Accounting and Auditing Update

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Editorial

Indian Accounting Standards (Ind AS) are largely converged with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB). In view of the issuance of new Conceptual Framework by the IASB and with an objective to remain converged with the global accounting framework, the Institute of Chartered Accountants of India (ICAI) has recently issued revised Conceptual Framework for Financial Reporting under Ind AS. The revised Conceptual Framework introduces some new concepts and clarifications along with revision in definitions and changes in recognition criteria of assets and liabilities under Ind AS. In this edition of Accounting and Auditing Update (AAU), we discuss some of the key changes introduced by the Conceptual Framework vis-à-vis financial reporting under Ind AS relevant for the preparers of the financial statements.

In the recent past, various instances of corporate failures have been reported on account of inability to meet their repayment obligations or siphoning off funds/utilisation of funds for purposes other than business purpose. The Companies (Auditor's Report) Order, 2020 (CARO 2020) has introduced various reporting requirements which are aimed to assess the veracity of the loans and advances provided by or granted to the companies. Some of the key reporting requirements relate to loans or advances in the nature of loans which are either repayable on demand or do not specify any terms or period of repayment; application of terms loans for the purpose for which those have been raised, if not then specific reporting on amount so diverted; default in repayment of loans/borrowings by a company to any lender or declared as a willful defaulter and specific reporting on evergreening of loans. Our article on the topic covers these reporting requirements and also highlights related guidance provided by ICAI in the Guidance Note on CARO 2020 issued in this regard.

As is the case each month, we have also included a regular round-up of some recent regulatory updates in India and internationally. The much-awaited Companies (Amendment) Act, 2020 has received the Presidential assent on 28 September 2020. It makes significant amendments to the provisions of the Companies Act, 2013 (2013 Act). For instance, Central Government is now empowered to exclude companies issuing specified classes of securities from the definition of a listed company, certain class of public companies will be permitted to list their securities on permitted stock exchanges in permissible foreign jurisdictions and companies with a Corporate Social Responsibility (CSR) liability of up to INR50 lakh will be exempt from the requirement of constituting a CSR committee under the 2013 Act. Further, certain relaxations have also been given to companies by MCA amid COVID-19 up to 31 December 2020. Those, *inter alia*, include, conduct of board meetings for specific matters and Extraordinary General Meetings (EGMs) through video conferencing or other audio-visual means and extension of timeline for enrolment in data bank of independent directors. Our article provides an overview of these and other regulatory and financial reporting developments.

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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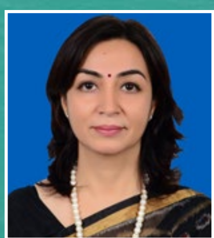

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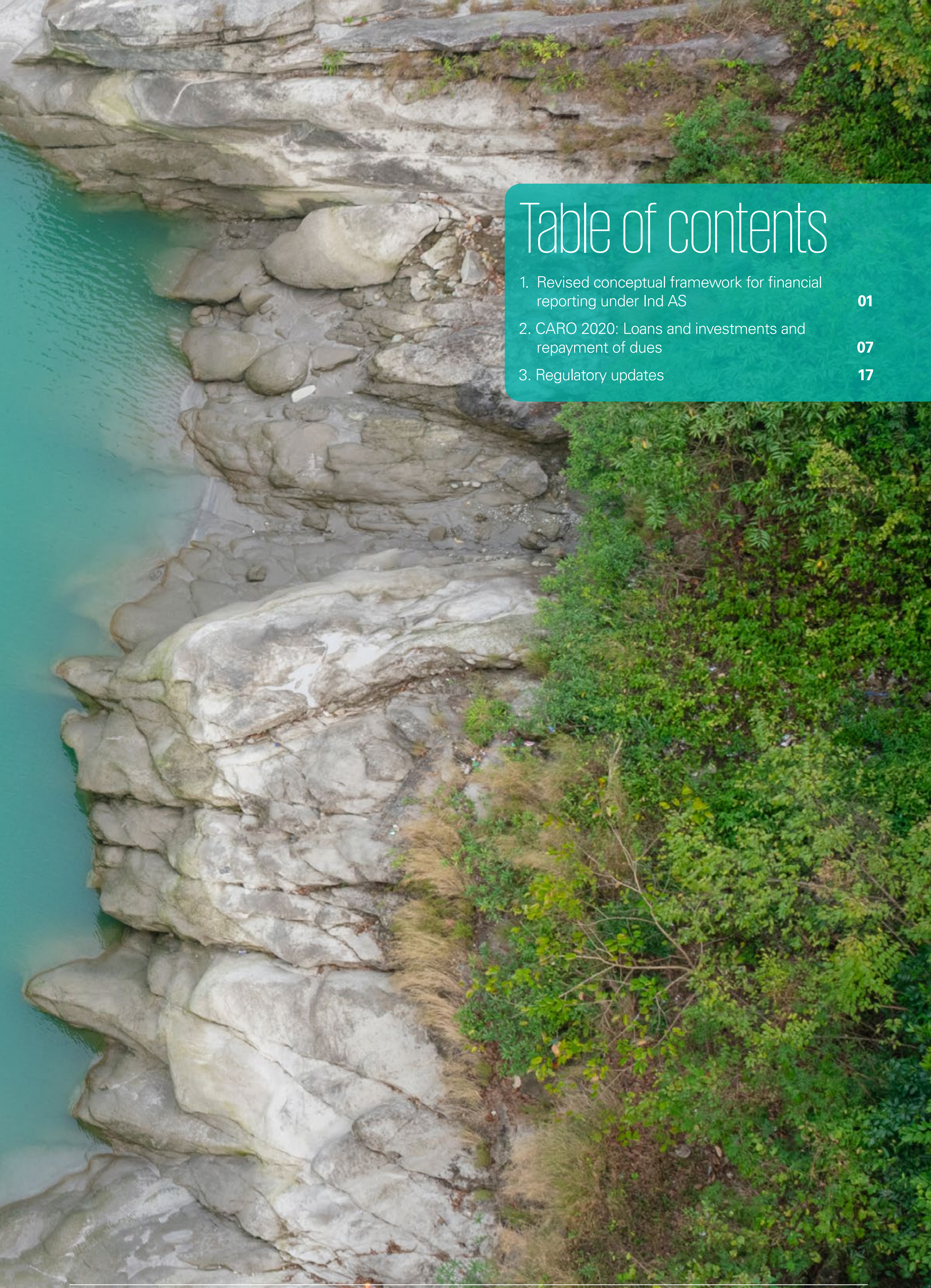

