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Editorial

Companies cater to their financial needs in various forms including acceptance of deposits from members or public. Stringent provisions are laid down under the Companies Act, 2013 for acceptance of deposits by a company. On the other hand, companies are also required to make certain payments under various laws and regulations such as provident fund, income-tax, etc. to the concerned regulatory authorities within the timelines prescribed. In order to ensure how far the companies are compliant with the respective laws and regulations, Companies (Auditor's report) Order 2020 has introduced enhanced reporting requirements with respect to deposits accepted by companies and payment of statutory dues. In this edition of Accounting and Auditing Update (AAU), we aim to discuss these reporting requirements along with highlighting the related guidance provided by the Institute of Chartered Accountants of India (ICAI).

Climate change is rapidly emerging as a threat to the stability of the financial systems across the globe. Therefore, there is an increase in demand for decision-useful, climate related information by a range of participants in the financial markets, particularly by the investors. To address the concern, internationally, in 2015, the Financial Stability Board (FSB) formed the Task Force on Climate-related Financial Disclosures (TCFD) to help investors understand their financial exposure to climate risk and help companies disclose this information in a clear and consistent way. With this objective, in 2017, the TCFD issued a report with its recommendations which focus specifically on business disclosure of how climate change affects financial performance now and in the future. The topic has been continuously discussed in various other forums including the International Accounting Standards Board (IASB) and the International Auditing and Assurance Standards Board (IAASB). Our article on the topic discusses in detail the financial impacts of climate related issues along with recommended financial disclosures to be considered by companies.

The economic fallout on account of the COVID-19 pandemic has led to significant financial stress for borrowers across the board. The resultant stress can potentially impact the long-term viability of many firms, otherwise having a good track record, due to their debt burden becoming disproportionate relative to their cash flow generation abilities. Therefore, in order to preserve the soundness of the Indian banking sector and mitigate risks to financial stability, the Reserve Bank of India (RBI) has introduced a 'Resolution Framework for COVID-19-related Stress' (the framework) in August 2020. The framework aims to enable lenders to implement a resolution plan in respect of eligible corporate exposures without change in ownership and personal loans, while classifying such exposures as standard, subject to specified conditions. Recently, RBI has issued certain clarifications to ease the implementation of the framework by the lenders. Our article summarises the key clarifications provided by RBI.

As is the case each month, we have also included a regular round-up of some recent regulatory updates in India.

We would be delighted to receive feedback/ suggestions from you on the topics we should cover in the forthcoming editions of AAU.

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CARO 2020: Acceptance of deposits and payment of statutory dues

This article aims to:

- Discuss the reporting requirements of CARO 2020 relating to acceptance of deposits and payment of statutory dues by a company along with highlighting the related guidance provided by ICAI.

Introduction

The Companies (Auditor's Report) Order, 2020 (CARO 2020) has introduced enhanced reporting requirements for auditors of specified companies. The aim of reporting requirements is to highlight critical areas involved with the operations of the companies and also showcasing how far the companies are compliant with the respective laws and regulations.

Companies cater to their financial needs in various forms, such as raising capital through issuance of shares/ debentures, acquiring funds from lending institutions, etc. An alternate mode through which companies fulfil their financial needs is through acceptance of deposits from members or public. Stringent provisions are laid down under the Companies Act, 2013 (2013 Act) with respect to acceptance of deposits by a company. With a view to ensure whether these provisions are followed in spirit by the companies, CARO 2020 requires the auditors to report on the compliances met by companies vis-à-vis deposits accepted by them.

Companies are also obliged to make certain payments under various laws and regulations such as sales-tax, Tax Deducted at Source (TDS), Provident Fund (PF), income-tax, duty of customs, etc. These amounts are to be deposited with the concerned regulatory authorities within the timelines prescribed. Delay or non-payment of such dues attracts penal provisions. Therefore, companies need to ensure that these are paid in a timely manner. Non-compliances of certain provisions are also required to be reported in the auditors' report.

In this article, we aim to cast our lens on the requirements of CARO 2020 related to acceptance of deposits and payment of statutory dues by a company along with highlighting the key considerations as stipulated in the guidance note on CARO 2020 (guidance note) issued by the Institute of Chartered Accountants of India (ICAI).

Acceptance of deposits by a company

CARO 2020 has modified the reporting requirement relating to acceptance of deposits by a company vis-à-vis CARO 2016 and includes reporting on 'amounts which are deemed to be deposits'. As per the revised clause, an auditor is required to report whether the directives issued by the Reserve Bank of India (RBI) and the provisions of Sections 73 to 76 or any other relevant provisions of the 2013 Act and the rules made thereunder, where applicable, have been complied with, in respect of deposits accepted by the company or **amounts which are deemed to be deposits.** If there are contraventions, then an auditor is required to report the nature of such contraventions.

Also, if an order has been passed by Company Law Board (CLB), National Company Law Tribunal (NCLT), RBI, any court or any other tribunal, an auditor would need to evaluate whether the same has been complied with or not.

(Emphasis added to highlight the addition made by CARO 2020 vis-à-vis CARO 2016)

Applicability of provisions of the 2013 Act

The deposit related provisions under the 2013 Act are applicable to the following classes of companies:

- A company that accepts deposits from its members. Such a company has to pass a resolution in its general meeting according to the Rules prescribed and subject to the fulfilment of the specified conditions (Section 73(2))
- A company that is eligible to accept deposits from the public (Section 76) (i.e. eligible company[1] as defined under the Companies (Acceptance of Deposits) Rules, 2014 (Deposits Rules)).

However, certain companies are exempted from the deposit related provisions and they are as follows:

- A banking company
- A Non-Banking Financial Company (NBFC)
- A housing finance company
- A company as may be specified by the Central Government (CG) after consultation with the Reserve Bank of India (RBI).

1. An eligible company means a public company fulfilling the following conditions:
   a. Net worth of not less than INR100 crore or a turnover of not less than INR500 crore
   b. Obtained prior consent of the company in the general meeting by means of a special resolution*, and
   c. Filed the said resolution with the ROC before making any invitation to the public for acceptance of deposits.

*(*In case, deposit is with respect to the limits specified under Section 180(1)(c) of the 2013 Act, an ordinary resolution may suffice the requirement.)*

Definition of term 'deposits' and 'amount deemed to be deposits'

Section 2(31) of the 2013 Act defines 'deposit' to include any receipt of money by way of deposit or loan or in any other form by a company but does not include such categories of amount as may be prescribed in consultation with the RBI. Further, the Deposits Rules provide various categories and items that are excluded from the definition of deposits.

Some of the significant items which are not to be categorised as deposits except in specific situations where they can be classified as *deemed deposits* are as follows:

- **Receipt of amount towards subscription of securities in certain situations:** An amount received towards subscription of securities would not be treated as a deposit except in the following situations:

  a. The securities against which amount has been received could not be allotted within 60 days from the date of receipt of the application money, or

  b. Advance for such securities and application money or advance has not been refunded to the subscribers within 15 days from the date of completion of 60 days.

  As per the guidance note, the above receipts of amount (point (a) and (b)) would be considered as *deemed deposits.*

- **Receipt of amount for the purpose of business:** Any amount received in the course of, or for the purposes of, the business of the company would not be treated as a deposit. For example, amount received as:

  a. An advance for the supply of goods or provision of services provided that such an advance is appropriated against supply of goods or provision of services within a period of 365 days from the date of acceptance of such advance

  b. An advance received in connection with consideration for an immovable property under an agreement/arrangement, provided that such advance is adjusted against such property in accordance with the terms of the agreement/arrangement

  c. An advance received under long-term projects for supply of capital goods except those covered under (b) above

  d. Security deposit for the performance of the contract for supply of goods or provision of services

  e. An advance towards consideration for providing future services in the form of a warranty or maintenance contract as per the written agreement/arrangement, if the period for providing such services does not exceed the period prevalent as per common business practice, or five years from the date of acceptance of such service, whichever is less.

  However, above amounts would be *deemed to be deposits* on the expiry of 15 days from the date they become due for refund.

  If an amount (given in point (a), (b) and (c) above) become refundable (with or without interest) due to the reasons that the company accepting the money does not have necessary permission or approval, wherever required, to deal in the goods or properties or services for which the money was taken, then the amount received would be *deemed to be a deposit.*

Conditions for acceptance of deposits

A company (including an eligible company) intending to invite deposits is required to comply with certain conditions while accepting deposits. These, *inter alia,* includes:

- **Maintenance of liquid assets:** On or before 30 April of each year, an amount not less than 20 per cent of the amount of deposits maturing during the following Financial Year (FY) should be kept in a scheduled bank (in a separate bank account) to be called as 'deposit repayment reserve account.'

  Such a reserve should be used only for the purpose of repayment of deposits.

- **Credit rating**

  – *Eligible company:* Every eligible company is required to obtain at least once in a year, a credit rating for deposits accepted by it and the copy of such rating should be sent to the ROC along with the return of deposits in Form DPT-3.

    Such a credit rating should not be below the minimum investment grade rating or other specified credit rating for fixed deposits from any one of the approved credit rating agencies (as specified for NBFCs).

