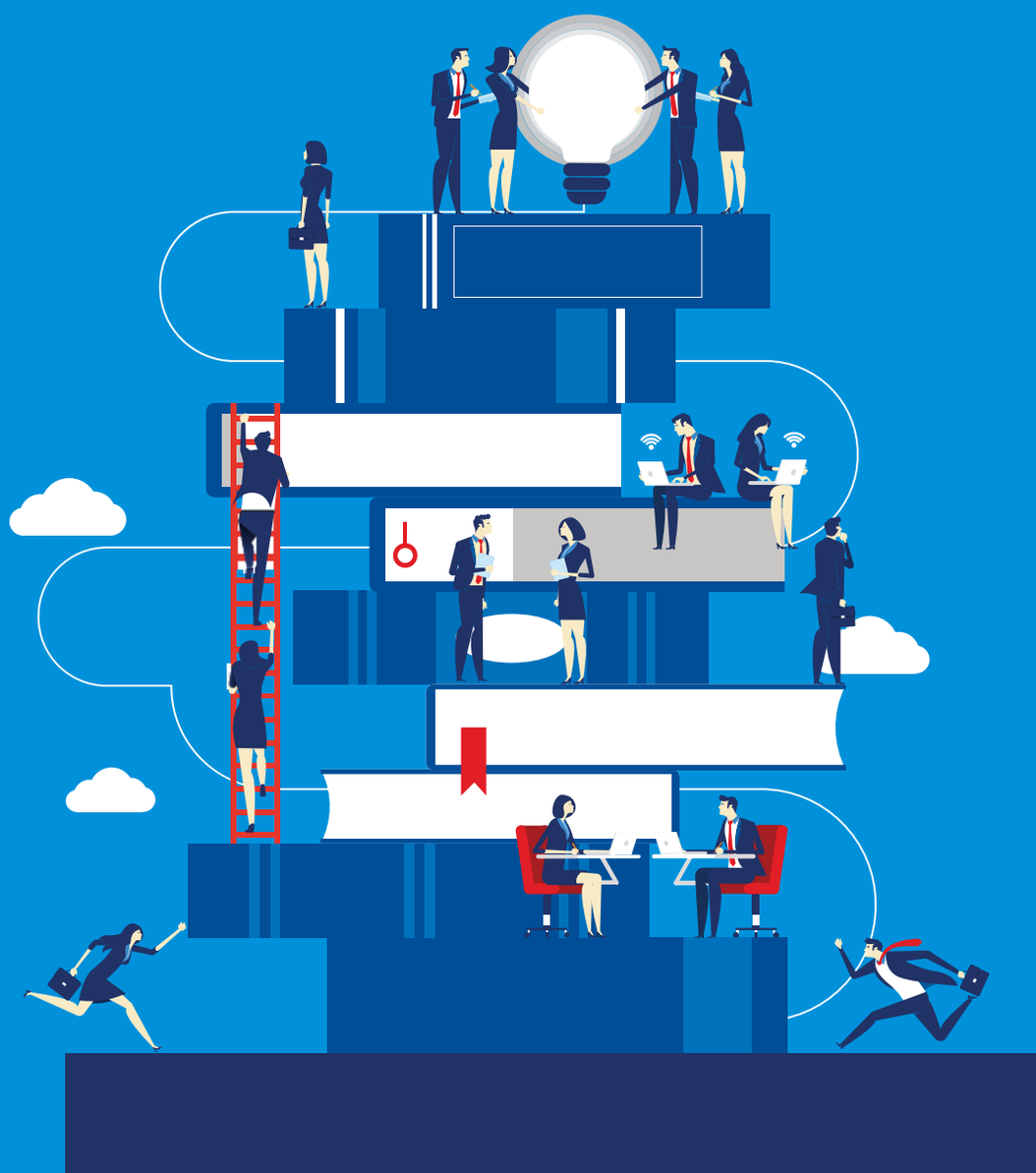
Quarterly updates



July 2018

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In this publication, we have summarised important updates relevant to the quarter ended 30 June 2018 from the Ministry of Corporate Affairs (MCA), the Securities and Exchange Board of India (SEBI), the Reserve Bank of India (RBI) and the Institute of Chartered Accountants of India (ICAI).

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Updates relating to Ind AS

Ind AS implementation road map for Non-Banking Financial Companies (NBFCs) - Phase I companies - Quick recap

On 30 March 2016, the Ministry of Corporate Affairs (MCA) notified the Companies (Indian Accounting Standards) (Amendment) Rules, 2016, which include a road map for implementation of Indian Accounting Standards (Ind AS) by NBFCs. As per this road map, Ind AS has become applicable to the following class of NBFCs in a phased manner from Financial Year (FY) 2018-19:

a) NBFCs with net worth of INR500 crore or more, and

b) Their holding, subsidiary, joint venture or associate entities, other than those entities already covered under the corporate road map.

Important Ind AS transition dates for NBFCs covered in phase I of the road map are as follows:

Date of transition: 1 April 2017

First Ind AS financial statements: 2018-19

Comparative year: 2017-18

Voluntary adoption of Ind AS: NBFCs would apply Ind AS when preparing their financial statements only if they meet the specified criteria and are not permitted to voluntarily adopt Ind AS.

However, NBFCs that are subsidiaries, associates or joint ventures of a parent company, that is required to prepare consolidated Ind AS financial statements under the corporate road map, will be required to provide relevant financial information based on the parent's accounting policies for consolidation purposes.

Some key implementation issues for NBFCs to consider are as follows:

- **First-time adoption considerations:** On first-time application of Ind AS, an NBFC should consider the following:
  - Application of derecognition requirements of Ind AS 109, *Financial Instruments* for transfers done on or from the date of transition.
  - An NBFC may choose not to apply the requirements of Ind AS 102, *Share-based Payments* to equity instruments that vested before the date of transition to Ind AS.

- Classification of financial assets as measured at amortised cost/Fair Value through Other Comprehensive Income (FVOCI)/Fair Value Through Profit and Loss (FVTPL) should be based on facts and circumstances as on the date of transition to Ind AS.
- On the date of transition in the stand-alone financial statements, an NBFC has an option to account for investment in subsidiaries, joint ventures and associates either at cost or fair value.
- As on the date of transition, an NBFC has an option to grandfather Indian GAAP carrying amounts as deemed cost under Ind AS for property, plant and equipment, investment properties and intangible assets.
- Differences in the amount arising from transition to Ind AS would form part of retained earnings as a transitional reserve.

- **Business model assessment:** In order to classify and measure financial assets, an entity is required to assess its business model as per Ind AS 109. Business model is required to determine the basis of measurement for financial assets at amortised cost, FVTPL or FVOCI. Such a business model is required to be approved by the Key Managerial Personnel (KMP).

  In case of NBFCs, management's policy with respect to securitisation/direct assignment of loans may affect the business model within which underlying loans are measured.

  Similarly, there could be complexities around the classification of loans that are originated by an NBFC and part of which is sub-participated to another entity. In such cases, a question arises as to whether there can be two different business models: one with the objective to hold the loan to collect the contractual cash flows and another with the objective to originate and distribute, i.e., the intention to sell.

  In the first case, the part that is held to collect contractual cash flow may be classified as amortised cost and the one with the intention to sell may be categorised as FVOCI/FVTPL, depending upon the facts of the case, therefore, a detailed analysis of the fact pattern would be required to arrive at a conclusion as each case could pose unique challenges in terms of the business model of the NBFC.

- **Derecognition:** Ind AS 109 specifies the criteria for derecognition of a financial asset. As per the standard, derecognition criteria would apply if any of the below mentioned criteria is met:

  a) The cash flows from that portion of the asset are specifically identifiable,

  b) The cash flows are a proportionate share of the total cash flows of the asset, or

  c) The cash flows are a proportionate share of specifically identified cash flows of the asset.

  In case of NBFCs, securitisation/direct assignment transactions which qualify for 'true sale' accounting under Indian GAAP may not qualify as sale under Ind AS. Additionally, under Ind AS, all losses and gains on derecognition of a financial asset would be recognised upfront i.e. they cannot be deferred.

  An NBFC should assess the possible impact on Consolidated Financial Statements (CFS) for securitisation transaction.