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Revised conceptual framework for financial reporting under Ind AS

This article aims to:

Discuss key changes made by the revised Conceptual Framework for financial reporting under Ind AS relevant for the preparers of financial statements.

Introduction

Recently, the Institute of Chartered Accountants of India (ICAI) has issued a revised 'Conceptual framework for financial reporting under the Indian Accounting Standards (Ind AS)' (the Conceptual Framework)[1]. The framework has been revised basis the revised conceptual framework[2] issued by the International Accounting Standards Board (IASB). The IASB issued the Conceptual Framework in March 2018.

While, the primary purpose of the Conceptual Framework is to assist ICAI in formulating Ind AS, it would also assist preparers of financial statements to develop consistent accounting policies when no Ind AS applies to a particular transaction or other event or when an Ind AS allows a choice of an accounting policy. The Conceptual Framework provides the foundation for IFRS/Ind AS and serves as a basis on which new/revised accounting standards are developed.

The Conceptual Framework introduces some new concepts and related clarification along with revision in definitions and changes in recognition criteria of assets and liabilities under Ind AS.

In this article, we aim to highlight some of the key changes introduced by the Conceptual Framework vis-à-vis financial reporting under Ind AS. Understanding these changes would be relevant for the preparers of the financial statements.

Overview of the changes

Objective of financial reporting

The objective of financial reporting is to provide useful financial information about the reporting entity to its stakeholders to assist them in making decisions relating to providing resources to the entity.

As per the Conceptual framework, those decisions would depend on the stakeholders' expectations about returns which would further depend on assessment of the amount, timing and uncertainty of future net cash inflows to the entity and assessment of management's stewardship of the entity's economic resources.

To achieve the said objective, the Conceptual Framework emphasises the importance of providing information about a reporting entity's economic resources, claims against the entity and changes in resources and claims along with information about use of an entity's economic resources in the financial reports.

Qualitative characteristics of useful financial information

As per the Conceptual Framework, for a useful financial information, in addition to being relevant, the information needs to **faithfully represent** the substance of the financial information. To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral/unbiased and free from error.

Further, whether the information would depict faithful representation could be affected by the level of measurement uncertainty associated i.e. uncertainty that arises when monetary amounts in financial reports cannot be observed directly and must instead be estimated. In some cases, the most useful information may be a highly uncertain estimate, accompanied by a description of the estimate and an explanation of the uncertainties that affect it. In other cases, if the information would not provide a sufficiently faithful representation, the most useful information may include an estimate of another type that is slightly less relevant but is subject to lower measurement uncertainty.

Enhancing qualitative characteristics

As per the Conceptual Framework, comparability, verifiability, timeliness and understandability are qualitative characteristics that enhance the usefulness of information that both is relevant and provide a faithful representation of what it purports to represent.

1. The Conceptual Framework is not an Ind AS. Accordingly, nothing in the Conceptual Framework overrides any Ind AS or any requirement in an Ind AS.

2. Conceptual Framework for Financial Reporting

Financial statements and reporting entity

The objective of financial statements is to provide financial information about the reporting entity's assets, liabilities, equity, income and expenses that is useful to users of financial statements.

As per the Conceptual Framework, reporting entity could be any entity that is required or chooses to prepare financial statements but not necessarily a legal entity. It can be a single entity or a portion of an entity or can comprise more than one entity.

Further, the Conceptual Framework also provides guidance in cases where it is difficult to determine the boundary of a reporting entity in the absence of legal form. According to it, in such cases, determining the boundary of the reporting entity is driven by the information needs of the primary users of the reporting entity's financial statements which is relevant information that faithfully represents what it purports to represent.

Additional guidance has been provided with respect to consolidated, unconsolidated and combined financial statements as different forms of financial statements.

Elements of financial statements

The Conceptual Framework defines following elements of financial statements:

a. Assets, liabilities and equity, which relate to a reporting entity's financial position and

b. Income and expenses, which relate to a reporting entity's financial performance.

The Conceptual Framework made significant changes in the definition of an asset and a liability. According to it:

- **An asset** is a present economic resource **controlled** by the entity as a result of past events wherein an economic resource is a **right** that has the potential to produce economic benefits.

  The main change to definition of an asset is a separate definition of an economic resource.

  As per the Conceptual Framework, not all of an entity's rights are assets of that entity. For rights to be assets of the entity, the rights must have following two characteristics:

  – The potential to produce for the entity economic benefits beyond the economic benefits available to all other parties and

  – Be controlled by the entity.

  Also, a right can meet the definition of an economic resource even if the probability that it will produce economic benefits is low.

- **A liability** is a present obligation of the entity to transfer an economic resource as a result of past events wherein an obligation is a duty or responsibility that an entity has no practical ability to avoid. As per the Conceptual Framework, an obligation can meet the definition of a liability even if the probability of a transfer of an economic resource is low.

Related changes have also been made to the definition of income and expenses.