  – *Company covered under Section 73(2):* Company taking deposits from its members also needs to provide credit rating obtained in the circular issued to its members.

- **Repayment of deposits:** A company should not default in the repayment of the deposit (or interest thereon) accepted before or after the commencement of the 2013 Act. Companies which have made good on a default committed in the past are allowed to accept deposits after five years from the date of default remediation.

Other considerations

- **Permissible amount of deposits:** The 2013 Act along with the Deposits Rules, prescribes the following limits for acceptance of deposits from members and the public:
  - *Eligible company (excluding government company):* An eligible company is allowed to accept deposits up to 10 per cent of the aggregate of its paid-up share capital, free reserves and securities premium account from its members.

    In case of any other deposits, deposits of up to 35 per cent of the aggregate of the paid-up share capital, free reserves and securities premium account are permitted.
  - *Other company (i.e. public company which is not an eligible company and private company):* Such other company is allowed to accept deposits up to 35 per cent of its paid-up share capital, free reserves and securities premium account from its members.
  - *Private company:* A private company is allowed to accept deposits up to 100 per cent of the aggregate of its paid-up share capital, free reserves and securities premium account from its members and does not have to comply with the conditions specified under Section 73(2) of the 2013 Act. It has to file details of monies so accepted with ROC in Form DPT-3.
- **Disclosures:** Following disclosures are required:

  a. Return of deposits: Every company is required to file with the ROC a return of deposits (comprising information contained therein as on 31 March of that year duly audited by the auditor of the company) in Form DPT-3, on or before 30 June of every year along with the specified fees. Form DPT-3 (return of deposits) should be used for filing:

  i. A return of deposit

  ii. Particulars of a transaction not considered as deposit or

  iii. Both.

  This form has to be filed by every company, other than a government company.

  b. Disclosure in financial statements: Every company is required to disclose the amount received from the director (also relatives of directors in case of a private company) in the notes to the financial statements.

Guidance by ICAI

The guidance note requires reporting on compliance by the company with regard to all matters specified in Sections 73 to 76 of the 2013 Act by an auditor. In case of companies with large number of deposits, an auditor would examine the system by which deposits are accepted and records are maintained by the company. With respect to assessment of amounts which could be deemed to be deposits, companies should maintain a list of amounts received in the course of, or for the purposes of, the business of the company (for instance, advances and security deposits) for an auditor to verify. Further, an auditor would examine the efficacy of the internal controls instituted by the company to evaluate that the deposits accepted by the company remain within the limits.

In addition to commenting on the compliance with the provisions of the 2013 Act relating to deposits accepted by a company, an auditor is required to report on compliance with any order, if issued by the CLB, NCLT, RBI, any court or any other tribunal in response to contravention of provisions relating to deposits or any other relevant provisions of the 2013 Act and the rules thereunder. Accordingly, companies would need to inform about all such instances along with the steps taken to comply with those orders to an auditor. In case of non-compliance with the order issued by CLB, NCLT, RBI, any court, or any other tribunal, the fact would be reported along with the nature of contravention in the auditor's report.

Payment of statutory dues

Another reporting requirement that has been modified by CARO 2020 vis-à-vis CARO 2016 relates to payment of statutory dues by a company. As per the revised clause, an auditor is required to report on the regularity of payment of the company in depositing undisputed statutory dues including **Goods and Services Tax (GST),** provident fund, employees' state insurance, income-tax, sales-tax, service tax, duty of custom, duty of excise, value added tax, cess and any other statutory dues to appropriate authorities.

If the company is not regular in depositing the stated undisputed statutory dues, then an auditor is further required to state the extent of arrears of statutory dues which have remained outstanding as at the last day of the financial year concerned for a period of more than six months from the date they became payable.

(Emphasis added to highlight the addition made by CARO 2020)

Additionally, in case the above-mentioned statutory dues have not been deposited on account of any dispute, then an auditor is required to report the amounts involved and the forum where dispute is pending. Under CARO 2016, this reporting was restricted to non-payment of income-tax, sales-tax, service-tax, duty of customs, duty of excise and value added tax on account of any dispute.

It is to be noted that mere representation to the concerned department would not be treated as a dispute for the purpose of reporting under this clause.

Guidance by ICAI

Regularity of payment of statutory dues

As per the guidance note, the term 'any other statutory dues' would cover all types of dues under various statues which may be applicable to a company having regard to its nature of business. Therefore, an auditor would be required to comment on the regularity of the company in depositing any other statutory dues payable by the company to appropriate authorities as per the statutes applicable to the company, in addition to the ones specifically listed under the clause.

As the intent of reporting is to ascertain how regular the company is in depositing statutory dues with the appropriate authorities, the scope of reporting would be limited to cover only those statutory dues which the company is required to deposit regularly to an authority under a statue. Consequently, the reporting would not cover those amounts which may be levied by an appropriate authority from time to time upon occurrence or non-occurrence of certain events and therefore, are not required to be paid regularly. Following are examples of dues which will not be classified as statutory dues for the purpose of reporting under this clause:

a. Any sum payable to an electricity company as electricity bill as the due has arisen on account of supply of goods or services between the parties.

b. Dividend payment to shareholders under the 2013 Act as the same is on account of contractual obligation with the shareholders.

   However, dividend declared and not paid to the shareholders within specified time limit and which is required to be transferred to a specified fund would be considered as a statutory due.

c. Bonus to an employee

d. Any sum payable to public sector undertakings, despite the fact that such undertakings are incorporated, owned and operated by the state government/CG.

It is to be noted that any dues recoverable as arrears of land revenue by the concerned authority would be treated as a statutory due.

Further, while assessing the regularity of payment, due consideration needs to be given to the nature of the statutory dues. With respect to some of the dues such as PF, GST, etc., regularity could be a normal feature as companies are required to deposit the money with appropriate authorities on a monthly or quarterly basis. However, in case of other dues such as duty of custom on import of goods, demands arising on account of assessment orders, etc., wherein a company is required to pay as and when an event giving rise to the liability of the company occurs, payments would be considered regular if the company deposits them as and when they occur. Though, reporting would cover regularity of the company in depositing the installments, if any, granted by an authority in respect of a demand against the company.

Accordingly, non-payment of advance income-tax and non-deduction of TDS would constitute default in payment of statutory dues. Erroneous adjustments of one category of GST credit with other category without appropriately applying the prevailing laws would also be considered as default in payment to be reported.

Period of default and amounts payable

Reporting under this clause would cover all such cases where the company has been in default in depositing the statutory dues anytime during the year, irrespective of the fact that there are no arrears on the balance sheet date.

For the purpose of reporting, statutory dues would be considered as payable:

- As at the date of the expiry of the stay granted by the authorities or
- Where installments have been granted for the payment of statutory dues, the date on which the default occurs, and the amount becomes payable to the authorities.

Reporting would be restricted to actual arrears and would not include the amounts which have not fallen due for payment to appropriate authority and have been recognised as outstanding dues at the balance sheet date. However, penalty and/or interest levied under the respective laws would be covered within the term 'amounts payable'.

As per the guidance note, while indicating the arrears, the period to which the arrears relate should preferably be given and further, wherever possible, the fact of subsequent clearance or otherwise may also be indicated by an auditor in its report.

Disputed statutory dues

In case of non-payment of any statutory due on account of any dispute, an auditor is required to state the amounts involved irrespective of the treatment of such disputed amounts in books of accounts along with the forum where the dispute is pending. The reporting would cover minor amounts as well.

As per the guidance note, a matter would be considered as 'disputed', where there is a positive evidence or action on the part of the company to show that it has not accepted the demand for payment of tax or duty, e.g., where the company has gone into an appeal. Further, in case the demand notice/intimation for the payment of a statutory due is for a certain amount and the dispute relates only to a part and not the whole of such amount, then only that part of amount would be treated as disputed. Balance amount would be regarded as undisputed.

Issuance of a show cause notice by the concerned department should not be construed to be demand payable by a company. Though, tax demands which have been stayed by the relevant authority would be regarded as disputed dues. Further, in cases where the appellate authority has decided a case in favour of a company, but the department may prefer to make an appeal to a higher authority, there will be no dispute until the time the department makes an appeal to the relevant appellate authority. In case where amount under dispute is pending for an appeal to be filed and the time limit for filing the appeal has lapsed, then the disputed amount would become a statutory due.

Conclusion

To facilitate reporting, companies may need to maintain a list of various statutes under which they are required to make payments regularly to appropriate authorities, the kind of payments under each statute, the due date for making the payment to the appropriate authority, the date on which the payment is made by the company, the arrears not due and the arrears overdue for more than six months along with the underlying documents for an auditor to verify and report accordingly.

Also, companies may need to maintain adequate system to identify amounts which may be considered as deemed deposits under the 2013 Act and consequently, would need to ensure compliances with the provisions of the 2013 Act with respect to such deposits.

2 Climate change: Potential financial impacts and related disclosures

This article aims to:

– Discuss potential financial impacts associated with climate change and related disclosures to be made by companies.