- **Equity vs financial liability:** Substance of the contractual arrangement determines classification of an instrument as equity and/or financial liability. For example:

  a) Redeemable preference shares are presented as financial liability

  b) Convertible bonds/debentures may need to be split between liability and equity.

- **Expected Credit Loss (ECL):** Ind AS 109 introduces a new impairment model i.e. ECL for financial assets. The model applies to financial assets (not measured at FVTPL), bank deposits, loans, lease and trade receivables, debt securities, and specified financial guarantees and loan commitments issued.

  The model uses a dual measurement approach, under which the loss allowance is measured as either a 12-month ECL or a lifetime ECL. These requirements represent a paradigm shift from the current practice in the Indian banking and NBFC industry, which follows the income recognition, asset classification and provisioning norms as prescribed by RBI.

The extant norms of RBI are based on the 90-day past-due concept, which ensure consistent application across the industry. The provisioning requirements are based on the period for which the asset has remained non-performing and whether the security is available. The transition from a rule-based regulator-specified criteria approach that ensures consistency of application across the system to an ECL framework based on management judgement, is data intensive, necessitates fairly sophisticated credit modeling skills and would represent an enormous challenge not only for the industry, but also for auditors, regulators, government, etc.

- **Effective Interest Rate (EIR) - Income recognition:** Under Ind AS 109, financial assets and liabilities that are classified at amortised cost are subsequently measured using EIR method. Financial assets classified into FVOCI category may also require application of the EIR method for recognition of interest income.

  Some of the key areas relating to determination of EIR that an NBFC should consider are as follows:

  – Only directly attributable and incremental fees and costs (transaction costs) would need to be considered.

  – The fees and costs would need to be amortised over the expected life of the contract.

  – Interest income would continue to be recognised on financial assets classified within stage 3.

- **Detailed disclosure requirements:** An NBFC would be required to give detailed disclosures under Ind AS relating to the following:

  – Fair valuation and fair value related hierarchy disclosures

  – Credit quality, rating and past due status disclosures

  – Reconciliation type disclosures

  – Extensive disclosures including qualitative and quantitative information.

- **Other issues:** Some of the other issues that require additional consideration by an NBFC are as follows:

  – Consolidation of trust or funds

  – Employee benefits

  – Segment reporting

  – Impact on key ratios (such as cost to income, gross Non-Performing Asset (NPA), provision coverage, return on assets and return on equity)

  – Budgeting and forecasting for FY2018-19

  – Communicating with investors the integration of changes into the business.

(Source: MCA issued Companies (Indian Accounting Standards) (Amendment) Rules, 2016 dated 30 March 2016)

Ind AS Transition Facilitation Group (ITFG) issues Clarifications Bulletin 15

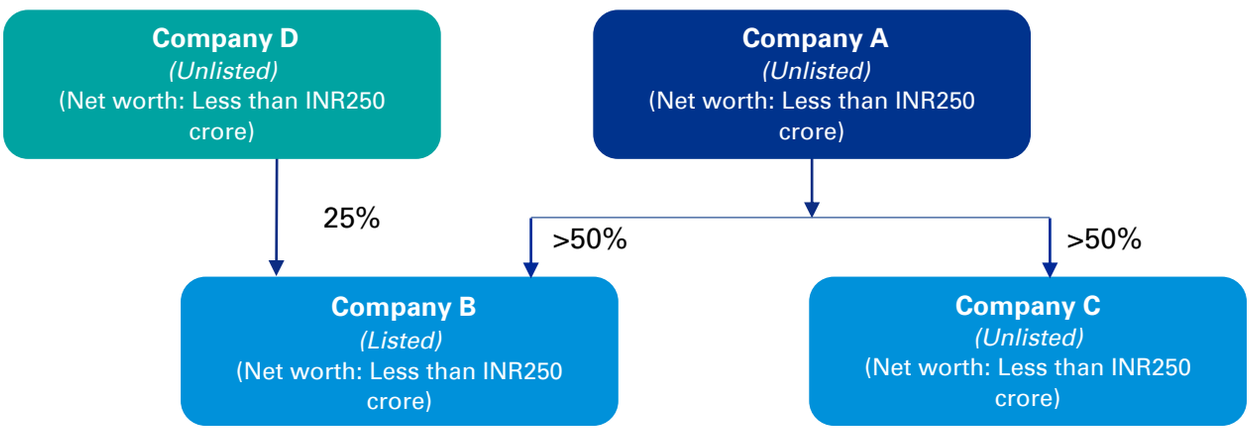
The Ind AS Transition Facilitation Group (ITFG) in its meeting considered certain issues received from the members of the Institute of Chartered Accountants of India (ICAI), and issued its Clarifications' Bulletin 15 on 5 April 2018 to provide clarifications on 10 application issues relating to Ind AS.

Some key clarifications provided in ITFG Bulletin 15 are as follows:

Applicability of Ind AS

a) **Ind AS applicability to entities in a group (Issue 10):** The Ind AS corporate road map applies to all companies which meet the specified criteria, and to their holding, subsidiary, joint venture and associate companies. The ITFG considered a situation wherein a listed entity (company B) with a net worth of less than INR250 crore adopted Ind AS for FY beginning 1 April 2017 (phase II of the corporate road map).

The ITFG considered the applicability of Ind AS to its group companies. The group structure of company B is depicted below:



(Source: KPMG in India's analysis, 2018)

i. **Company A is an unlisted company with net worth less than INR250 crore and the holding company of B:** As per the Ind AS corporate road map, holding, subsidiaries, associate and joint venture companies of entities covered in the Ind AS corporate road map are required to prepare Ind AS financial statements. Accordingly, company A is required to prepare Ind AS financial statements from 1 April 2017.

ii. **Company C is an unlisted company with net worth less than INR250 crore and a fellow subsidiary of B (subsidiary of company A):** The ITFG noted that the requirement to adopt Ind AS does not extend to a fellow subsidiary company, i.e., another subsidiary of an entity's holding company (which is required to adopt Ind AS because of its holding company relationship with the entity that meets the net worth/listing criteria).

A holding company is required to prepare separate and CFS under Ind AS, if one of its subsidiaries meets the specified criteria. Therefore, other subsidiaries may be required by the holding company to furnish financial information as per Ind AS for the purpose of preparing the holding company's consolidated Ind AS financial statements. Such fellow subsidiaries may, however, voluntarily opt to prepare their financial statements as per Ind AS.

Hence, in the given case, company C is not mandatorily required to adopt Ind AS for its statutory reporting, although it may apply Ind AS voluntarily.

iii. **Company D is an unlisted company with net worth less than INR250 crore and holding 25 per cent stake in company B:** With respect to Ind AS applicability to the investor - company D, the ITFG noted that an investor company does not qualify as a holding company of company B. Accordingly, company D is not required to comply with Ind AS by virtue of company B falling within the Ind AS road map. For consolidation purposes, company B may be required to provide financial statement data prepared in accordance with Companies (Accounting Standards) Rules, 2006 for the purpose of preparation of CFS of company D.

Ind AS 32, *Financial Instruments: Presentation*

The ITFG provided clarifications on considerations when determining the classification and measurement of financial instruments as financial liability or equity as per Ind AS 32. The financial instruments considered were:

a) **Foreign Currency Convertible Bonds (FCCBs) (Issue 1):** The ITFG considered a situation where an entity (PQR) had issued FCCBs prior to transition to Ind AS at an interest rate of six per cent per annum, payable on a half-yearly basis for a period of five years and one day (which would mature post transition to Ind AS). The holder of the instruments has an option to convert them into fixed number of shares of PQR.

A borrowing in the same currency, with a similar time period and credit status, but without the conversion option would have carried an interest rate of 7.5 per cent per annum.