Recognition and derecognition

- **Recognition** is the process of capturing for inclusion in the balance sheet or the statement of profit and loss an item that meets the definition of one of the elements of financial statements–an asset, a liability, equity, income or expenses.

  As per the Conceptual Framework, recognition of a particular asset or a liability is appropriate if it provides relevant information along with faithful representation of the asset or liability and of any resulting income, expenses or changes in equity.

- **Derecognition** is the removal of all or part of a recognised asset or liability from an entity's balance sheet which normally occurs when that item no longer meets the definition of an asset or of a liability. The guidance on derecognition has been newly introduced in the Conceptual Framework.

  As per the Conceptual Framework, derecognition normally occurs:

  a. For an asset: When an entity loses control of all or part of the recognised asset and

  b. For a liability: When an entity no longer has a present obligation for all or part of the recognised liability.

  Further, derecognition should aim to faithfully represent assets and liabilities retained after the transaction or other event that led to the derecognition (including any asset or liability acquired, incurred or created as part of the transaction or other event) and the change in the entity's assets and liabilities as a result of that transaction or other event.

Measurement

A measurement basis is an identified feature of an item being measured, for instance, historical cost, fair value or fulfilment value. As per the Conceptual Framework, while selecting a measurement basis, it is important to consider the nature of the information that the measurement basis will produce in both the balance sheet and the statement of profit and loss.

It identifies following two types of measurement basis:

- **Historical cost:** Historical cost measures provide monetary information about assets, liabilities and related income and expenses, using information derived, at least in part, from the price of the transaction or other event that gave rise to them. Accordingly:
  - *For an asset*: It is the value of the costs incurred in acquiring or creating the asset, comprising the consideration paid to acquire or create the asset plus transaction costs.
  - *For a liability:* It is the value of the consideration received to incur or take on the liability minus transaction costs.

  Measurement of assets and liabilities at historical cost provides relevant information about both the asset or liability and the price of the transaction that gave rise to that asset or liability. Measurement of income and expenses at historical cost may have predictive and confirmatory value as the information provided by it can be used as an input in predicting future cash flows and also it may provide feedback to users of financial statements about their previous predictions of cash flows or of margins.
- **Current value:** Current value measures provide monetary information about assets, liabilities and related income and expenses, using information updated to reflect conditions at the measurement date. Current value measurement bases include fair value, value in use for assets, fulfilment value for liabilities and current cost.

In addition to the nature of information, other factors to be considered while selecting a measurement basis includes, assessment of whether the information provided to users of financial statements is useful i.e. it is relevant and faithfully represent what it purports to represent. Other factors could include qualitative characteristics of useful financial information and cost constraint. Consideration of these factors could result in selection of different measurement basis for different assets, liabilities, income and expenses.

Presentation and disclosure

According to the Conceptual Framework, effective communication of information in financial statements makes that information more relevant and contributes to a faithful representation of an entity's assets, liabilities, equity, income and expenses. It also enhances the understandability and comparability of information in financial statements.

Accordingly, following principles should be considered while communicating information in financial statements:

a. Entity-specific information is more useful than standardised descriptions ('boilerplate')

b. Duplication of information in different parts of the financial statements is usually unnecessary and could make financial statements less understandable.

Applicability

The Conceptual Framework is applicable for standard-setting activity effective from 1 April 2020. The applicability of the Conceptual Framework for preparers of financial statements will be notified separately along with consequential amendments to certain Ind AS arising from the Conceptual Framework.

Our comments

The Conceptual Framework provides a point of reference for preparers of financial statements while selecting their accounting policies in the absence of specific Ind AS dealing with the subject matter under consideration or related issues. Accordingly, entities should consider the principles of financial reporting as highlighted under the Conceptual Framework for effective communication of information to their stakeholders.

The main changes to the Conceptual Framework's principles have implications for how and when assets and liabilities are recognised and derecognised in the financial statements. Some of these implications are as follows:

- **New 'bundles of rights' approach to assets:** A physical object can be 'sliced and diced' from an accounting perspective. However, to what extent an asset can be split into different rights and consequent impact on recognition and derecognition could pose challenge for entities.
- **New 'practical ability' approach for recognising liabilities:** Under the Conceptual Framework, a liability would be recognised if a company has no practical ability to avoid it. This may bring some liabilities on the balance sheet earlier than at present. However, if there is uncertainty over existence and measurement or a low probability of outflows, then this may result in no or delayed recognition in some cases.

  The challenge would be determining which future actions/costs a company has no 'practical ability' to avoid.
- **New control-based approach to derecognition:** A company would take an asset off balance sheet when it loses control over all or part of it – i.e. the focus is no longer on the transfer of risks and rewards. The challenge would be determining what to do if the company retains some rights after the transfer.

(Source: Conceptual Framework for Financial Reporting under Ind AS issued by ICAI on 28 August 2020 and KPMG IFRG Ltd.'s publication 'Conceptual Framework – The new foundation for IFRS' dated 29 March 2018)

02

CARO 2020: Loans and investments and repayment of dues

This article aims to:

Discuss the reporting requirements relating to investments made, guarantee/ security or loans/ advances in the nature of loans provided by companies along with those relating to default in repayment of loans or other borrowings granted to the company.

Introduction

The Companies (Auditor's Report) Order, 2020 (CARO 2020) significantly enhances the reporting requirements by auditors along with the need for companies to maintain adequate records for the purpose of verification.