Introduction

Climate change is rapidly emerging as a threat to the stability of the financial systems across the globe. More frequent and severe weather events are damaging infrastructure and disrupting supply chains. Transition to a lower carbon economy and new emission standards are expected to bring new policies, regulations and rapid changes to market dynamics. The automotive industry in India, for instance, is required to transition to Bharat Stage (BS) -VI emission standards with effect from 1 April 2020. Together these trends are likely to impose financial risks on companies and other stakeholders including investors, lenders and insurers.

There is an increase in demand for decision-useful, climate related information by a range of participants in the financial markets. Inadequate information about financial risks due to climate change can lead to mispricing of assets, misallocation of capital and can potentially give rise to concerns about financial stability since markets can be vulnerable to abrupt corrections.

Addressing the challenge, internationally, in 2015, the Financial Stability Board (FSB)[1] formed the Task Force on Climate-related Financial Disclosures (TCFD) to help investors understand their financial exposure to climate risk and help companies disclose this information in a clear and consistent way.

In 2017, the TCFD issued a report with its recommendations which focus specifically on business disclosure of how climate change affects financial performance now and in the future. They do not address disclosure of how a company may, or may not, be contributing to climate change.

In November 2019 - In Brief Nick Anderson, member of the International Accounting Standards Board (IASB) through an article on 'IFRS Standards and climate-related disclosures' has explained how existing requirements within International Financial Reporting Standards (IFRS) relate to climate change risks and other emerging risks. The article highlights how the principle-based approach of IFRS would help address disclosures regarding climate change and other emerging risks even though such risks are not explicitly referenced in the standards. Additionally, in October 2020, the International Auditing and Assurance Standards Board (IAASB) has issued a guidance material on consideration of climate-related risks in an audit of financial statements.

In this article, we aim to discuss in detail the financial impacts of climate related issues along with recommended financial disclosures to be considered by companies.

Financial impacts of climate related risks and opportunities

The financial impacts of climate-related issues on companies are not always clear or direct. For many companies, challenge would lie in identifying the issues, assessing potential impacts and ensuring that material issues are reflected in their financial statements. This could be on account of:

- Limited knowledge of climate-related issues within companies
- Tendency to focus mainly on near-term risks without paying adequate attention to risks that may arise in the longer term and
- Difficulty in quantifying the financial effects of climate-related issues.

In order to make informed decisions, it becomes imperative to understand how climate-related risks and opportunities are likely to impact a company's future financial position as reflected in its income statement, cash flow statement and balance sheet.

1. FSB is an international body that monitors and makes recommendations about the global financial system.

Climate-related risks

Climate related risks can be categorised into:

- **Transition risks:** Risks that arise due to changes in legislation, market forces or technological changes on transition to a lower-carbon economy and other regulatory standards. Some of the examples of transition related risks are as follows:

  Policy and legal risks

  – Carbon pricing and reporting obligations

  – Mandates on and regulation of existing products and services

  – Exposure to litigation.

  Technology risks

  – Substitution of existing products and services with lower emissions options

  – Unsuccessful investment in new technologies.

Market risks

– Changing customer behaviour

– Uncertainty in market signals

– Increased cost of raw materials.

Reputation risks

– Shift in consumer preferences

– Increased stakeholder concern/negative feedback

– Stigmatisation of sector.

- **Physical risks:** Risks that arise as a direct result of changes in weather and climate. Physical risks resulting from climate change can be event driven (acute) or longer-term shifts (chronic) in climate patterns. Some of the examples of physical risks are as follows:

Acute risks

– Increased severity of extreme weather events such as cyclones and floods.

Chronic risks

– Changes in precipitation patterns and extreme variability in weather patterns

– Rising mean temperatures

– Rising sea levels.

Climate-related opportunities

Efforts to mitigate and adapt to climate change could also produce opportunities for companies. For instance, resource efficiency and cost savings, adoption of low-emission energy sources, development of new products and services, access to new markets and building resilience along the supply chain.

Climate related financial disclosures

Climate-related risk is a non-diversifiable risk that is expected to affect every sector. The TCFD identifies the following types of companies that are likely to be affected by climate-related risks:

- Companies in the financial sector such as, banks, insurance groups, asset owners (investment companies), and asset managers and
- Companies in non-financial industries, such as, energy, transportation, material and buildings and agriculture, foods and forest products.

As a result, stakeholders would require adequate information to understand the impact and the steps taken by companies to address those risks.

In order to facilitate transparency regarding the climate related issues faced and addressed by companies, there is an increasing need of providing adequate climate related disclosures in the company's accounts and/or other reports.

Basis above, the TCFD structured its recommendations around four thematic areas that represent core elements of how companies operate. The recommendations were supported by specific disclosures which companies should include in financial filings or other reports to provide decision-useful information to investors and other stakeholders.

Following figure provides the core elements of climate-related disclosures as recommended by the TCFD in its report:

Governance

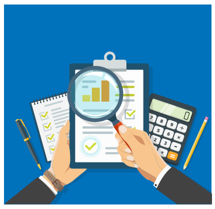
Company's governance around climate-related risks and opportunities.

Strategy

The actual and potential impacts of climate-related risks and opportunities on the company's businesses, strategy and financial planning.

Risk management

The processes used by the company to identify, assess and manage climate-related risks.



Metrics and targets

The metrics and targets used to assess and manage relevant climate-related risks and opportunities.

The recommended disclosures under each of the above elements are as follows:

Governance

- Describe the board's oversight of climate-related risks and opportunities.
- Describe management's role in assessing and managing climate-related risks and opportunities.

Strategy

- Describe the climate-related risks and opportunities the company has identified over the short, medium and long term.
- Describe the impact of climate-related risks and opportunities on the company's business, strategy and financial planning.
- Describe the resilience of the company's strategy, taking into consideration different climate-related scenarios.

Risk management

- Describe the company's processes for identifying, assessing and managing climate-related risks.
- Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the company's overall risk management.

Metrics and targets

- Disclose the metrics used by the company to assess climate-related risks and opportunities in line with its strategy and risk management process.
- Describe the targets used by the company to manage climate-related risks and opportunities and performance against targets.

(**Source:** TCFD report issued in June 2017)

Disclosures in financial statements

Currently there is no mandatory international framework for reporting climate-related risks. However, IAASB in its guidance material *'Consideration of Climate-Related Risks in an Audit of Financial Statement'* highlighted that there is a growing support for climate-related financial reporting, generally within the financial statements or associated with the other information.

These risks would be instrumental in the decision-making of investors. Therefore, companies may need to consider climate related risks in the context of their financial statements rather than solely as a matter of corporate social responsibility reporting or sustainability reporting. Companies should consider the following while preparing their financial statements:

- Whether investors could reasonably expect that emerging risks, including climate-related risks, could affect the amounts and disclosures reported in the financial statements. Investors have indicated the importance of information about such risks to their decision-making; and
- What information about the effect of emerging risks, including climate-related risks, on the assumptions made in preparing the financial statements is material, and thus should be disclosed.

Some of the potential financial implications arising from climate-related and other emerging risks may include, but are not limited to:

- Asset impairment, including goodwill
- Changes in the useful life of assets
- Changes in the fair valuation of assets
- Effects on impairment calculations because of increased costs or reduced demand
- Changes in provisions for onerous contracts because of increased costs or reduced demand
- Changes in provisions and contingent liabilities arising from fines and penalties and
- Changes in expected credit losses for loans and other financial assets.

Companies would need to consider the relevant requirements of IFRS/Ind AS and would need to make adequate disclosures to address these implications.

The majority of climate-related information is currently disclosed within management commentary and not in the financial statements. As per November 2019 In Brief, applying materiality definition and principles in the materiality practice statements, would result in some of this information being reflected within the financial statements. The disclosures in the notes will be most helpful to users of financial statements if the disclosures focus on specific issues and assumptions made that are relevant to the amounts recognised in the financial statements; and if they are not of a boilerplate nature.

It is important to note that disclosures in other documents (including presentations, management commentary and sustainability reports) will not compensate for the omission of disclosures that are required to be made in the financial statements and are therefore, subject to audit in most jurisdictions. Therefore, management should report on environmental and societal issues to the extent necessary for primary users of financial statements to form their own assessment of the company's longer-term prospects and management's stewardship of the business.

Auditor's responsibility

If climate change impacts an entity, then the auditor needs to consider whether the financial statements appropriately reflect this in accordance with the applicable financial reporting framework (i.e., in the context of risks of material misstatement related to amounts and disclosures that may be affected depending on the fact and circumstances of the entity). Auditors also need to understand how climate-related risks relate to their responsibilities under professional standards, and applicable law and regulation.

In India, the Securities and Exchange Board of India (SEBI) requires top 1,000 listed companies to provide a Business Responsibility Report (BRR) as part of their annual reports. In the report, companies are required to describe the initiatives taken by them from an environmental, social and governance perspective. The current version of BRR is based on the business responsibility and sustainability indicators contained in the National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business (NVGs) issued in 2011 by the Ministry of Corporate Affairs (MCA). These guidelines were updated as the National Guidelines for Responsible Business Conduct (NGRBC) in 2019.

Companies are specifically required to comment on their strategies/initiatives to address global environmental issues such as climate change, global warming, etc. in the report.