The ITFG clarified that from the perspective of the issuer, the FCCB had both a liability and an equity component. The liability component comprised a contractual obligation of PQR to deliver cash to the holder, and the equity component comprised the holder's equity conversion option embedded in the FCCB to acquire a fixed number of entity's own equity instruments. Although the FCCB was denominated in a foreign currency, the conversion option would meet the definition of an equity instrument based on the guidance in paragraph 11(b) of Ind AS 32. Accordingly, PQR would be required to split the FCCB into the liability and equity components on initial recognition and present these separately in the balance sheet as follows:

- **Liability component:** The liability component of the FCCB would be measured at fair value by discounting the contractually determined future cash flows under the instrument (i.e. the scheduled payments of interest and principal) at an interest rate applied at that time by the market to instruments of comparable credit status, providing substantially the same cash flows, on the same terms, but without the conversion option (market interest rate). In this case, the comparable discount rate is 7.5 per cent and therefore, company PQR should discount the future cash flows at 7.5 per cent to determine the financial liability for initial recognition.
- **Equity component:** The equity component would be computed as the residual amount after deducting the liability component from the fair value of the compound instrument.

b) **Compulsorily Redeemable Non-Cumulative Preference Shares (RNCPS) (Issue 2):** The ITFG considered RNCPS issued by an entity (ABC) with a discretionary dividend of six per cent per annum, redeemable in cash after 10 years. The market rate of interest for similar instruments was four per cent per annum. The ITFG considered the accounting treatment for the preference shares and dividend thereon.

The ITFG clarified that in accordance with Ind AS 32, the RNCPS are compound financial instruments, and the liability and equity components of the instruments would be split as follows:

- **Liability component:** This component represents ABC's contractual obligation to redeem the preference shares in cash. Accordingly, the fair value of the liability component on initial recognition would be computed as the present value of the eventual redemption amount discounted at the market interest rate.
- **Equity component:** This component represents the discretionary dividend portion of the preference shares. It will be computed as the difference between the present value of the liability component and fair value of the instrument as a whole.

The ITFG further clarified that any discretionary dividends would be recognised when they are actually declared and paid, and since they relate to the equity component, they will be disclosed in the statement of changes in equity as a distribution of profit or loss.

Ind AS 109, *Financial Instruments*

a) **Classification of incentives receivable from government entities as financial assets (Issue 3):** The ITFG considered whether incentives receivable from government entities on compliance with stipulated conditions (for example, sales tax refunds) would fall within the definition of financial instruments, considering there is no formal one-to-one contractual agreement between the government and the entities.

Ind AS 32 defines a financial asset as a contractual right to receive cash or another financial asset from another entity. It further defines 'contract' and 'contractual' as an agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable by law. Ind AS 32 clarifies that the contract need not be in writing, and may take a variety of forms. Ind AS 109 states that an entity should recognise a financial asset or a financial liability in its balance sheet when the entity becomes a party to the contractual provision of the instrument.

In view of the above, ITFG clarified that when the government provides incentives (for example taxation benefits), it may not enter into a one-to-one agreement with each entity availing those benefits with regard to the rights and obligations of the scheme. Instead, there is an understanding between the government and the entities, that on complying with the stipulated conditions attached to the scheme, the entities will be granted the benefits of the scheme. Once the entities comply with the conditions attached to the schemes, they rightfully become entitled to the incentives. Thus, such an incentive receivable would fall within the definition of financial instruments, and accounted for as a financial asset in accordance with Ind AS 109.

b) **Accounting for interest free refundable security deposits (Issue 7):** The issue considered by ITFG was, whether interest free refundable security deposits given by an entity (such as rent deposits paid to lessor, etc.) are required to be discounted as per Ind AS, and the discount rate to be considered for the same.

A refundable security deposit given by an entity represents its contractual right to receive cash from the holder of the deposit, and hence it falls under the definition of a financial asset in accordance with Ind AS 32. As per Ind AS 109, all financial assets subsequently measured at amortised cost and at fair value through other comprehensive income, are initially recognised at their fair value, plus or minus directly attributable transaction costs. Normally, the fair value of financial assets at initial reocognition is their transaction price (i.e. consideration given or received). However, where a part of the consideration given or received is for something other than the financial instrument, entities are required to compute the fair value of the financial instrument using a fair valuation technique prescribed in Ind AS 113, *Fair Value Measurement*.

In accordance with the above, ITFG clarified that where the effect of time value of money is material (determined on an overall consideration of total cash flows, etc.), the refundable security deposits should be shown at their present value, by discounting all future cash receipts at the market interest rate (to be evaluated by the entity based on its own facts and circumstances). The difference between the transaction price and fair value as determined should be accounted for as an expense, or a reduction of income, unless it qualifies for recognition as some other type of asset. For example, in case of an interest free rent deposit paid to a lessor in respect of a non-cancellable operating lease arrangement, the difference may be deferred as prepaid rent to be recognised as an expense over the underlying lease term in accordance with Ind AS 17, *Leases.*

Ind AS 103, *Business Combinations*

a) **Application of Ind AS to past business combinations of entities under common control (Issue 6):** The ITFG considered a situation where an entity (Y) merged with its wholly- owned subsidiary (X) prior to transition to Ind AS. On the day prior to the merger, the promoters of Y held 49.95 per cent stake in Y. On transition to Ind AS, X did not opt for the exemption from applying Ind AS 103 retrospectively to past business combinations (under paragraph C1 of Ind AS 101, *First-time Adoption of Indian Accounting Standards*). The issue considered by ITFG was, whether X is required to apply the requirements of Appendix C to Ind AS 103 (business combinations of entities under common control) in the given case.

As per paragraph C1 of Ind AS 101, where a first-time adopter of Ind AS restates its past business combinations to comply with Ind AS 103, it is also required to apply Ind AS 110, *Consolidated Financial Statements* from that same date.

Under the Indian Generally Accepted Accounting Principles (IGAAP), AS 21, *Consolidated Financial Statements* stated that control was established when an entity owned more than half of the total voting power of an enterprise or controlled the composition of the Board of Directors (BoD) or of the corresponding governing body (as the case may be). Ind AS 110 widens the concept of control, and accordingly, investors with less than majority voting rights can also have control over the investee under Ind AS 110 (e.g. through contractual arrangements, de facto control, potential voting rights, etc.). It also specifies the accounting treatment for a business combination involving entities under common control.

In this regard, ITFG clarified that X should evaluate whether both X and Y were under common control before and after the amalgamation. Assuming there was common control, X would be required to apply the provisions of Appendix C to Ind AS 103 retrospectively to the amalgamation.

Ind AS 17, *Leases*

a) **Lease premium collected at the time of lease deed (Issue 8):** A situation was considered by ITFG, where a government company (XYZ), in the business of development of a smart city, allotted its land to a customer on 99 years of lease. The customer was required to pay a non-refundable lease premium (being the market value of land) at the time of execution of the lease deed, and a nominal amount of lease rent would be paid on an annual basis over a period of 99 years. On completion of 99 years, the lease would be renewable at the mutual consent of the lessor and lessee. The issue considered was the accounting treatment for the non-refundable lease premium collected at the time of execution of the lease deed as per Ind AS.

The ITFG clarified that revenue arising from lease agreements would be accounted for in accordance with Ind AS 17 (and not Ind AS 18, *Revenue*). Accordingly, the recognition of income would depend on the classification of lease, either as an operating lease or a finance lease, as given below:

- **Operating lease:** XYZ would be required to present assets subject to operating lease in its balance sheet according to their nature. Further, lease income would be recognised on a straight-line basis over the lease term, unless another systematic basis was more representative of the time pattern in which user benefit was derived.
- **Finance lease:** The lessor, XYZ, is required to recognise a receivable at an amount equal to the net investment in the lease. Finance income would be recognised based on a pattern reflecting a constant periodic return on the lessor's net investment in the finance lease.

The ITFG further clarified that a lease of land for 99 years is an indication for classification as a finance lease. The ITFG previously in its Bulletin 7 (Issue 5) dealt with the broad principles to be assessed while classifying a lease as an operating or a finance lease. Therefore, consideration should be given to relevant facts and circumstances. If the lease is considered as a finance lease, then in this case the entire lease premium has been received upfront, therefore, the lessor would not be required to recognise a receivable.

For a detailed overview of the clarifications, please refer to KPMG in India's IFRS Notes on 'ITFG issues Clarifications Bulletin 15' dated 18 April 2018.

Key takeaways

The ITFG clarifications are expected to resolve various practical implementation issues faced by companies transitioning to Ind AS. The companies should consider the interpretations provided by the ITFG in their implementation efforts. However, it should be noted that some of the issues would require consideration of facts and circumstances and the exercise of judgement while analysing each individual situation.