In general, companies engage in borrowing or lending activities from/to other entities including their subsidiaries, joint ventures and associates for their business operations. In the recent past, various instances of corporate failures have been reported on account of failure to meet their repayment obligations or siphoning of funds/utilisation of funds for purposes other than business purpose. In order to assess the veracity of such loans and borrowings, CARO 2020 introduces various reporting requirements on following aspects:

- Investments made, guarantee/ security or loans/advances in the nature of loans provided by companies
- Compliance with provision of Section 185 and 186 of the 2013 Act
- Default in repayment of loans and other borrowings by companies
- Situations when a company is declared as a wilful defaulter
- Purpose for which term loans have been applied
- Situations where short-term funds have been applied for long-term purposes
- Funds raised to meet obligations of subsidiaries, associates or joint ventures
- Funds raised on pledge of securities held in subsidiaries, joint ventures or associates.

In this article, we aim to discuss these reporting requirements and will also highlight the related guidance provided by the Institute of Chartered Accountants of India (ICAI) in the Guidance Note on CARO 2020 (guidance note) issued in this regard.

Investments and loans and advances in the nature of loans

CARO 2020 has modified the requirement relating to providing loans and advances by companies vis-à-vis CARO 2016 and has also added few new reporting requirements.

As per the revised requirement, an auditor is required to report whether the company has made **investments in, provided any guarantee or security** or granted any loans or **advances in the nature of loans,** secured or unsecured, to companies, firms, Limited Liability Partnerships (LLPs) or **any other parties.** Therefore, in addition to loans, the revised clause covers reporting on investments made, guarantee or security provided or advances in the nature of loans granted by companies.

The reporting requirement under this clause are sub-divided into six clauses which has been discussed below.

Guidance by ICAI

An auditor is required to comment on each of the sub-clause and in respect of all loans/advances in nature of loans granted, guarantee or security provided to companies, firms, LLPs or any other parties. Further, all kind of loans i.e. long-term/short-term, in cash or in kind given by the company to any party would be covered.

Loans, advances in the nature of loan and guarantee/security provided

CARO 2020 has introduced a new reporting requirement relating to whether a company has provided loans or advances in the nature of loans, or stood guarantee, or provided security to any other entity during the year. If the answer is yes, then it would need to indicate:

a. The aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to subsidiaries, joint ventures and associates.

b. The aggregate amount during the year, and balance outstanding at the balance sheet date with respect to such loans or advances and guarantees or security to parties other than subsidiaries, joint ventures and associates.

Guidance by ICAI

The clause would be applicable to all companies except companies whose principal business is to give loans for example, financial institutions, Non-Banking Financial Companies (NBFCs) or NBFC registered as a core investment company.

Determination of whether an advance is in the nature of a loan would depend upon the circumstances of each case. For instance, an advance given in excess of the value of an order or for a period which is in excess of the period for which such advances are usually extended as per the normal trade practice, could be considered as an advance in nature of a loan to the extent of such excess.

Further, reporting under this clause would cover only financial guarantee given by a company to a bank or financial institution in respect of loans taken by a third party.

For the purpose of reporting, an auditor would be required to determine the gross amount (i.e. without adjusting any subsequent settlements) of all loans, advances in nature of loans, guarantees, security provided **during the year** (emphasis added) to subsidiaries, joint ventures, associates[1] and to any other parties. Loans/advances in nature of loan that have been squared-up (i.e. given and repaid) during the year would also be reported under this clause.

In addition to the sectoral laws such as guidelines prescribed by the Reserve Bank of India (RBI) in respect of NBFCs, an auditor would be required to evaluate compliance with the requirements of relevant provisions of the 2013 Act dealing with power of the board of directors with respect to granting of loans, norms relating to loans granted to directors, and loans and investments made by companies (i.e. Section 179, 180, 185, 186 and 187).

Terms and conditions not prejudicial to a company's interest

CARO 2020 has modified the reporting requirement and requires an auditor to comment on whether the terms and conditions of the **investments, guarantee, security, all loans/advances in nature of loans** granted during the year are not prejudicial to the interest of the company.

(Emphasis added to highlight the additions made vis-à-vis CARO 2016)

Guidance by ICAI

Reporting under the clause would be applicable to all companies including financial institutions, NBFCs, etc.

A due consideration would need to be given to the terms and conditions of the loans/advances in the nature of loans/investments made/guarantee/security provided. Other factors would also be considered such as company's ability to lend/make investment/borrow and financial standing of the borrower/investee/party on whose behalf the company has given the guarantee. As per the guidance note, financial support by a holding company to its loss-making subsidiary would not be construed as prejudicial to the interest of the holding company.

Schedule of repayment of principal and interest

In respect of loans and advances in the nature of loans, an auditor is also required to report on stipulation of schedule of repayment of principal and payment of interest and on regularity of their repayments i.e. the principal and interest should normally be received whenever they fall due.

(Emphasis added to highlight the additions made vis-à-vis CARO 2016)

1. The definition of subsidiary, joint venture and associates would be construed in accordance with the 2013 Act.

Guidance by ICAI

Reporting under this clause would be applicable to all companies and would cover:

- Loans and advances in nature of loans granted during the year
- Loans and advances in nature of loans with opening balances and
- Advances in nature of loans which do not contain the schedule of repayment and payment of interest.

The clause requires examination of loan agreements, mutually agreed letter of arrangement, schedule of repayment of principal and payment of interest, etc. In certain cases where there is no loan agreement/ arrangement or the loan agreement/arrangement do not contain the schedule of repayment of principal and payment of interest, then the auditor would need to report this fact along with his/her inability to make a specific comment on the regularity of repayment of principal and payment of interest.

Additionally, where a schedule of repayment of principal or payment of interest is stipulated but such payments are not regular then an auditor may report this fact and may give number of such cases and remarks.