Recently, SEBI has issued a consultation paper and proposed a new format of reporting, namely, Business Responsibility and Sustainability Reporting (BRSR). SEBI recommended that the new format for BRSR should be made applicable to top 1,000 listed companies by market capitalisation mandatorily from the financial year 2021-22. The new format also requires specific disclosures on strategies/initiatives to address global environmental issues such as climate change, resource scarcity, health pandemics and emergencies, natural disasters, etc.

Additionally, SEBI requires top 500 listed companies to adopt Integrated Reporting (<IR>) on a voluntary basis from the financial year 2017-2018.

The information related to IR may be provided in the following ways:

- As part of annual report with a separate section on IR
- Incorporating in management discussion and analysis, or
- By preparing a separate report (annual report prepared as per IR framework).

In case the company has already provided the relevant information in any other report prepared in accordance with national/international requirement/ framework, it may provide appropriate reference to the same in its integrated report so as to avoid duplication of information. Companies may host the integrated report on their website and provide appropriate reference to the same in their annual report.

The intent of both the reports is almost similar i.e. responsible and better business reporting. SEBI prescribed a format for BRR/BRSR, whereas the IR does not contain any prescribed format for reporting.

Companies may use these reports to disclose their commitment to and performance against their economic, social and environment impacts including climate change.

Next steps

There could be innumerable challenges associated with measuring the impact of climate change. Companies would need to adopt appropriate measures to address the financial risks and opportunities related to climate change. More guidance in this area is expected to emerge in near future.

(**Source:** 'TCFD – Overview publication' issued by TCFD, Recommendations of the TCFD- Final Report issued by TCFD in June 2017, Staff Audit Practice Alert on 'The Consideration of Climate-Related Risks in an Audit of Financial Statement' issued by IAASB in October 2020, Article on 'IFRS® Standards and climate-related disclosures' dated 28 November 2019 on IASB website)

3 Clarifications on the Resolution Framework for COVID-19 related stressed assets

This article aims to:

– Summarise the clarifications provided by RBI regarding the Resolution Framework.

Background

To help preserve the soundness of the Indian banking sector and mitigate risks to financial stability, on 6 August 2020, the Reserve Bank of India (RBI) had notified the Resolution Framework for COVID-19 related stress (Resolution Framework). The Resolution Framework is a special window under the RBI (Prudential Framework for Resolution of Stressed Assets) Directions, 2019, issued in June 2019 (Prudential Framework), which enables resolution of accounts under stress on account of COVID-19, without adversely affecting the asset classification of these accounts.

The Resolution Framework has guidance on following two sections:

Resolution of stress in personal loans

Resolution of stress in 'Other Exposures'

On 14 October 2020, RBI issued 17 Frequently Asked Questions (FAQs) which provide clarification on various aspects of the Resolution Framework.

This article provides a summary of the clarifications provided by RBI.

Summary of the clarifications

The FAQs issued by RBI provide clarification on the following aspects of the Resolution Framework:

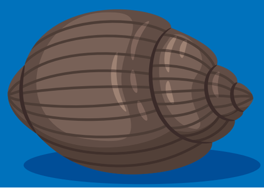
I. Eligible borrowers and eligibility criteria for the Resolution Framework

The Resolution Framework is applicable to personal loans and other exposures which have stress on account of COVID-19. Eligibility criteria for these loans/credit facilities to apply Resolution Framework has been specified in the framework. Exposures which do not fulfil the required eligibility conditions, would continue to be resolved under the Prudential Framework, or the relevant instructions applicable to specific category of lending institutions.

Clarifications

Following are the clarifications relating to eligibility of loans and their classification as personal loans/ other exposures:

- The Resolution Framework may be invoked for resolution of all exposures of lending institutions to eligible borrowers including investment exposures (such as corporate bonds, commercial papers, etc.). However, the Resolution Framework is without prejudice to all applicable guidelines issued by the relevant financial sector regulators and other Departments of the RBI in respect of any particular exposure. *(Clarification no. 7).*
- For entities/exposures (including investment exposures) that are undergoing COVID-19 related stress and meet the eligibility criteria prescribed in the Resolution Framework, only the Resolution Framework can be used for resolving that stress. For all other borrowers, the RBI's extant instructions[1] as otherwise applicable would be applicable. *(Clarification no. 4).*
- Personal loans are defined (in RBI circular DBR. No.BP.BC.99/08.13.100/2017-18) as loans given to individuals, which consist of consumer credit, education loan, loans given for creation/ enhancement of immovable assets and loans given for investment in financial assets. Accordingly, loans against property, which are used for business purposes or loans to individuals, where non-individuals have been considered as co-borrowers would not qualify as personal loans. In such cases, the resolution of eligible borrowers may be undertaken under the Resolution Framework for 'Other Exposures'. *(Clarification no. 17)*



1. Paragraph 2(1)(zc)(ii) of the Master Circular – The Housing Finance companies (NHB) Directions, 2010 for housing finance companies, and Paragraph 2.2.7.21 of the Master Circular- Income Recognition, Asset Classification, Provisioning and Other Related Matters – UCBs dated 1 July 2015 for Urban Co-operative Banks.

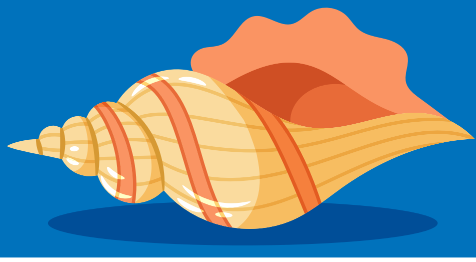
The circular specifies six categories of borrowers/ credit facilities which would not be eligible for resolution under the Resolution framework. These include:

- MSME borrowers whose aggregate exposure to lending institutions is INR25 crore or less as on 1 March 2020
- Farm credit (as defined in master directions issued by RBI on priority sector lending)[2]
- Loans to specific organisations, which would be on-lending for agricultural purposes
- Financial service providers
- Government bodies
- Exposures of Housing Finance Companies (HFCs) which have been rescheduled under the Master Circular - The Housing Finance Companies (NHB) Directions, 2010 after 1 March 2020.

Clarifications

Clarifications that delineate the applicability of the Resolution Framework are as follows:

- Effective 1 July 2020, the definition of MSME has been revised. For the purpose of assessing eligibility under the Resolution Framework, the definition of MSME that existed as on 1 March 2020 (i.e. the old definition) would apply. *(Clarificaition no. 14)*
- All farm credit exposures (as defined in the master circular on priority sector lending) of all lending institutions, except for loans to allied activities are excluded from the scope of the Resolution Framework. However, loans given to farmer households would be eligible for resolution under this Resolution Framework, provided they do not meet any other conditions for exclusions specified in the Resolution Framework. *(Clarificaiton no. 2)*
- All loans that meet the eligibility criteria, unless specifically excluded from the Resoultion Framework, would fall within the purview of the Resolution Framework. Loans that fall within the definition of 'personal loans' would be resolved as per criteria laid down in the Resolution Framework, even if they are not explicitly classified as such in any regulatory/supervisory reporting. In other cases, they would be resolved as per the criteria of 'other exposures' in the Resolution Framework. *(Clarification no. 5)*



The Resolution Framework sets out 1 March 2020 as the reference date for the purpose of assessing whether loans meet the eligibility conditions prescribed thereunder. Additionally, for the loans to be eligible under this framework, they should be classified as a standard asset as on the reference date, and they should not be in default for more than 30 days. However, it is not clear if 1 March 2020 would be considered as the reference date for the outstanding amount of debt too.

Clarifications

The clause mentioning the reference date of 1 March 2020 in the Resolution Framework is a general clause regarding the date on which the eligibility criteria for resolution under the Resolution Framework may be assessed. Therefore, the actual debt that would be considered for resolution would be the outstanding amount as on the date of invocation. *(Clarification no. 1)*

In certain cases, exposures that did not meet the eligibility criteria as on 1 March 2020 (e.g. a loan account was more than 30 DPD on 1 March 2020), and subsequently met the eligibility criteria (i.e. post the reference date). In such cases, those exposures cannot be resolved under the Resolution Framework but may be resolved under the Prudential Framework or other extant guidelines. *(Clarification no. 16)*

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2. Para 6.1 of the Master Directions on priority sector lending (Master Direction FIDD.CO.Plan.1/04.09.01/2016-17 dated July 7, 2016 (as updated)) defines farm credit as:
   A. Loans to individual farmers (including Self Help Groups (SHGs) or Joint Liability Groups (JLG)) and proprietorship of farmers, directly engaged in agriculture and allied activities
   B. Loans to corporate farmers, farmers' producer organisations/ companies of individual farmers, partnership firms and co-operatives of farmers directly engaged in agriculture and allied activities (allied activities would be upto a specified limit).

   Allied activities include dairy, fishery, animal husbandry, poultry, bee-keeping and sericulture.

II. Invocation and Implementation of the resolution plan

The circular requires all resolution plans under the Resolution Framework to be invoked by 31 December 2020. Further, it provides 90 days for implementation of the plan for personal loans, and 180 days for implementation of plans for other exposures.