(Source: ICAI-ITFG clarifications' bulletin 15 dated 5 April 2018 and KPMG in India's IFRS Notes dated 18 April 2018)

Updates relating to the Companies Act, 2013

Notification of certain sections of the Companies (Amendment) Act, 2017 and modification of certain Rules under the Companies Act, 2013 (2013 Act)

On 3 January 2018, the Companies (Amendment) Act, 2017 received the assent of the President of India. The various provisions of the Companies (Amendment) Act, 2017 would come into force on the date of their notification in the official gazette by the Central Government (CG). Different dates could be appointed for different provisions of the Companies (Amendment) Act, 2017.

The MCA has notified 45 sections of the Companies (Amendment) Act, 2017 till 9 February 2018.

Recently, MCA through its notifications dated 7 May 2018 and 13 June 2018 notified certain sections of the Companies (Amendment) Act, 2017. Additionally, MCA issued amendments to certain related rules under the 2013 Act.

Key amendments effective from 7 May 2018

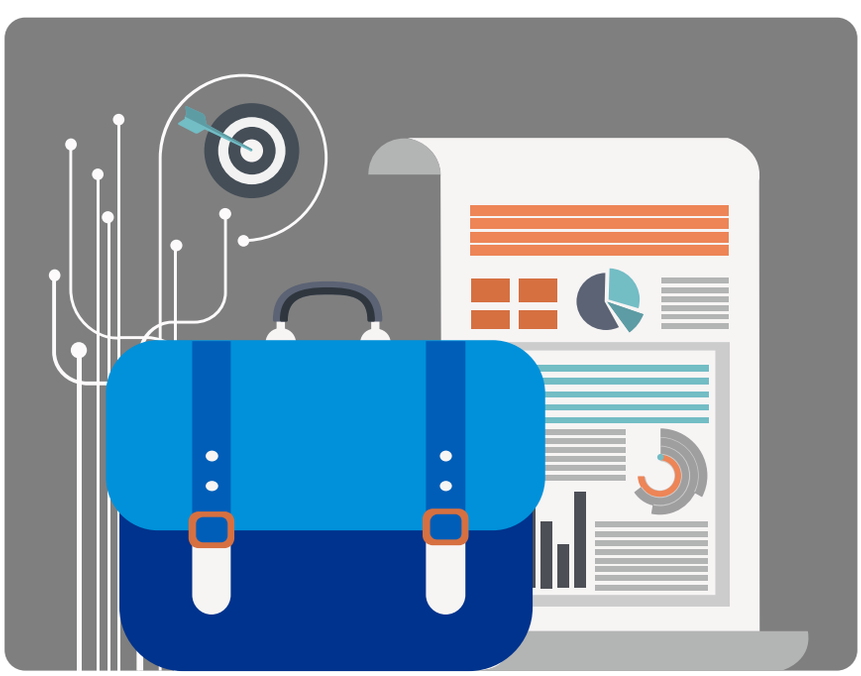
Section	Overview of the amendments
Definitions	
Explanation to Section 2(6) and Section 2(87)	The Companies (Amendment) Act, 2017 has modified the definitions of the following terms: • **Subsidiary:** The term 'total share capital' (i.e. paid-up equity share capital and convertible preference share capital) has been replaced by the term **'total voting power'** as the basis for deciding holding/subsidiary relationship. (Section 2(87)) Also the definition of the term 'total share capital' has been removed from the Companies (Specification of Definitions Details) Rules, 2014. • **Associate company:** In the revised definition of an 'associate company', significant influence means control of at least 20 per cent of the **total voting power** (earlier total share capital), or control of or **participation in business decisions under an agreement**. (Section 2(6))

Section	Overview of the amendments
Definitions (cont.)	
Explanation to Section 2(6)	• **Joint venture:** Currently, the term 'joint venture' has not been specifically defined in the 2013 Act and the definition of an associate company included the term 'joint venture'. The Companies (Amendment) Act, 2017 defines 'joint venture' as a 'joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement'. The definition is in accordance with Ind AS 28, *Investments in Associates and Joint Ventures*. (Section 2(6))
Appointment and qualification of directors	
Independent directors **(Section 149)**	**Independent director:** Following changes have been notified with respect to provisions of an independent director: • Pecuniary relationship will not include the remuneration received by an independent director and any amount from a transaction which does not exceed 10 per cent of his/her total income (or such amount as may be prescribed). • Section 149(6)(d) has been amended with respect to the scope of restriction on a 'pecuniary relationship or transaction' entered by a relative and has been made more specific by clearly categorising the types of transaction. For example, none of the relatives of an independent director: a) Should hold any security of or interest in the company, its holding, subsidiary or associate company during the two immediately preceding FYs or during the current FY. However, the relative may hold security or interest in the company of face value not exceeding INR50 lakh or two per cent of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed. b) Is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors, in excess of such amount as may be prescribed during the two immediately preceding FYs or during the current FY (the Companies (Appointment and Qualification of Directors) Rules specify that indebtedness should not be in excess of INR50 lakh). c) Has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company (the Companies (Appointment and Qualification of Directors) Rules specify that indebtedness should not be in excess of INR50 lakh). Currently, an individual is restricted from being appointed as an independent director in case he/she or his/her relative is a KMP or an employee of the company or its holding, subsidiary or associate company during any of the preceding three FYs. The Companies (Amendment) Act, 2017 clarifies that this restriction would not apply if a relative of an independent director is employed during the preceding three FYs.

Section	Overview of the amendments
Appointment and qualification of directors (cont.)	
Disqualification for appointment of a director **(Section 164)**	Currently, a director of a company which has defaulted on certain requirements is not eligible to be reappointed as a director of that company or appointed in another company for a period of five years from the date of the failure. Those defaults are as follows: a) Not filed financial statements or annual returns for any continuous period of three FYs or b) Failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared for a continuous period of one year. The Companies (Amendment) Act, 2017 has clarified that a director would not incur disqualification (if the company has defaulted on the above grounds) for a period of six months from the date of his/her appointment. Additionally, a director would continue to be disqualified if he/she has been convicted by a court for any offence, on the order of the Tribunal and convicted in the matter of Related Party Transactions (RPTs), even if an appeal or petition has been filed against the order of conviction or disqualification.
Vacation of office **(Section 167)**	Section 167 of the 2013 Act specifically provides that the office of a director should become vacant in case he/she incurs disqualifications specified in Section 164 of the 2013 Act or becomes disqualified by an order of a court or the Tribunal. However, the Companies (Amendment) Act, 2017 clarifies that in case a director gets disqualified on grounds of Section 164(2) of the 2013 Act (i.e. non-filing of financial statements or failure to repay dues), then the office of the director would become vacant in all the companies other than the company which is in default under Section 164(2). Additionally, the Companies (Amendment) Act, 2017 has provided a relaxation and provided that a director would not be required to vacate his/her office in respect of disqualification by an order of a court or the Tribunal or conviction for any offence in the following events: • For 30 days from the date of conviction or order of disqualification • Where an appeal or petition is preferred within 30 days as aforesaid against the conviction resulting in sentence or order, until expiry of seven days from the date on which such appeal or petition is disposed of or • Where any further appeal or petition is preferred against order or sentence within seven days, until such further appeal or petition is disposed of. Earlier the 2013 Act was stringent and required that the office should be vacated by the director even if he/she has filed an appeal against the order of such court.
Meetings of board and its powers	
Meetings of board **(Section 173 and the Meetings Amendment Rules, 2018)**	The 2013 Act empowered the CG to specify matters which should not be dealt in a meeting through video conferencing or other audio visual means. These matters include the approval of the annual financial statements, the approval of the board's report, etc. The Companies (Amendment) Act, 2017 and the Companies (Meetings of Board and its Powers) Amendment Rules, 2018 (Meetings Amendment Rules, 2018) clarify that in case the quorum for a meeting is met through physical presence of directors, then any other director may participate through video conferencing or other audio visual means and discuss the matters as specified.