Amount overdue for more than 90 days

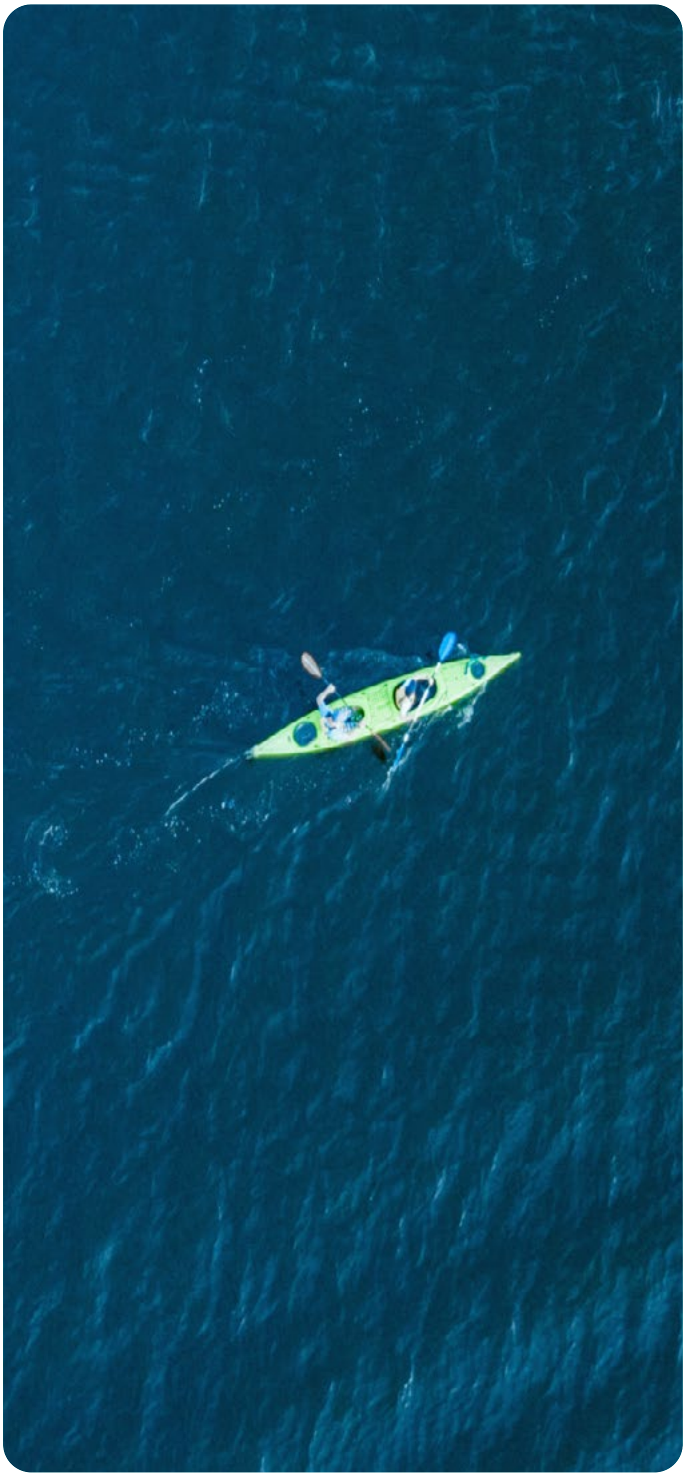
Similar to CARO 2016, CARO 2020 requires an auditor to disclose the total amount overdue (i.e. principal and interest) for more than 90 days from all parties as at the balance sheet date along with whether reasonable steps have been taken by the company for recovery of the principal and interest.

There is no major change in the reporting requirement vis-à-vis CARO 2016. This clause would cover loans including advances in nature of loans given by the company to any party.

Guidance by ICAI

Reporting under this clause would be applicable to all companies. As per the guidance note, facts and circumstances of each case including the amount involved would need to be considered by an auditor while examining whether reasonable steps (not necessarily legal steps) have been taken by the company for recovery of principal and interest.

Management of a company would need to provide in writing the steps taken by the management for recovery of the principal and interest.



Renewal of loans/fresh loans to settle overdues of existing loans

CARO 2020 introduces a new reporting requirement in respect of loan or advance in the nature of loan granted which has fallen due during the year and has been renewed or extended or fresh loans granted to settle the overdues of existing loans given to the same parties i.e. identification of instances of 'evergreening'[2] of loans/advances in the nature of loans.

Guidance by ICAI

Reporting under the clause would be applicable to all companies except companies whose principal business is to give loans for example, financial institutions, Non-Banking Financial Companies (NBFCs) or NBFC registered as a core investment company.

As per the guidance note, reporting under this clause would also cover loans falling due as on the balance sheet date and which were renewed/extended/settled post balance sheet date and before the date of audit report. Such instances would be reported in subsequent year as well. The clause is not restricted to 'overdue' loans but also extends to situations where fresh loans are given close to settlement date.

Loans granted to promoters and related parties

This is also a new clause which requires disclosure of gross amount of loans or advances in the nature of loans which are either repayable on demand or do not specify any terms or period of repayment in the auditor's report. If a company has granted such loans then specific disclosures would be made for aggregate amount of loans granted to promoters and related parties as defined under relevant provisions of the 2013 Act. As per the guidance note, such relationship (promoter or related party) may exist at any point during the year. Reporting under the clause would be applicable to all companies.

Compliance with provisions of Section 185 and 186 of the 2013 Act

CARO 2020 brings forward this reporting requirement from CARO 2016. This requirement relates to whether the company has complied with the provisions of Section 185 and 186 of the 2013 Act in respect of loans, investments, guarantees, and security provided in connection with loans.

As per the provisions of Section 185 of the 2013 Act, a company cannot advance any loan, including loan represented by a book debt, directly or indirectly to any of its directors. Such a restriction also extends to any guarantee given or security provided in connection with a loan. However, companies are allowed to give loans (including loan represented by a book debt), any guarantee or can provide any security in connection with any loan, to any person in whom any of the director is interested,[3] subject to prior approval by a special resolution and loans should be utilised by the borrowing company for its principal business activities.