Clarifications

Following are the clarifications:

- Date of invocation has been defined in the circular as the date when both the borrower and the lender (requisite lenders in case of multiple lenders) have agreed to proceed with a resolution plan under the Resolution Framework.
- For personal loans, the resolution plan would be deemed to have been implemented when the documentation is in place, changes in terms and conditions of the loans is reflected in the lenders' books, and the borrower is not in default with the lending institution as per the revised terms.
- A resolution plan for other exposures would have a similar meaning as prescribed in the Prudential Framework. Accordingly, resolution plans for other exposures would be deemed to have been implemented when:
  - *Resolution plans involving restructuring/ change in ownership:* When documentation is in place, changes in terms of conditions of the loans is reflected in the lenders' books, and the borrower is not in default with the lending institution
  - *Resolution plans not involving restructuring/ change in ownership:* When the borrower is not in default with any of the lenders as on the 180th day from end of review period
  - *Resolution plan where lenders exit the exposure by assignment/recovery:* When exposure to the borrower is fully extinguished. *(Clarification no. 6)*

III. Features of the resolution plan

The circular prescribes some of the features of the resolution plan which may include restructuring (excluding compromise settlements), change in ownership, extension of the loan, provision of a moratorium of a maximum of two years, etc. However, the circular is silent on whether resolution plans involving deferment of Date of Commencement of Commercial Operations (DCCO) in respect of projects under implementation can be implemented under the Resolution Framework.

Clarification

The restructuring in respect of projects under implementation involving deferment of DCCO are excluded from the scope of the Resolution Framework. The extant regulations contained in Paragraph 4.2.15 of DBR.No.BP. BC.2/21.04.048/2015-16 dated 1 July 2015, DOR.No.BP.BC.33/21.04.048/2019-20 dated 7 February 2020 and the other relevant instructions as applicable to specific category of lending institutions, already permit revisions of the DCCO and consequential shift in repayment schedule without being treated as restructuring subject to a maximum of four years in the case of infrastructure projects and a maximum of two years in the case of non-infrastructure projects (including commercial real estate exposures). In addition to the above, DCCO of projects may be extended by a further two years in case of change in ownership subject to the conditions specified in the above instructions. *(Clarification no. 11)*

IV. Specific aspects relating to resolution of other exposures

The Resolution Framework prescribes various requirements while invoking and implementing a resolution plan for 'Other Exposures'. Some of these requirements include:

- **Lenders to sign an inter-Creditor Agreement (ICA):** In all cases involving multiple lending institutions, once the resolution process has been invoked, ICA should be signed by all lenders (and at least the requisite number of lending institutions[3]) within 30 days from the date of invocation. Failure in doing so would result in the invocation being lapsed, and a resolution process cannot be invoked again for that facility, under Resolution framework.
- **Key ratios:** RBI constituted an Expert Committee which has recommended a list of financial parameters (key ratios) with sector specific ranges for such parameters[4]. These parameters need to be factored into the assumptions that go in **each resolution plan[5]** pertaining to 'other exposures'.
- **Escrow account:** In accounts involving multiple banking arrangements, post implementation of the resolution plan, all receipts and repayments by the borrower, and additional disbursements by lenders as part of the resolution plan, would be routed through an escrow account maintained by one of the lending institutions.

In its circular dated 7 September 2020, RBI stated that the applicability of ICA and maintenance of escrow account would be at a borrower level.

Clarifications

Following are the clarifications:

- The circular does not provide for any minimum cut off with respect to aggregate outstanding exposure with banking system for mandatorily signing ICA. Accordingly, if there are multiple lending institutions with exposure to a borrower falling in the category of 'Other Exposures' of the Resolution Framework, then all lending institutions having exposure to such borrower are required to enter into ICA. *(Clarification no 12)*
- The list of financial parameters prescribed by the Expert Committee are applicable to all resolution plans to be undertaken in terms of Resolution Framework. The Resolution Framework is applicable to all borrowers in respect of 'Other Exposures'. *(Clarification no. 9)*
- For sectors, where the sector-specific thresholds (financial parameters) have not been specified in the list issued by the Expert Committee, the lenders are required to make their own internal assessment for specific ratios[6]. *(Clarification no. 15)*
- In the case of real estate sector, and other sectors, a company typically has multiple projects which are financed through multiple instruments. Therefore,
  - There is a sufficient flexibility to the lending institutions to formulate the ICAs in order to address specific requirements of each borrower, including designing different resolution approaches for different projects within an ICA
  - While an escrow account is required to be set up at a legal entity level, there is no prohibition in setting up additional separate escrow accounts at each project level, if the lenders desire
  - Only in respect of borrowers belonging to real estate sector, which have both residential and commercial real estate business, the prescribed thresholds for the financial parameters may be applied at the project level. *(Clarification no. 3)*

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3. Requisite number of lending institutions include:
   - At least 75 per cent by value of total outstanding credit facilities, and
   - At least 60 per cent by number of total lending institutions
4. In its circular dated 7 September 2020, the Expert Committee has prescribed the key ratios to be considered while evaluating resolution plans, and has specified 26 sectors with sector specific ranges for the key ratios.
5. Irrespective of the exposure.
6. 6 Lenders are required to make internal assessment of the following ratios- Total Outstanding Liabilities/Adjusted Tangible Net Worth (TOL/ATNW) and Total debt/EBITDA. However, the current ratio and Debt Service Coverage Ratio (DSCR) would be 1.0 and above in all cases, and Average DSCR (ADSCR) would be 1.2 and above in all cases.

As per the circular, resolution plans for accounts where the aggregate exposure of the lending institutions at the time of invocation of the resolution process is INR100 crore and above, are required to obtain an Independent Credit Evaluation (ICE) by any one Credit Rating Agency (CRA) authorised by RBI under the Prudential Framework. However, the circular does not specify the minimum desirable ICE symbol for the plan to be considered for implementation.

Clarification

The RBI clarified that resolution plans which receive a credit opinion of RP4 or better for the residual debt from one/multiple CRAs, would be considered for implementation under the Resolution Framework. In case credit opinion is obtained from more than one CRA, all such credit opinions must be RP4 or better. *(Clarification no. 13)*

V. Additional loan loss provisions to be maintained under the framework

Once the resolution plan has been implemented under the framework, the lending institutions are required to maintain loan loss provisions (termed as additional provisions) which would be higher of the provisions held as per the extant Prudential Norms on Income Recognition, Asset Classification and Provisioning (IRAC norms) or a prescribed percentage of the existing debt. However, it was not clear whether these provisions would be treated as specific provisions or as general provisions that would partly qualify to be included as Tier 2 capital.

Clarification

The additional provisions would be treated as specific provisions which would be maintained in respect of each exposure under consideration. *(Clarification no. 10)*

VI. Accounting implications of the Resolution Framework

The Resolution Framework prescribes the additional provisions that are required to be maintained on exposures for which a resolution plan has been implemented. However, it is silent on the accounting treatment for these provisions for financial institutions that have adopted the Indian Accounting Standards (Ind AS). Under Ind AS, entities are required to follow the principles enunciated in Ind AS 109, *Financial Instruments* for creating a provision for impairment on financial assets. However, it was not clear on whether they would be required to follow the principles of Ind AS or the provisions of the circular while accounting for the additional provisions.

Clarification

NBFCs which are required to comply with Ind AS would continue to be guided by the guidelines duly approved by their Boards and as per advisories issued by the Institute of Chartered Accountants of India (ICAI) for recognition of significant increase in credit risk and computation of Expected Credit Losses (ECL).

The additional provisions prescribed in the circular would constitute prudential floors[7]. *(Clarification no. 8)*

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7. As per RBI circular dated 13 March 2020 (which provides additional guidance to NBFCs and Asset Reconstruction Companies on Ind AS implementation), NBFCs are required to maintain provisions in the financial statements as per Ind AS. They are also required to compute the provision as per IRAC norms which would be treated as prudential floors. These entities would then disclose a comparison between prudential floors and Ind AS in the notes to financial statements.

4 Regulatory updates

Amendments to SEBI regulations

ICDR Regulations

The Securities and Exchange Board of India (SEBI) through a notification dated 28 September 2020 has amended the provisions relating to rights issue under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations).

Key amendments are as follows:

- **Applicability of ICDR Regulations:** The provisions of the ICDR Regulations are now applicable to a rights issue by a listed issuer where the aggregate value of the issue is **INR50 crore** (earlier INR10 core) or more.
- **Minimum subscription:** Currently, the minimum subscription to be received in the issue should be at least 90 per cent of the offer through the offer document. In case of non-receipt of minimum subscription, all application monies received should be refunded to the applicants not later than 15 days from the closure of issue.

  Amendment

  As per the amendment, the minimum subscription criteria will not be applicable to an issuer if:

  a. The objects of the issue involves financing other than financing of capital expenditure for a specific project and

  b. The promoter(s) and the promoter group of the issuer undertake to subscribe fully their portion of rights entitlements and do not renounce their rights entitlements except to the extent of renunciation within the promoter group.
- **Eligibility conditions for fast track rights issue:** Currently, an issuer is required to satisfy certain conditions for making a rights issue through the fast track route. Those, *inter alia,* include the following:

  a. No show-cause notices have been issued or prosecution proceedings have been initiated by SEBI and pending against the issuer, its promoters or whole-time directors as on the reference date.

  b. There are no audit qualifications on the audited accounts of the issuer in respect of those financial years for which such accounts are disclosed in the letter of offer.