Section	Overview of the amendments
Meetings of board and its powers (cont.)	
Audit committee **(Section 177 and Rule 6 of the Meeting Rules)**	As per the Companies (Amendment) Act, 2017, the BoD of every listed **public** company (earlier the 2013 Act referred to every listed company) and such other class or classes of companies, as may be prescribed should constitute an audit committee. Similar amendment has been made in the Companies (Meetings of Board and its Powers) Rules, 2014 (Meeting Rules) as well. The Companies (Amendment) Act, 2017 clarified that the existing requirement under the 2013 Act for the audit committee to pre-approve all RPTs subject to the approval of the BoD or shareholders as required by Section 188 would continue. Whereas, for transactions that are not covered under Section 188, the audit committee can give recommendations to the BoD, in case it does not approve the transaction. Additionally, a transaction (involving an amount up to INR1 crore) is voidable at the option of the audit committee if it has been entered without its approval and has not been ratified subsequently by it. Further, where the transaction is with a related party of a director, or a director has authorised the transaction, such director would indemnify the company against any loss. Further, RPTs between a holding company and its wholly-owned subsidiary that do not require board's approval under Section 188, would not require approval of an audit committee.
Nomination and Remuneration Committee (NRC) **(Section 178)**	Following changes have been made to the provisions relating to NRC: • Every listed **public** company (earlier the 2013 Act referred to every listed company) and a company covered under Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014 is required to constitute a NRC. • NRC is required to specify the methodology for effective evaluation of the performance of the individual directors, committees of the board and the board as a whole which should be carried out by the board, by the NRC or by an independent external agency and should review its implementation and compliance. Additionally, companies could place their remuneration policy on their website, if any, and should disclose only the salient features of the policy, the changes, if any along with the web address of the policy in the board's report.
Loans and investments by companies	
Loan to directors **(Section 185)**	Companies can now provide a loan, guarantee or security in connection with any loan, to any person in whom the director is interested, subject to prior approval by a special resolution in a general meeting and loans should be utilised by the borrowing company for its principal business activities. Further, companies that provide loans or give guarantees or securities in normal course of business, are permitted to do so at specified interest rate **i.e. not less than the rate of prevailing yield of one year, three year, five year or 10 year government security, closest to the tenor of the loan** (currently, specified interest rate is the rate not less than the bank rate declared by the RBI).

Section	Overview of the amendments
Loans and investments by companies (cont.)	
Loan and investment by company **(Section 186 and Rule 13 of the Meeting Rules)**	A company is allowed to give loan to its employees in excess of the specified limits (i.e. 60 per cent of its paid-up share capital, free reserves and securities premium account or 100 per cent of its free reserves and securities premium account, whichever is higher) without passing a special resolution. In this relation, MCA amended Rule 13 of the Meeting Rules, to provide that the special resolution should specify the total amount up to which the BoD are authorised to provide such loan or guarantee, security or acquire shares of other companies. Additionally, definition of an investment company has been modified to provide that a company would be deemed to be principally engaged in the business of acquisition of shares, debentures or other securities, if its: a) Assets in the form of investment in shares, debentures or other securities constitute not less than 50 per cent of its total assets, or b) Its income derived from investment business constitutes not less than 50 per cent as a proportion of its gross income.
Audit and Auditors	
Appointment of an auditor **(Section 139 and Rule 3 of the Audit Rules)**	Currently under the 2013 Act, companies are required to appoint their auditors for a period of five years which is subject to annual ratification by the shareholders at the annual general meeting. The Companies (Amendment) Act, 2017 has removed this requirement of annual ratification once the auditors have been appointed for five years. The provision with respect to the annual ratification has been removed from the Companies (Audit and Auditors) Rules, 2014 (Audit Rules) as well.



Key amendments effective from 13 June 2018 and 14 June 2018

Section	Overview of the amendments
Declaration of significant beneficial ownership in a company	
Section 90[1] and Beneficial Owners Rules[2]	Every individual, (either acting alone or together, or through one or more persons or trust, including a trust and persons resident outside India) holding beneficial interests[3], of not less than 25 per cent in shares of a company or the right to exercise, or the actual exercising of significant influence or control would be required to make a declaration to the company (of nature of interest and other particulars). This declaration would be made in **Form No. BEN-I** as per the Companies (Significant Beneficial Owners) Rules, 2018 (Beneficial Owners Rules) in the following manner: • *Beneficial interests held as on 14 June 2018:* Up to 12 September 2018 (i.e. within 90 days from 14 June 2018) • *Any change in significant beneficial ownership:* Up to 14 July 2018 (i.e. within 30 days from 14 June 2018) • *Beneficial interests acquired after 14 June 2018:* Within 30 days of acquiring such significant beneficial ownership or in case of any change in such ownership. A declaration in **Form No. BEN-2** to be filed by the company with the Registrar of Companies (ROC) within 30 days from the date of receipt of above mentioned declaration.

(Source: KPMG in India's analysis, 2018 based on the provisions of the Companies (Amendment) Act, 2017 notified with effect from 7 May 2018 and 13 June 2018 and MCA notification no. G.S.R. 561(E) dated 14 June 2018)

For a detailed overview of the sections notified, please refer to KPMG in India's First Notes on 'MCA notified certain provisions of the Companies (Amendment) Act, 2017' dated 28 May 2018.

1. Applicable from 13 June 2018.
2. Applicable from 14 June 2018.
3. *Beneficial interest* in a share includes, directly or indirectly, through any contract, arrangement or otherwise, the right or entitlement of a person alone or together with any other person to:
   a) Exercise or cause to be exercised any or all of the rights attached to such share or
   b) Receive or participate in any dividend or other distribution in respect of such share.

Key takeaways

With the recent MCA notification, the Companies (Amendment) Act, 2017 is now largely effective. The new legislations and changes introduced are very vast and also aimed at aligning the 2013 Act with various rules and regulations of the SEBI and the RBI.

Some of the key changes notified are as follows:

- **Alignment of definitions:** Some of the fundamental definitions in the 2013 Act were inconsistent with the AS/Ind AS and had effect on number of provisions of the 2013 Act. Some of the important changes to definitions are as follows:
  - *Subsidiary:* The definition of subsidiary in the 2013 Act referred to 'total share capital' i.e. aggregate of the paid-up equity share capital and the convertible preference share capital. Now, the Companies (Amendment) Act, 2017 has changed the reference to 'total voting power'. In many cases, the total voting power would be with reference to the equity share capital. However, if dividend in respect of a class of preference shares has not been paid for a period of two years or more, then such class of preference shareholders would also have right to vote on the resolutions placed before the company.
  - *Joint Venture:* The 2013 Act did not define the term 'joint venture' and made reference to joint venture as an inclusive part in the definition of the term 'associate company'. The Companies (Amendment) Act, 2017 continues to refer joint venture within the term associate company but also defines joint venture in line with Ind AS 28. However, Ind AS 28 further defines the terms 'joint arrangement' and 'joint control' which are associated with the definition of joint venture. While the Companies (Amendment) Act, 2017 does not include these definitions, we believe that the intent of the law has been to align the definition of joint venture with Ind AS and therefore, the two associated definitions of joint control and joint arrangement could be read harmoniously with Ind AS.
- **Loans and investments by companies in which directors are interested:** The newly notified provision permits companies to provide loans/guarantees/security to any person in whom the director is interested, subject to specified conditions. This is a welcome step as it is expected to provide significant relief to the companies and to resolve practical issues being faced in genuine transactions of financing among group companies due to complete restriction on providing loans enforced by the 2013 Act.
- **Loans and investments by companies in wholly-owned subsidiaries or joint ventures:** Currently, Rule 11 of the Meeting Rules provide a relaxation to companies in relation to loans/security/ guarantees provided to the company's wholly-owned subsidiary or a joint venture, or when the company acquires the securities of its wholly-owned subsidiary. However, the 2013 Act was silent on them. Therefore, the Companies (Amendment) Act, 2017 has incorporated the relaxation into the 2013 Act, hence, resolves the anomaly.
- **Transactions outside the scope of pecuniary relationship for an independent director:** The Companies (Amendment) Act, 2017 specifically excludes the amount of remuneration received by an independent director and any transaction up to 10 per cent of his/her total income from the definition of pecuniary relationship. The change is very significant and expands the scope of transactions that an independent director could enter into. However, such transactions would still be monitored by the companies in order to ensure the independence of an independent director at all times.

  Additionally, the Companies (Amendment) Act, 2017 has modified the scope of restriction on a 'pecuniary relationship or transaction' entered by a relative of an independent director by clearly categorising them into types of transactions. These restrictions are in relation to holding of a security or interest, indebtedness, providing guarantee or security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company. Additionally, the restrictions also scope in any other pecuniary transaction or relationship. The Companies (Amendment) Act, 2017 provides relief to independent directors by specifying thresholds upto which these restrictions would not apply.

Key takeaways (cont.)