Further, Section 186 of the 2013 Act governs the provisions relating to granting loans, guarantee or security and making investments by companies in other entities. While making investments, a company is not allowed to enter into certain transactions if the amount involved in the transaction exceeds 60 per cent of paid-up share capital, free reserves and securities premium account or 100 per cent of its free reserves and securities premium account, whichever is more, except by way of a special resolution passed at a general meeting. It also prohibits a company from making investments through more than two layers of investment companies, unless specifically exempted.

2. The term 'evergreening' is not defined in the 2013 Act. However, in general parlance it implies an attempt to mask loan default by giving new loans to help delinquent borrowers to repay/adjust principal or pay interest on old loans
3. Any person in whom any of the director of the company is interested' means:
   i. Any private company of which any such director is a director or member
   ii. Any body corporate at a general meeting of which not less than 25 per cent of the total voting power may be exercised or controlled by any such director, or by two or more such directors, together
   iii. Any body corporate, the BoD, MD or manager, whereof is accustomed to act in accordance with the directions or instructions of the BoD, or of any director or directors, of the lending company.

Guidance by ICAI

In respect of loan or related guarantee/security given by a company to its directors, the nature of the non-compliance, the maximum amount outstanding during the year and the amount outstanding as at the balance sheet date would be reported in respect of:

- Directors and
- Any person in whom any of the director of the company is interested (specifying the relationship with the director concerned).

With respect to loans and investments by companies to other entities, companies would need to disclose full particulars of the loan given, investment made or guarantee given or security provided in the financial statements including the purpose for which the same is proposed to be utilised by the recipient. Further, it would involve assessment of rate of interest, which should not be lower than the prevailing yield of government security, special resolution duly passed in case loans exceed the specified limits and prior approval from the public financial institution where any term loan is subsisting.

Default in repayment of loans or other borrowings by companies

Unlike CARO 2016, CARO 2020 requires an auditor to report on whether the company has defaulted in repayment of loans/other borrowings or **in the payment of interest thereon** to **any lender** (earlier reported only in case of defaults in repayment to a financial institution, bank or government) in a specified format as given below:

Guidance by ICAI

The clause covers defaults in payment of loans or other borrowings (including principal and interest) to any lender.

It also covers rescheduled/restructured loans, disputed loans and loans and borrowings on demand.

For the purpose of reporting under this clause, borrowings will not include public deposits and preference share capital. As per the guidance note, reporting under this clause would cover:

- Amount of all defaults[4] committed during the year along with number of days of default
- Amount and period of defaults existing at the balance sheet date irrespective of when those defaults have occurred.

Period up to the date of the auditor's report would be considered for the purpose of reporting the number of days delay or amount that remains unpaid.

In case of reschedulement/restructuring of loan, it has been clarified that mere submission of application would not mean that no default has occurred. In case the application for reschedulement of loan has been approved by the concerned bank or financial institution during the year covered by the auditor's report, then the fact would be reported by the auditor. However, if reschedulement has been approved subsequent to the balance sheet date, defaults during the year would be reported.

Nature of borrowing, including debt securities	Name of lender*	Amount not paid on due date	Whether principal or interest	No. of days delay or unpaid	Remarks, if any
	*lender wise details to be provided in case of defaults to banks, financial institutions and government.				
	Other lenders: Aggregate for each type of lender may be given, for example, debenture holders.				

4. The term 'default' for the purpose of reporting under this clause would mean non-payment of dues to lenders on the last dates specified in loan documents or debentures trust deed, as the case may be.

Further, in case of disputes between the lender and the company regarding repayment, prevailing terms and conditions would be considered by an auditor and a brief about nature of dispute would be reported.

Wilful defaulter

CARO 2020 intoduces a new reporting requirement relating to whether the company has been declared as a willful defaulter by any bank or financial institution or other lender.

Guidance by ICAI

As per the guidance note, reporting under this clause would be restricted to the relevant financial year under audit till the date of auditor's report. The term 'willful default' has been defined by RBI in its circular on willful defaulters[5] which, *inter alia*, includes occurrence of any of the following events as a willful default:

- The unit has defaulted in meeting its payment/ repayment obligations to the lender even when it has the capacity to honour the said obligations.
- The unit has defaulted in meeting its payment/ repayment obligations to the lender and has diverted the funds for purposes other than for which it was availed or has siphoned off the funds.
- The unit has defaulted in meeting its payment/ repayment obligations to the lender and has also disposed-off or removed the movable or immovable property given by it for the purpose of securing a term loan without the knowledge of the bank/lender.

The term 'lender' under the RBI circular covers all banks/financial institutions to which any amount is due. Though considering the objective of the clause, the guidance note has clarified that the clause would cover any bank or financial institution even if such bank or financial institution has not lent to the company. In respect of 'other lenders', reporting would be restricted to declaration of willful defaulter by government/ government authorities.

Further, if a company has not been declared a wilful defaulter but has received a show-cause notice in accordance with the RBI circular, the auditor may consider disclosing this fact in its report.

Apart from obtaining direct confirmations from banks/ financial institutions, an auditor may examine monthly reports submitted by banks and financial institutions to the credit information companies such as Credit Information Bureau (India) Limited (CIBIL) including verification of database of Central Repository of Information on Large Credits (CRILC), set up by RBI to collect, store, and disseminate credit data to lenders for the purpose of reporting under this clause.

Application of term loans

Another new reporting requirement under CARO 2020 relates to whether term loans were applied for the purpose for which these loans were obtained. If not, then the auditor is also required to report the amount of loan so diverted and the purpose for which it is used.