  Amendment

  The amendments have modified the above-mentioned conditions. Accordingly, an issuer is required to, *inter alia,* satisfy the following while making a rights issue through the fast track route:

  a. No show-cause notices, excluding proceedings for imposition of penalty, have been issued by SEBI and pending against the issuer, its promoters or whole-time directors as on the reference date.

  In cases where show-cause notice(s) has been issued by SEBI in a proceeding for imposition of penalty or prosecution proceedings have been initiated by SEBI against the issuer, its promoters or whole-time directors, necessary disclosures in respect of such action(s) along-with its potential adverse impact on the issuer should be made in the letter of offer.

  b. For audit qualifications, if any, in respect of any of the financial years for which financial statements are disclosed in the letter of offer, the issuer should provide the restated financial statements adjusting for the impact of the audit qualifications.

  Further, for the qualifications wherein impact on the financial statements cannot be ascertained the same should be disclosed appropriately in the letter of offer.

Effective date: The amendments are effective from the date of their publication in the Official Gazette i.e. 1 October 2020.

(Source: SEBI notification no. SEBI/LAD-NRO/GN/2020/31 dated 28 September2020)

Listing Regulations

On 8 October 2020, SEBI has issued certain amendments to the SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 (Listing Regulations).

Key amendments are as follows:

- **Asset cover by debt listed companies:** Currently, a listed company with listed Non-Convertible Debt Securities (NCDS) is required to maintain 100 per cent asset cover in respect of NCDS which should be sufficient to discharge the principal amount at all times for the NCDS issued.

  The requirement is not applicable in case of unsecured debt securities issued by regulated financial sector entities eligible for meeting capital requirements as specified by respective regulators.

  Amendment

  In addition to the current requirement, the amendments to the Listing Regulations permits a listed company to maintain an asset cover as per the terms of offer document/Information Memorandum and/or debenture trust deed in respect of the NCDS issued.

  Additionally, the exemption from maintaining an asset cover granted to unsecured debt securities issued by regulated financial sector entities has been removed.

- **Intimation to debenture trustee:** Currently, a company with listed debt securities is required to send certain documents and intimations to the debenture trustee promptly. Those, *inter alia,* includes:

  a. Intimations regarding revision in credit rating, default in timely payment of interest or redemption or both in respect of the NCDS and failure to create charge on assets.

  b. A half-yearly certificate regarding maintenance of 100 per cent asset cover in respect of listed NCDS, **by either a practicing Company Secretary (CS) or a practicing Chartered Accountant (CA),** along with the half-yearly financial results.

  The submission of half-yearly certificate is not applicable in cases **where a listed entity is a bank, Non-Banking Financial Company (NBFC) registered with the Reserve Bank of India (RBI)** or where bonds are secured by a government guarantee.

  Amendment

  In addition to the current requirements, a listed company is required to provide an intimation of all covenants of the issue (including side letters, accelerated payment clause, etc.) to the debenture trustees.

  Further, the requirement relating to submission of half-yearly certificate has also been amended. As per the revised requirement, a listed entity is required to submit a half-yearly certificate regarding maintenance of 100 per cent asset cover **or asset cover as per the terms of offer document/Information Memorandum and/or debenture trust deed, including compliance with all the covenants,** in respect of listed NCDS, **by the statutory auditor,** along with the half-yearly financial results.

  The submission of half-yearly certificate is not applicable where bonds are secured by a government guarantee. Accordingly, no exemption is available to a listed company which is a bank or NBFC from submission of the said half-yearly certificate.

  (Emphasis added to highlight the changes)

- **Forensic audit (Schedule III – Part A):** Para A of Part A of Schedule III to the Listing Regulations specifies events which are deemed to be material events to be reported by companies with listed specified securities (i.e. equity shares and convertible securities) to the recognised stock exchange(s) as soon as possible but not later than 24 hours from the occurrence of the event or information. Those, *inter alia,* includes events relating to:

  a. Fraud/defaults by a promoter, Key Managerial Personnel (KMP) or by the listed company

  b. Arrest of KMP or promoter

  c. Change in directors, KMP, auditor and compliance officer

  d. Resignation by an auditor and independent director of the listed company.

Amendment

In addition to the current requirements, every company with listed specified securities is required to make following disclosures to the stock exchange(s) in case of initiation of forensic audit (by whatever name called):

a. The fact of initiation of forensic audit along-with name of entity initiating the audit and reasons for the same, if available

b. Final forensic audit report (other than for forensic audit initiated by regulatory/enforcement agencies) on receipt by the listed entity along with comments of the management, if any.

Effective date: The amendments are effective from the date of their publication in the Official Gazette i.e. 9 October 2020.

For a detailed read, please refer to KPMG in India's First Notes on 'SEBI issues amendments for listed companies including disclosure of forensic audit' dated 28 October 2020.

(Source: SEBI notification no. SEBI/ LAD-NRO/GN/2020/33 dated 8 October 2020)

Debt Listing Regulations

The SEBI (Issue and Listing of Debt Securities) Regulations, 2008 (Debt Listing Regulations) are applicable to a public issue of debt securities and listing of debt securities issued through public issue or on a private placement basis on a recognised stock exchange. On 8 October 2020, SEBI has issued certain amendments to the Debt Listing Regulations.

Key amendments are as follows:

- **Revised definition of 'private placement':** Currently, 'private placement' has been defined to mean 'an offer or invitation to **less than 50 persons** to subscribe to the debt securities in terms of Section 67(3) of the **Companies Act, 1956 (1956 Act)'.**

  Amendment

  The amendments revised the definition of private placement in the Debt Listing Regulations. As per the revised definition, private placement would mean 'an offer or invitation to subscribe **or issue of securities to a select group of persons by a company (other than by way of public offer) through private placement offer-cum-application,** which satisfies the conditions specified in **Section 42 of the Companies Act, 2013 (2013 Act).**

  (Emphasis added to highlight the changes)

- **Creation of security:** A new requirement has been introduced by the amendments wherein an issuer is required to give an undertaking in the Information Memorandum that the assets on which charge is created are free from any encumbrances. Further, in cases where the assets are already charged to secure a debt, the permission or consent to create a second or pari-passu charge on the assets of the issuer has been obtained from the earlier creditor.

- **Recovery expense fund:** An issuer of debt securities is now required to create a recovery expense fund in the manner as may be specified by SEBI from time to time and inform the debenture trustee about the same.

  Manner and operation of recovery expense fund

  On 22 October 2020, SEBI through a circular has prescribed the manner of creation and operation of recovery expense fund. As per the circular, an issuer proposing to list debt securities should deposit an amount equal to 0.01 per cent of the issue size subject to a maximum of INR25 lakh per issuer towards recovery expense fund with the designated stock exchange as identified and disclosed in its offer document/Information Memorandum.

  The provisions of the circular would be effective from 1 January 2021.

Effective date: The amendments are effective from the date of their publication in the Official Gazette i.e. 9 October 2020.

For a detailed read, please refer to KPMG in India's First Notes on 'SEBI issues amendments for listed companies including disclosure of forensic audit' dated 28 October 2020.

(Source: SEBI notification no. SEBI/ LAD-NRO/GN/2020/35 dated 8 October 2020 and circular no. SEBI/HO/MIRSD/CRADT/CIR/P/2020/207 dated 22 October 2020)

Debenture Trustees Regulations

On 8 October 2020, SEBI has issued certain amendments to the SEBI (Debenture Trustees) Regulations, 1993 (Debenture Trustees Regulations).

Key amendments are as follows:

- **Duties of a debenture trustee:** Currently, a debenture trustee is required to ensure the implementation of the conditions regarding creation of security for the debentures, if any, and debenture redemption reserve. Additionally, in case where listed debt securities are secured by way of receivables/book debts, the debenture trustee is required to obtain the following:

Quarterly basis	a. Certificate from the director/ Managing Director (MD) of the issuer company certifying the value of the book debts/ receivables b. Certificate from an independent CA giving the value of book debts/ receivables.
Yearly basis	a. Certificate from the statutory auditor giving the value of book debts/receivables.

  Amendments

  The amendments require a debenture trustee to perform the following:

  – *Recovery expense fund:* A debenture trustee would need to ensure implementation of the conditions regarding recovery expense fund in addition to those relating to creation of security for the debentures and debenture redemption reserve.

– *Quarterly/yearly reporting:* The current requirements of obtaining documents on a quarterly/yearly basis have also been amended. According to the revised requirements, in case where listed debt securities are secured by way of receivables/book debts, a debenture trustee is required to perform the following on a:

Quarterly basis	Carry out the necessary due diligence and monitor the asset cover in the manner as may be specified by SEBI.
Half-yearly basis	Obtain a certificate from the statutory auditor of the issuer giving the value of receivables/book debts including compliance with the covenants of the offer document/Information Memorandum in the manner as may be specified by SEBI.