- **Vacation of office by director:** Earlier, the 2013 Act specified that if any director incurs disqualification specified under Section 164(2) (i.e. non-filing of financial statements/annual return or failure to repay dues by the company) then such a director was required to immediately vacate offices in all the companies where he or she is a director. This situation posed a challenge for the companies if they have committed the default as their office of directors would become vacant due to disqualification. Also the company would have difficulty in appointing a new director as such new director would also attract disqualification.

  To resolve these issues, the Companies (Amendment) Act 2017 provides that in case of disqualification specified under Section 164(2), the director would vacate offices in all companies except the company which is in default. Further, the person appointed as director in defaulting company would not incur disqualification for a period of six months from the date of appointment. Additionally, the director of a company under such default would continue to remain liable for the affairs of the defaulting company.

- **New sections notified:** MCA notified following sections of the Companies (Amendment) Act, 2017 with effect from 15 August 2018:
  - Prohibition on acceptance of deposits
  - Repayment of deposits
  - Companies capable of being registered under Chapter XXI of the 2013 Act and
  - Obligations of companies registered under Chapter XXI of the 2013 Act.

- **Sections not yet notified:** Following are some of the key sections which are still pending to be notified:
  - Issue of shares on private placement basis
  - Financial statements, board's report, etc.
  - Corporate Social Responsibility (CSR)
  - Managerial remuneration
  - Calculation of profits
  - Inspection, inquiry and investigation.

(Source: MCA notifications dated 7 May 2018, 13 June 2018 and 5 July 2018, notification no. G.S.R. 561(E) dated 14 June 2018 and KPMG in India's First Notes dated 28 May 2018)

Amendment to AS 11 relating to disposal of a non-integral foreign operation

On 18 June 2018, MCA issued Companies (Accounting Standards) Amendment Rules, 2018 to issue amendments to AS 11, *The Effects of Changes in Foreign Exchange Rates* effective from 1 April 2018.

Currently, AS 11, provides that in case of disposal of a non-integral foreign operation, the cumulative amount of the exchange differences which have been deferred and which relate to that operation should be recognised as an income or as an expense in the same period in which the gain or loss on disposal is recognised. Additionally, AS 11 specifies what would constitute a disposal of interest by an entity in a non-integral foreign operation.

In this regard, MCA amended AS 11 to clarify that the remittance from a non-integral foreign operation by way of repatriation of accumulated profits does not form part of a disposal unless it constitutes return of the investment.

(Source: MCA notification no. G.S.R. 569(E) dated 18 June 2018)

Updates relating to SEBI

Amendments to SEBI Listing Regulations pursuant to Kotak Committee recommendations

On 9 and 10 May 2018, SEBI issued certain amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations). These amendments are a follow up to the decisions taken at the SEBI Board meeting held in March 2018, wherein it had accepted a number of recommendations of the Committee on Corporate Governance constituted by SEBI under the chairmanship of Uday Kotak (the Kotak Committee)[4].

The amendments relate to the following areas:

i. Composition and role of the board

ii. Institution of independent directors

iii. Board committees

iv. Monitoring of group entities and related parties

v. Accounting and audit-related matters

vi. Disclosures and transparency

vii. Investor participation.

It is important to note that while many of the amendments are applicable from 1 April 2019, there are certain amendments that are applicable immediately. These are as follows:

Amendment effective from 9 May 2018 (Mandatory)

- **Searchable formats of disclosures:** All the disclosures made by the listed entity on its website and submitted to the stock exchanges would need to be in a searchable format that allows users to find relevant information easily.

  Additionally, all disclosures made to the stock exchanges by listed entities should be in XBRL format.

Amendments effective from 10 May 2018 (Recommendatory)

- **Group governance unit:** Where a listed entity has a large number of unlisted subsidiaries:

  a) The listed entity may monitor their governance through a dedicated group governance unit or governance committee comprising the members of the board of the listed entity.

4. The Committee was formed in June 2017 with the aim of improving standards of corporate governance of listed entities in India. On 5 October 2017, SEBI released for comments the report of the committee.

b) A strong and effective group governance policy may be established by the entity.

The decision of setting up of such a unit/committee or having such a group governance policy would rest with the BoD of the listed entity.

- **Disclosures on board evaluation:** The equity listed entities may consider following points as a part of their disclosures on board evaluation:

  a) Observations of board evaluation carried out for the year

  b) Previous year's observations and actions taken

  c) Proposed actions based on current year observations.

- **Disclosures on long-term and medium term strategy:** A listed entity may disclose, under the Management Discussion and Analysis (MD&A) section of the annual report, within the limits set by its competitive position, its medium-term and long-term strategy based on a time frame as determined by its BoD.

For a detailed overview of the amendments made to the Listing Regulations, please refer to KPMG in India's publications 'Amendments to SEBI Listing Regulations pursuant to Kotak Committee recommendations' and 'Corporate Governance for listed entities - Are you ready for the change?' dated 19 June 2018.

(Source: SEBI (Listing Obligations and Disclosure Requirements) (Amendment) Regulations, 2018 dated 9 May 2018, SEBI circular SEBI/HO/CFD/CMD/CIR/P/2018/79 dated 10 May 2018 and KPMG in India's publications dated 19 May 2018)

SEBI's decision to approve SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations)

Background

On 26 August 2009, SEBI issued ICDR Regulations, 2009 which laid down guidelines relating to various kinds of issues including public and rights issue. The ICDR Regulations provide detailed provisions relating to public issue such as conditions for making an Initial Public Offer (IPO) and Further Public Offer (FPO), conditions relating to pricing in public offerings, conditions governing promoter's contribution, etc.

In June 2017, SEBI constituted an ICDR committee to review and realign the ICDR Regulations, 2009 with the changes in market practices and regulatory environment.

Based on the recommendations of the ICDR committee, in May 2018, the Primary Market Advisory Committee (PMAC) of SEBI issued a consultation paper on changes to be made to the ICDR Regulations through ICDR Regulations, 2018.

New development

The SEBI in its board meeting dated 21 June 2018, decided to approve the ICDR Regulations, 2018.

Some of the key proposals approved by SEBI are as follows:

- **Revised definition of promoter group:** In case the promoter is a **body corporate**:

  – Any body corporate in which the promoter holds **20 per cent** (earlier 10 per cent) or more or which holds **20 per cent** (earlier 10 per cent) or more of the promoter would be classified as being part of the same promoter group.

  – Any body corporate in which a group of individuals or companies or combinations thereof, which holds **20 per cent** (earlier 10 per cent) or more of the equity share capital in that body corporate, also holds **20 per cent** (earlier 10 per cent) or more of the issuer, would be classified as promoter group only if they are acting in concert.

- **Clarification regarding definition of group company(ies):** Group company(ies) should include companies (other than promoter(s) and subsidiary(ies)) with which **there were RPTs, during the period for which financial information is disclosed (i.e. three years),** as covered under the applicable ASs and other companies as considered material by the BoD of the issuer.

- **Financial disclosures in case of public/rights issue**: In case of public/rights issue:

  – Financial disclosures would be required to be made for **three** years (currently for five years).

- Restated and audited financial disclosures in the offer document would be made on **consolidated basis only**. **Audited stand-alone financials** of the issuer and material subsidiaries would be required to be disclosed on the website of the issuer company.
- Incorporation of the principles governing disclosures of Ind AS on Indian GAAP financials.

- **Others:** The SEBI has approved the following other recommendations:
  - In case of rights issue, the threshold for submission of the draft letter of offer to SEBI would be increased to **INR10 crore** (currently INR50 lakh).
  - For a company to be eligible to make a fast track rights issue, it should not have any audit qualification or adverse opinion.
  - If 90 per cent of the fresh issue has been subscribed in a main board IPO, underwriting would be restricted to that portion only.

    Accordingly, the requirement to underwrite 100 per cent of the issue without regard to the minimum subscription requirements has been omitted.
  - The requirement of announcing price band five working days before opening of the issue would be reduced to **two working days before opening of the issue**.

(Emphasis added to highlight the changes approved by SEBI)

Key takeaways

The ICDR Regulations, 2018 are intended to align the provisions of the ICDR with that of the 2013 Act, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and SEBI (Share Based Employee Benefits) Regulations, 2014.

Companies planning to go for an IPO should carefully consider the requirements of the ICDR Regulation, 2018 as these are likely to change the manner of making any offer (including an IPO).