Guidance by ICAI

Term loans generally carry a repayment period of more than 36 months. Therefore, term loans would not cover cash credit, overdraft and call money accounts/deposits. As per the guidance note, term loans obtained from entities/persons other than banks/financial institutions would also be covered for the purpose of reporting under this clause.

The RBI circular on willful default defines diversion of funds to, *inter alia*, include any of the following events:

- Utilisation of short-term working capital funds for long-term purposes not in conformity with the terms of sanction
- Deploying borrowed funds for purposes/activities or creation of assets other than those for which the loan was sanctioned
- Investment in other companies by way of acquiring equities/debt instruments without approval of lenders.

Therefore, if the company has applied the general-purpose loan for any such purpose which can be defined as a diversion, an auditor would be required to report it accordingly. Further, utilisation of term loans which have been split as equity and debt components under the accounting framework would be considered in entirety for the purpose of reporting under this clause.

5. RBI master circular RBI/2014- 15/73DBR.No.CID.BC.57/20.16.003/2014-15 dated 1 July 2014.

There could be a situation that a company took a term loan during the year but did not apply for the stated purpose as it was disbursed at the end of the year. An auditor would be required to state this fact in his/her report. Additionally, the clause covers term loans which were taken in the previous accounting period but have been actually utilised during the current accounting period.

Application of short-term funds for long-term purposes

CARO 2020 introduces a new reporting requirement relating to whether funds raised on short-term basis have been utilised for long-term purposes. If the answer is yes, then an auditor would be required to report the nature and amount so utilised.

Guidance by ICAI

The underlying principle for the requirement is to assess financial health of an entity. For the purpose of reporting under this clause, long-term sources of funds along with their long-term application by a company would be determined using the data contained in the financial statements. Long-term sources of funds would include share capital, reserves and surplus, long-term debt securities and long-term loans and long-term application of funds could be investment in property, plant and equipment, intangible assets and repayment/redemption of long-term loans/debt.

As per the guidance note, if the quantum of long-term funds is significantly less than the long-term application of funds, then it would be an indication that short-term funds have been used to finance the long-term assets of the company. Further, a current ratio of less than one would also be an indicator that short-term funds have been used to finance long-term assets of the company.

Funds raised to meet obligations of subsidiaries, associates or joint ventures

Another new reporting requirement relates to whether the company has taken any funds from any entity or person on account of or to meet the obligations of its subsidiaries, associates or joint ventures[6]. If yes, then an auditor is required to provide the details along with the nature of such transactions and the amount in each case.

Guidance by ICAI

As per the guidance note, reporting under this clause would normally be required when a company has taken any funds from any entity/person and has also granted loans or advances in the nature of loans to its subsidiaries, associate companies or joint ventures or has made further investments in such subsidiaries, joint ventures, or associate companies.

Funds could be short-term or long-term and could be obtained from any entity irrespective of the legal form. Further, reporting under this clause would cover:

- All funds taken during the year even if these have been repaid before the year end
- Funds taken in earlier years and were repaid during the year or are outstanding as at the year end.

Though the term obligation has not been defined in the 2013 Act or in CARO 2020, it would in general mean the amounts that the subsidiaries, joint venture or associate companies are required to pay themselves either to their vendors, lenders, employees, or statutory authorities.

For the purpose of reporting, an auditor may examine schedule of loans and advances/borrowings and related party transactions maintained by the company along with obtaining direct confirmations from subsidiaries, joint venture or associate companies. In case financial statements of subsidiaries, joint ventures, and associates are audited by another auditor, it may also seek specific information from the auditors of the components.

Funds raised on pledge of securities held in subsidiaries, joint ventures or associates

Under CARO 2020, an auditor is also required to report whether the company has raised loans during the year on the pledge of securities[7] held in its subsidiaries, joint ventures or associate companies. In case the answer is affirmative, it requires an auditor to:

- Give details of such loans and
- Report if the company has defaulted[8] in repayment of such loans raised.

6. For the purpose of this clause, the term subsidiary, associate or joint venture would be as defined under the 2013 Act.

7. The term 'securities' would mean securities as defined under Section 2(h) of the Securities Contracts (Regulation) Act, 1956 (SCRA) which include, shares, scrips, stocks, bonds, debentures, or other marketable securities, derivative and government securities.