– *Due diligence:* In addition to the current duties, a debenture trustee is required to exercise independent due diligence before creating a charge on the security for the debentures to ensure that such security is free from any encumbrance or that it has obtained the necessary consent from other charge-holders if the security has an existing charge, in the manner as may be specified by SEBI.

– *Inter-creditor agreement:* A debenture trustee may enter into inter-creditor agreements, on behalf of the debenture holders, as provided under the framework specified by RBI, subject to the approval of the debenture holders and the conditions as may be specified by SEBI.

- **Meeting of debenture holders:** Currently, a debenture trustee shall call or cause to be called by the body corporate a meeting of all debenture holders on the occurrence of any event, which constitutes a default or which in the opinion of the debenture trustees affects the interest of the debenture holders.

  Amendment

  In addition to the current guidance, meeting shall be called by a debenture trustee or cause to be called by the body corporate in case of breach of covenants (as specified in the offer document/ Information Memorandum and/or debenture trust deed).

Effective date: The amendments are effective from the date of their publication in the Official Gazette i.e. 9 October 2020.

For a detailed read, please refer to KPMG in India's First Notes on 'SEBI issues amendments for listed companies including disclosure of forensic audit' dated 28 October 2020.

(Source: SEBI notification no. SEBI/LAD-NRO/GN/2020/34 dated 8 October 2020)

Relaxation with respect to validity of SEBI observations and revision in issue size

SEBI through a circular dated 29 September 2020 has extended the timeline for relaxations provided with respect to validity of SEBI observations and revision in issue size as follows:

- **Flexibility in issue size:** An issuer is permitted to increase or decrease the fresh issue size by up to 50 per cent of the estimated issue size without filing a fresh draft offer document with SEBI subject to specified conditions. The relaxation is applicable up to 31 March 2021 (earlier up to 31 December 2020).

- **Extension of validity of SEBI observations:** Currently, a public issue/rights issue may be opened for public/shareholders within 12 months from the date of issuance of observations by SEBI on the draft offer document/draft letter of offer.

  In view of the pandemic, the validity of SEBI observations expiring between 1 October 2020 and 31 March 2021 has been extended up to 31 March 2021, subject to an undertaking from lead manager to the issue confirming compliance with Schedule XVI of the ICDR Regulations while submitting the updated offer document to SEBI.

The provisions of the circular are effective from 1 October 2020.

(Source: SEBI circular dated 29 September 2020)

Amendments to guidelines for preferential issue and institutional placement of units by listed InvITs and REITs

SEBI through its circular dated 28 September 2020 has modified the guidelines issued for preferential issue and institutional placement of units by listed Infrastructure Investment Trusts (InvITs)[1] and listed Real Estate Investment Trusts (REITs)[2] on account of COVID-19.

Key changes relate to the following:

- **Subsequent institutional placement:** The InvIT/REIT should not make any subsequent institutional placement until the expiry of two weeks (earlier six months) from the date of the prior institutional placement made pursuant to one or more special resolutions.
- **Optional pricing method:** For any preferential issue between 28 September 2020 (date of SEBI circular) and 31 December 2020, the InvIT/REIT may opt for a pricing method where the price of the units to be allotted pursuant to the preferential issue should not be less than the higher of the average of the weekly high and low of the volume weighted average price of the related equity shares quoted on the recognised stock exchange during:

  a. 12 weeks preceding the relevant date or

  b. Two weeks preceding the relevant date.

  Additionally, the units allotted on a preferential basis using the above mentioned pricing option would be subject to a lock-in period of three years.

(Source: SEBI circular no. SEBI/HO/DDHS/DDHS/CIR/P/2020/184 and SEBI/HO/DDHS/DDHS/ CIR/P/2020/183 dated 28 September2020)

Extraordinary meeting of InvITs and REITs

SEBI through a circular dated 8 October 2020 has allowed InvITs and REITs to conduct extraordinary meeting(s) of their unitholders through Video Conferencing (VC) or Other Audio-Visual Means (OAVM) up to 31 December 2020 subject to a prescribed procedure.

(Source: SEBI circular no. SEBI/HO/DDHS/DDHS/CIR/P/2020/201 dated 8 October 2020)

Standard timelines for listing of securities issued on a private placement basis

SEBI through a circular dated 5 October 2020 has issued standard timelines for listing of securities issued on a private placement basis under the following regulations:

a. SEBI (Issue and Listing of Debt Securities) Regulations, 2008

b. SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013

c. SEBI (Public Offer and Listing of Securitised Debt Instruments and Security Receipts) Regulations, 2008 and

d. SEBI (Issue and Listing of Municipal Debt Securities) Regulations, 2015.

The timelines are as follows:

Details of activities	Due dates
Closure of issue	T day
Receipt of funds	To be completed by T+2 trading day
Allotment of securities	
Issuer to make listing application to stock exchange(s)	To be completed by T+4 trading day
Listing permission from stock exchange	

In case of delay in listing of securities issued on a private placement basis beyond the timelines specified above, an issuer would be:

a. Liable to pay a penalty at the rate of one per cent per annum over the coupon rate for the period of delay to the investor (i.e. from date of allotment to the date of listing) and

b. Permitted to utilise the issue proceeds of its subsequent two privately placed issuances of securities only after receiving final listing approval from stock exchanges.

The provisions of the circular are effective from 1 December 2020.

(Source: SEBI circular no. SEBI/HO/DDHS/CIR/P/2020/198 dated 5 October 2020)

1. SEBI circular no. SEBI/HO/DDHS/DDHS/CIR/P/2019/143 dated 27 November 2019.

2. SEBI circular no. SEBI/HO/DDHS/DDHS/CIR/P/2019/142 dated 27 November 2019.

Additional framework related to issuance, listing and trading of perpetual non-cumulative preference shares

Background

Perpetual Non-Cumulative Preference Shares (PNCPS) and Innovative Perpetual Debt Instruments (IPDIs)/Perpetual Debt Instruments (PDIs) (commonly referred to as 'AT 1 instruments') are essentially non-equity regulatory instruments, forming part of a bank's capital. These are governed by the Reserve Bank of India (RBI) guidelines and issued under the issuance and listing framework given under Chapter VI of the SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 (NCRPS Regulations).

These instruments have certain unique features which, *inter-alia,* grant the issuer (i.e. banks, in consultation with RBI) a discretion in terms of writing down the principal/interest, to skip interest payments, to make an early recall, etc. without commensurate right for investors to legal recourse, even if such actions of the issuer might result in potential loss to investors.

New development

SEBI through a circular dated 6 October 2020 has issued an additional framework relating to issuance, listing and trading of PNCPS and IPDIs which are proposed to be listed.

Key features of the framework are as follows:

- **Manner of issuance:** The AT 1 instruments should mandatorily be issued on the Electronic Book Provider (EBP) platform regardless of the issue size.
- **Investors:** Issuers and stock exchange(s) should ensure that only Qualified Institutional Buyers (QIBs) are allowed to participate in the issuance of AT1 instruments.
- **Allotment size:** The minimum allotment of AT1 instruments should not be less than INR1 crore.
- **Trading lot size:** The minimum trading lot size for AT1 instruments should be INR1 crore.
- **Disclosures:** Additional disclosures specified for the issuers of AT1 instruments which, *inter alia,* include specific disclosures about:
  a. Details of all conditions based on which call option will be exercised for these instruments in the Information/Private Placement Memo.
  b. Risk factors, to include all the inherent features of AT1 instruments.

The provisions of the circular are effective from 12 October 2020.

(Source: SEBI circular no. SEBI/HO/DDHS/CIR/P/2020/199 dated 6 October 2020)

SEBI clarifications on Insider Trading norms

Background

On 4 November 2019, SEBI had issued certain clarifications relating to the provisions of the SEBI (Prohibition of Insider Trading) Regulations, 2015 (PIT Regulations) in the form of Frequently Asked Questions (FAQs).

The FAQ, *inter alia,* clarified that in case the designated person is a fiduciary or intermediary, the structured digital database of the listed company should contain the names of the fiduciary or intermediary with whom they have shared Unpublished Price Sensitive Information (UPSI) along with the Permanent Account Number (PAN) or other identifier, in case PAN is not available. Further, the fiduciary or intermediary will be required to maintain details of persons with access to UPSI as specified in Schedule C to the PIT Regulations.

On 17 July 2020, SEBI issued amendments to the PIT Regulations which, *inter alia,* included amendments relating to maintenance and preservation of the structured digital database by a listed company.

New development

In line with the amendments to the PIT Regulations, on 8 October 2020, SEBI has issued revised clarification relating to information to be maintained in a structured digital database, in case the designated person is a fiduciary or intermediary.

As per the revised clarification, a listed company should maintain a structured digital database internally, which should contain information including the following:

- Details of UPSI
- Details of persons with whom such UPSI is shared (along with their PANs/other unique identifier in case PAN is not available) and details of persons who have shared the information.

Similarly, another structured digital database should be maintained internally by fiduciary or intermediary capturing the above information in accordance with Regulation 9A(2)(d) and Schedule C to the PIT Regulations.