(Source: SEBI consultation paper on 'Review of ICDR Regulations, 2009' issued in June 2017 and SEBI press release no. PR No.20/ 2018 dated 21 June 2018)

Updates relating to RBI

Prudential norms for classification, valuation and operation of investment portfolio by banks - spreading of Marked-To-Market (MTM) losses and creation of Investment Fluctuation Reserve (IFR)

Background

The investment portfolio of banks is categorised under the following categories:

- **Held to Maturity (HTM):** It comprises securities which have been acquired by the banks with the intention to hold them up to maturity.
- **Held for Trading (HFT):** It comprises securities acquired by the banks with the intention to trade by taking advantage of the short-term price/ interest rate movements.
- **Available for Sale (AFS):** Securities which do not fall within the above two categories are to be classified under AFS category.

Further, investments classified under HTM category need not be MTM and will be carried at acquisition cost. If acquisition cost is more than the face value, then the premium should be amortised over the period remaining to maturity.

However, banks are required to MTM individual scrips in AFS category at quarterly/more frequent intervals and HFT at monthly/more frequent intervals and provide for net depreciation, if any.

The RBI through its notification dated 2 April 2018, decided to grant banks the option to spread provisioning for MTM losses on investments held in AFS and HFT categories, for the quarters ended 31 December 2017 and 31 March 2018.

New development

There has been continuous increase in the yields on government securities and many banks did not have adequate time to build IFR. Therefore, RBI through its notification dated 15 June 2018, decided to grant banks the option to spread provisioning for their MTM losses on all investments held in AFS and HFT for the quarter ended 30 June 2018.

Accordingly, the provisioning required could be spread equally over up to four quarters, commencing with the quarter ended 30 June 2018.

Banks which utilise the above option are required to make suitable disclosures in their notes to accounts/quarterly results which should provide following details:

a) Provisions for depreciation of the investment portfolio for the quarter ended June 2018

b) Balance required to be made in the remaining quarters.

It is important to note that other requirements (including creation of IFR) of the prudential norms would remain unchanged.

Key takeaways

- The notification allows banks to spread provision for MTM losses for the first quarter of the FY2018-19 equally over the next four quarters, commencing from the quarter ended 30 June 2018.
- When a bank spreads its provisions for MTM losses over the four quarters, then it needs to provide adequate disclosures in its quarterly results.

(Source: RBI notification no. RBI/2017-18/147 dated 2 April 2018 and notification no. RBI/ 2017-18/200 dated 15 June 2018)

Updates relating to ICAI

Notification of Indian Valuation Standards (Ind VS)

Background

Section 247 of the 2013 Act governs the provisions relating to valuation by registered valuers. On 18 October 2017, MCA notified Section 247 of the 2013 Act and issued Companies (Registered Valuers & Valuation) Rules, 2017 (Valuation Rules) which provide that the CG may constitute a committee to advise on matters and to make recommendations on formulation and laying down of valuation standards and policies for compliance by the companies and registered valuers.

New development

On 10 June 2018, ICAI issued the following Ind VS:

- Ind VS 101, *Definitions*
- Ind VS 102, *Valuation Bases*
- Ind VS 103, *Valuation Approaches and Methods*
- Ind VS 201, *Scope of Work, Analyses and Evaluation*
- Ind VS 202, *Reporting and Documentation*
- Ind VS 301, *Business Valuation*
- Ind VS 302, *Intangible Assets*
- Ind VS 303, *Financial Instruments*.

The ICAI has issued Ind VS to standardise the principles, practices and procedures followed by registered valuers and other valuation professionals in valuation of assets, liabilities or a business. Additionally, the standards provides concepts, principles and procedures considering internationally accepted practices and procedures considering internationally accepted practices and legal framework and practices prevalent in India.

Further, in respect of valuation engagements under other statutes like Income-tax Act, 1961, SEBI, Foreign Exchange Management Act (FEMA), etc., the application of Ind VS would be on recommendatory basis for the members of ICAI.

Effective date: The Ind VS are applicable for the valuation reports issued on or after 1 July 2018. Further, the Ind VS will be effective till valuation standards are notified by the CG under Rule 18 of the Valuation Rules.

(Source: Ind VS 2018 issued by ICAI dated 10 June 2018)

FAQ on accounting treatment of increase in liability due to enhancement of the gratuity ceiling

Background

The Payment of Gratuity (Amendment) Act, 2018 (the Act) has been notified with effect from 29 March 2018 which amends the Payment of Gratuity Act, 1972 (Gratuity Act). The Act has empowered CG to notify the maximum ceiling for gratuity, as it deems fit (keeping in view the increase in wage and inflation, and future pay commissions).

Accordingly, the CG specified that the amount of gratuity payable to an employee should not exceed INR20 lakh (currently INR10 lakh). However, an employee has the right to receive better terms of gratuity under any award or agreement or contract with the employer.

New development

Recently, ICAI has issued a FAQ to clarify the accounting treatment of increase in liability due to enhancement of the gratuity ceiling.

As per the guidance, the gratuity benefit is an employee benefit and accordingly, any increase in company's liability due to enhancement of the gratuity ceiling would be accounted for as per the principles of AS 15, *Employee Benefits* or Ind AS 19, *Employee Benefits*, as the case may be.

The ICAI considered the guidance provided by AS 15/Ind AS 19 and clarified that the increase in liability arising due to enhancement of gratuity ceiling is a past service cost. Additionally, since no exemption is provided by AS 15/Ind AS 19 with regard to the accounting treatment of increase in liability arising on account of past service cost, companies would be required to account such increase in liability as an expense as per the applicable standard.

(Source: Payment of Gratuity (Amendment) Act, 2018 issued by the Ministry of Law and Justice on 29 March 2018 and FAQ issued by ICAI dated 14 May 2018)

FRRB issued its observations on compliance with financial reporting requirements by listed and other companies

The Financial Reporting Review Board (FRRB)[5] of the ICAI, issued its third volume of 'Study on Compliances of Financial Reporting Requirements' (the study). The study[6] highlights instances of non-compliances by certain companies[7] with the reporting requirements prescribed under:

- Accounting Standards (ASs)
- Standards on Auditing (SAs)
- Schedule II and III to the 2013 Act/Revised Schedule VI to the Companies Act, 1956
- Other relevant laws and regulations including:
  - The Companies (Auditor's Report) Order (CARO)
  - The Banking Regulation Act, 1949
  - The IRDAI (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002.

Some of the key observations of FRRB are as follows:

Compliance with AS

- **AS 1, *Disclosure of Accounting Policies:*** Gain on outstanding derivative contract has been recognised in the statement of profit and loss which is against the principle of prudence as given in AS 1 (i.e. in view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash). In this case, the company did not state whether it has adopted AS 30, *Financial Instruments: Recognition and Measurement*, AS 31, *Financial Instruments: Presentation* and AS 32, *Financial Instruments: Disclosures.*

5. The FRRB was formed by ICAI in the year 2002 to review the general financial statements and auditor's report thereon of certain companies and ensure compliance with the prescribed reporting requirements under the relevant statute governing the company.
6. Observations finalised between March 2011 and January 2017 have been considered.
7. Financial statements and the auditor's report thereon could be selected suo motto by FRRB or on a reference made to it by any regulatory body such as RBI, SEBI, etc. The FRRB may also review general purpose financial statements and the auditor's report thereon relating to which serious accounting irregularities have been highlighted by the media reports.

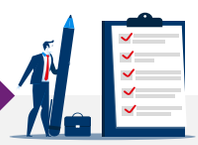
- **AS 3, *Cash Flow Statements***: A cash flow statement has not been prepared by a certain subsidiary of a listed company and also by a certain company which is in the process of listing (on the ground of being a small and medium sized company), when such companies are not exempt from preparation of cash flow statement under AS 3[8].
- **AS 14, *Accounting for Amalgamations:*** Systematic basis of amortising goodwill on amalgamation has not been followed.
- **AS 16, *Borrowing Costs***: In certain cases, cost of derivative transactions has been added to the cost of borrowings. Such cost does not qualify to be a borrowing cost as it is neither an ancillary cost incurred in connection with the arrangement of borrowings nor it is an exchange difference arising on the amount of principal of the foreign currency borrowings.
- **AS 17, *Segment Reporting:*** In certain cases, disclosure of the fact that there is only one business or geographical segment has not been made. Merely reporting that 'segment reporting as per AS 17 is not applicable' is not a sufficient disclosure as per AS 17.
- **AS 18, *Related Party Disclosures:*** In certain cases, there is a failure to disclose corporate guarantees given to banks/financial institutions for credit facilities extended to the subsidiaries and/or personal guarantees given by the directors for loans taken from banks/financial institutions as RPTs.
- **AS 21, *Consolidated Financial Statements:*** Fact that different policies have been adopted for subsidiaries (vis-à-vis parent) have been mentioned. However, companies have not mentioned proportion of the items in the CFS to which these different accounting policies have been applied. Additionally, such companies did not disclose the fact that it is not practicable to follow uniform accounting policies.