(Source: FAQs on SEBI (PIT) Regulations, 2015 issued by SEBI on 8 October 2020)

SEBI clarification on fraudulent and unfair trade practices for listed companies

Background

Currently, the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (Unfair Trade Practices Regulations) governs the provisions relating to market abuse such as manipulative, fraudulent and unfair trade practices. As per Regulation 4(1) of the Unfair Trade Practices Regulations, no person should indulge in a manipulative, fraudulent or an unfair trade practice in securities markets.

New development

SEBI through a notification dated 19 October 2020 has amended the Unfair Trade Practices Regulations and added an explanation to Regulation 4(1) of the Unfair Trade Practices Regulations.

The explanation clarified that any act of diversion, misutilisation or siphoning-off of assets or earnings of a company or any concealment of such act or any device, scheme or artifice to manipulate the books of accounts or financial statements of such a company that would directly or indirectly manipulate the price of securities of that company shall be and shall always be deemed to have been considered as manipulative, fraudulent and an unfair trade practice in the securities market.

The amendment is effective from 19 October 2020.

(Source: SEBI notification no. SEBI/LAD-NRO/GN/2020/36 dated 19 October 2020)

Amendment to the Companies (Prospectus and Allotment of Securities) Rules, 2014

Currently, Rule 14(1) of the Companies (Prospectus and Allotment of Securities) Rules, 2014 (Prospectus Rules) prohibits a company from making an offer or invitation to subscribe to securities through a private placement unless the proposal has been previously approved by the shareholders of the company, by a special resolution for each of the offers or invitations.

Amendment

The Ministry of Corporate Affairs (MCA) through a notification dated 16 October 2020 has amended Rule 14(1) of the Prospectus Rules and introduced a provision. As per the provision, in case of offer or invitation of any securities to QIBs, it would be sufficient if the company passes a previous special resolution only once in a year for all the allotments to such buyers during the year.

The amendment is effective from the date of its publication in the Official Gazette i.e. 16 October 2020.

(Source: MCA notification no G.S.R. 642(E) dated 16 October 2020)

Extension of relaxation relating to minimum residency of a director

Currently, Section 149(3) of the Companies Act, 2013 (2013 Act) requires every company to have at least one director who stays in India for a total period of not less than 182 days during the Financial Year (FY). In March 2020, as part of special measures introduced in lieu of COVID-19, MCA provided that if the company fails to ensure compliance with the said requirement for FY2019-20, then it will not be treated as a non-compliance.

Relaxation

MCA through a circular dated 20 October 2020 has extended the relaxation for FY2020-21. Accordingly, failure to meet the minimum residency requirement of a director would not be treated as a non-compliance also for FY2020-21.

(Source: MCA general circular no. 36/2020 dated 20 October 2020)

Labour codes received Presidential assent

With an aim to rationalise labour laws prevalent in India, recently, following codes have been passed by the Parliament and have received assent of the President of India on 28 September 2020:

- **The Occupational Health, Safety and Working Conditions Code, 2020:** The Code seeks to amend the laws regulating the occupational safety, health and working conditions of the persons employed in an establishment and related matters.
- **The Industrial Relations Code, 2020:** The Code seeks to consolidate and amend the laws relating to trade unions, conditions of employment in industrial establishment or undertaking, investigation and settlement of industrial disputes and related matters.
- **The Code on Social Security, 2020:** The Code seeks to amend and consolidate the laws relating to social security with the goal to extend social security to all employees and workers either in the organised, unorganised or any other sectors and related matters.

Effective date: The Codes will come into force on such date as the Central Government (CG) may, by notification in the Official Gazette, appoint. Different dates may be appointed for different provisions of the Code.

For a detailed read, please refer to KPMG in India's First Notes on 'Revised norms relating to PF and gratuity under the Code on Social Security, 2020' dated 29 October 2020.

(Source: Codes issued by the Ministry of Law and Justice on 29 September 2020)

Deferment of implementation of Net Stable Funding Ratio (NSFR)

Background

Net Stable Funding Ratio (NSFR) is one of the significant components of the Basel III reforms. It requires banks to fund their activities with sufficiently stable sources of funding over a time horizon of a year in order to mitigate the risk of future funding stress. As per the prescribed timeline, banks in India were required to maintain NSFR of 100 per cent from 1 April 2020. Related NSFR guidelines were also to be implemented from 1 April 2020.

In light of the pandemic (COVID-19), the implementation of NSFR and related guidelines were deferred up to 1 October 2020.

New development

RBI through a notification dated 29 September 2020 has further deferred the implementation of NSFR guidelines by a period of six months. Accordingly, these guidelines will now come into effect from 1 April 2021.

(Source: RBI notification no. RBI/2020-21/43 dated 29 September 2020)

SLR holdings in HTM category

Currently, banks are permitted to exceed the limit of 25 per cent of the total investments under Held to Maturity (HTM) category subject to the condition that the excess comprises only of Statutory Liquid Ratio (SLR) securities and total SLR securities held under HTM category is not more than 19.5 per cent of Net Demand and Time Liabilities (NDTL) as on the last Friday of the second preceding fortnight.

The RBI through a notification dated 1 September 2020 had permitted banks to hold under HTM category, SLR securities acquired on or after 1 September 2020 up to an overall limit of 22 per cent of their NDTL up to 31 March 2021 to be reviewed thereafter.

Relaxation

The RBI through a notification dated 12 October 2020 has extended the dispensation of the enhanced HTM limit of 22 per cent, for SLR securities acquired between 1 September 2020 and 31 March 2021, up to 31 March 2022 i.e. banks may continue to hold such excess SLR securities in HTM category up to 31 March 2022.

Further, the enhanced HTM limit should be restored to 19.5 per cent in a phased manner, beginning from the quarter ending 30 June 2022, i.e. the excess SLR securities acquired by banks during the period 1 September 2020 to 31 March 2021 should be progressively reduced such that the total SLR securities held in the HTM category as a percentage of the NDTL does not exceed the following:

a. 21 per cent as on 30 June 2022

b. 20 per cent as on 30 September 2022

c. 19.50 per cent as on 31 December 2022.

Banks may shift investments to/from HTM with the approval of the board of directors once a year and such shifting will normally be allowed at the beginning of the accounting year.

(Source: RBI notification no RBI/2020-2021/54 dated 12 October 2020)

CBDT amends the Tax Audit Report (Form 3CD)

On 1 October 2020, the Central Board of Direct Taxes (CBDT) through a notification has amended the Income-tax Rules, 1962 (the Rules) which, *inter alia,* includes amendments to Form 3CD (statement of particulars required to be furnished under Section 44AB of the Income-tax Act, 1961 (IT Act)). Those are as follows:

- **Clause introduced in Part A of Form 3CD:** Additional information to be provided as to whether the assessee has opted for taxation under Section 115BA[3]/115BAA[4]/115BAB[5] of the IT Act.
- **Clauses modified in Part B of Form 3CD:**
  - *Particulars of depreciation:* Additional information to be provided with respect to adjustment made to the written down value of assets under Section 115BAA (for assessment year 2020-21 only) along with adjusted written down value.
  - *Brought forward loss/depreciation allowance:* Details of brought forward loss or depreciation allowance in Form No. 3CD has been modified to incorporate details relating to losses/ allowances not allowed under Section 115BAA of the IT Act and amount as adjusted by withdrawal of additional depreciation on account of opting for taxation under Section 115BAA of the IT Act.

The amendments are effective from 1 October 2020.

(Source: CBDT notification no. G.S.R.610(E) dated 1 October 2020)

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3. Tax on income of certain manufacturing domestic companies
4. Tax on income of certain domestic companies
5. Tax on income of new manufacturing companies

Extension of the due date for filing of Form GSTR-9 and GSTR-9C

The Ministry of Finance through a press release dated 24 October 2020 has extended the due date of furnishing Form GSTR-9/GSTR-9A (Annual Return) and Form GSTR 9C (Reconciliation statement) for FY2018-19 up to 31 December 2020.

(Source: Ministry of Finance press release dated 24 October 2020)


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First Notes

Revised norms relating to PF and gratuity under the Code on Social Security, 2020

29 October 2020

With an aim to rationalise labour laws prevalent in India, recently, following codes have been passed by the Parliament and have received assent of the President of India on 28 September 2020:

- The Occupational Health, Safety and Working Conditions Code, 2020
- The Industrial Relations Code, 2020
- The Code on Social Security, 2020

The Codes will come into force on such date as the Central Government (CG) may, by notification in the Official Gazette, appoint. Different dates may be appointed for different provisions of the Code.

In this issue of First Notes, we aim to summarise key features of the Code on Social Security, 2020 along with highlighting the key changes introduced vis-à-vis existing provisions under various laws.

Voices on Reporting (VOR) – Quarterly updates publication

On 19 October 2020, KPMG in India released the Voices on Reporting – quarterly updates publication (for the quarter ended 30 September 2020). The publication provides a summary of key updates from the Securities and Exchange Board of India (SEBI), the Ministry of Corporate Affairs (MCA), the Institute of Chartered Accountants of India (ICAI) and the Reserve Bank of India (RBI).

To access the publication, please click here.

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