Compliance with Schedule II and III to the 2013 Act

- **Balance sheet and related notes:** Expenses on acquisition of intellectual property rights and licences for projects under development have been classified as capital work-in-progress instead of intangible assets under development.
- **Statement of profit and loss and related notes:** Exchange differences on foreign currency transactions and translation have been included in the cost of raw material consumed instead of presenting them separately.

For a detailed overview of the FRRB's observations, please refer to KPMG in India's First Notes dated 8 May 2018.

Key takeaways



The FRRB study has highlighted important areas to be considered while preparing and presenting the financial statements by companies. Similar observations were raised by the Quality Review Board (QRB) in its report dated 10 November 2017.

This implies that there is an urgent need for companies to evaluate whether the financial statements have been prepared in accordance with the prescribed accounting framework and are providing adequate disclosures.

It is important to note that in case of listed companies, the Quality Audit Report Review Committee (QARRC) of SEBI could refer to the FRRB, auditor's report of listed companies with modified opinion, where the impact of the modified opinion is significant and the explanation provided by the listed company seems unsatisfactory to QARRC.

8. AS 3 is not mandatory for small and medium sized companies. A small and medium sized company means a company:
   a) Whose equity or debt securities are not listed or are not in the process of listing on any stock exchange whether in India or outside India
   b) Which is not a bank, financial institution or an insurance company
   c) Whose turnover (excluding other income) does not exceed INR50 crore in the immediately preceding accounting year
   d) Which does not have borrowing (including public deposits) in excess of INR10 crore at any time during the immediately preceding accounting year and
   e) Which is not a holding or subsidiary company of a company which is not a small and medium sized company.

Key takeaways (cont.)

Accordingly, in case the FRRB opines that the:

- *Modified opinion is justified:* QARRC may recommend submission of revised pro-forma financial results, incorporating the effect of the modified opinion to the stock exchange(s) in the specified manner.
- *Modified opinion is not justified:* ICAI would take up the matter appropriately with the statutory auditor of the listed company.

However, in case the modified opinion is not quantifiable, QARRC could recommend rectification of such modified opinion in the subsequent FY.

(Source: Study on compliance of financial reporting requirements Volume – III issued by ICAI and KPMG in India's First Notes dated 8 May 2018)

ICAI publications relevant for the quarter ended 30 June 2018

Publications	Overview
Ind AS: An Overview (Revised 2018)	• Provides an overview of various aspects related to International Financial Reporting Standards (IFRS)-converged Ind AS such as road map for the applicability of Ind AS for corporates and for NBFCs, summary of all the Ind AS, etc. • Captures all the recent amendments to Ind AS notified by the MCA till March 2018.
Educational material on Ind AS 27, *Separate Financial Statements* and Ind AS 28, *Investment in Associates and Joint Ventures*	• Comprises summary of key requirements of Ind AS 27 and Ind AS 28 • Covers issues in the form of FAQs which are expected to be encountered frequently while implementing these standards.
Implementation guide on reporting standards	• This guide covers following SAs: – Revised SA 700, *Forming an Opinion and Reporting on Financial Statements* – Revised SA 705, *Modifications to the Opinion in the Independent Auditor's Report* and – Revised SA 706, *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*. • Revised standards are effective for audits of financial statements for periods beginning on or after 1 April 2018. • The implementation guide provides detailed guidance on various issues involved in the revised standards.
FAQs on SA 570 (revised), *Going Concern*	• SA 570 has been made applicable for audits of financial statements for periods beginning on or after 1 April 2017. • The FAQs provide guidance on implications of SA 570 (revised) on auditor's report and manner of reporting under SA 570 (revised).

(Source: ICAI announcements dated 1 May 2018, 21 May 2018 and 3 July 2018)

Expert Advisory Committee (EAC) opinions issued by ICAI during the quarter ended June 2018

Topic	Month
Amortisation of expenses incurred on various business requirements at the time of formation	April 2018
Provision for debtors transferred to franchisee	May 2018
Amortisation of goodwill in respect of subsidiaries and jointly controlled entities recognised as an asset in CFS (under Ind AS)	June 2018

(Source: The Chartered Accountant - ICAI journal for the month of April 2018, May 2018 and June 2018)

Glossary

2013 Act	The Companies Act, 2013
AFS	Available for Sale
AS	Accounting Standard
BoD	Board of Directors
CG	Central Government
EAC	Expert Advisory Committee
FAQs	Frequently Asked Questions
FCCB	Foreign Currency Convertible Bond
HFT	Held For Trade
HTM	Held to Maturity
ICAI	The Institute of Chartered Accountants of India
ICDR Regulations	SEBI (Issue of Capital and Disclosures Requirements) Regulations
IFR	Investment Fluctuation Reserve
IFRS	International Financial Reporting Standards
IRDAI	Insurance Regulatory and Development Authority of India
ITFG	Ind AS Transition Facilitation Group
Ind AS	Indian Accounting Standard
Ind VS	Indian Valuation Standard
Listing Regulations	SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
MCA	The Ministry of Corporate Affairs
NBFC	Non-Banking Financial Company
NCRPS	Non-Convertible Redeemable Preference Shares
RBI	The Reserve Bank of India
SA	Standard on Auditing
SEBI	The Securities and Exchange Board of India
QRB	Quality Review Board

Notes

KPMG in India's IFRS institute

Visit KPMG in India's IFRS institute - a web-based platform, which seeks to act as a wide-ranging site for information and updates on IFRS implementation in India.

The website provides information and resources to help board and audit committee members, executives, management, stakeholders and government representatives gain insight and access to thought leadership publications that are based on the evolving global financial reporting framework.

IFRS Notes

Financier Worldwide: A panel discussion on IFRS 16, *Leases*

4 June 2018

Recently, Financier Worldwide moderated a discussion on IFRS 16 between four experts of the Accounting Advisory Services (AAS) of the KPMG global network (Markus Kreher, Global Head of AAS, KPMG International; Sai Venkateshwaran, KPMG in India; Michelle Gibbs, KPMG in Australia; and Ruben Rog, KPMG in the Netherlands).

The insights of the discussion have been published in the form of an article in the June 2018 edition of Financier Worldwide. This issue provides the link to the article.

First Notes

MCA notified certain provisions of the Companies (Amendment) Act, 2017

28 May 2018

MCA through its notification dated 7 May 2018 notified certain sections of the Companies (Amendment) Act, 2017. Additionally, MCA issued amendment to certain rules under the Companies Act, 2013 (2013 Act). The notified provisions are effective from 7 May 2018.

This issue of First Notes aims to provide an overview of the recently notified sections of the Companies (Amendment) Act, 2017 and the amendments issued to the rules to the 2013 Act.

Accounting and Auditing Update

Issue no. 23 | June 2018

In this issue of the Accounting and Auditing Update (AAU), we focus on the impact of Ind AS 115, *Revenue Contracts with Customers* on the accounting of customer loyalty programmes. Ind AS 115 will change the way in which banks account for customer loyalty programmes. Banks provide various incentives to credit card holders as part of their marketing schemes.

The publication also carries an article on accounting treatment of liquidated damages under a contract. The article summarises the guidance that is available under Indian GAAP and also compares it with the Ind AS 115 guidance to explain how the accounting would be impacted under the new revenue standard.

The article on accounting of share warrants summarises the concept of equity and liability under Ind AS 32, *Financial Instruments: Presentation* and discusses certain practical issues such as anti-dilution features, contingent settlement provisions, reclassification of liability into equity, etc.

Our publication also carries a regular synopsis of some recent regulatory updates in India.

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