8. Default will include both repayment of principal and payment of interest.

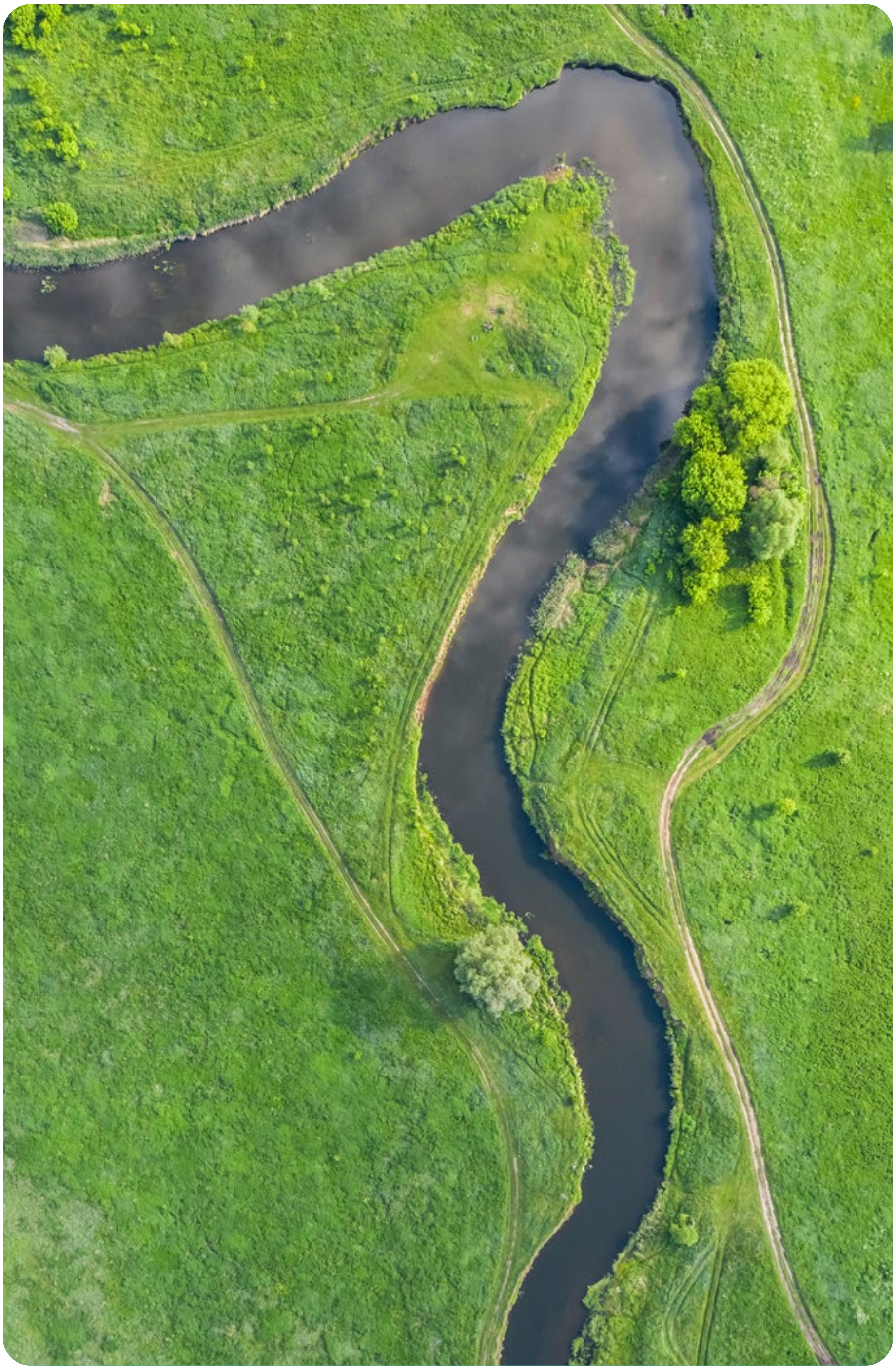
Guidance by ICAI

'Securities held in its subsidiaries, joint ventures or associate companies' would mean the investment of the company (reporting entity) in such subsidiary, joint venture or associate company.

Reporting under this clause would cover:

- All loans taken (from any lender) during the year even if repaid during the year. Accordingly, loans taken in earlier years and outstanding as at the balance sheet date would not be covered.
- Cases where security has been invoked by the lender on account of default by the company
- Only specific pledge of securities and not general or residual charge on all securities.

In accordance with the 2013 Act, companies are required to create a charge in case a company obtains loan by pledge of securities. Companies would need to maintain documents related to charges created including any modification thereof including loan agreements/ other documents such as term sheets for the purpose of verification by an auditor.



Conclusion

CARO 2020 with its new bundle of clauses aims to provide a comprehensive position of the loans and advances taken or given by a company. Some of the key reporting requirements introduced relates to:

- Loans or advances in the nature of loans which are either repayable on demand or do not specify any terms or period of repayment with a specific disclosure on such loans given to promoters or related parties.
- Specific reporting on evergreening of loans i.e. granting new loans for repayment of old loans in order to prevent a default.
- Application of terms loans for the purpose for which those have been raised, if not then specific reporting on amount so diverted.
- Funds taken to meet the obligations of subsidiaries, associates or joint ventures along with those taken on pledge of securities held by the company in subsidiaries, associates or joint ventures.
- Default in repayment of loans/ borrowings by a company to any lender or declared as a willful defaulter.

These reporting requirements cast an additional responsibility on the management of the company to ensure that all documents and relevant processes are in place for an auditor to verify and report accordingly.

03

Regulatory updates

SEBI proposed amendments to the Listing Regulations

On 11 September 2020, the Securities and Exchange Board of India (SEBI) issued a consultation paper on 'Review of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations)' and proposed various amendments to the Listing Regulations. These are aimed to strengthen corporate governance practices and disclosure requirements by listed companies along with harmonising the provisions of the Listing Regulations with that of the Companies Act, 2013 (2013 Act).

Key recommendations envisaged in the consultation paper are as follows:

- **Applicability of provisions basis market capitalisation:** It has been proposed that the provisions of the Listing Regulations which become applicable to listed entities on the basis of market capitalisation criteria will continue to apply to such listed entities even if they fall below such thresholds.
- **Applicability of corporate governance norms:** Currently, certain corporate governance provisions are applicable to listed entities with paid-up equity share capital of more than INR10 crore and net worth of more than INR25 crore as on the last day of the previous financial year.

  It has been proposed that provisions of the Listing Regulations will continue to remain applicable to a listed entity irrespective of subsequent changes in equity share capital or net worth of such an entity.
- **Disclosure of financial statements:** Currently, a listed entity is required to disclose to the stock exchange(s) the outcome of board meeting including financial results within 30 minutes of the conclusion of the board meeting.

  It has been proposed that the listed entity should disclose the financial results to the stock exchange(s) within 30 minutes of the approval of the board of directors.
- **Dividend distribution policy:** It has been proposed to extend the requirement to formulate and disclose the dividend distribution policy in the annual reports and websites to top 1,000 listed entities by market capitalisation (currently applicable to top 500 listed entities).
- **Quarterly compliance report:** The timeline for filing of a quarterly compliance report on corporate governance as required under Regulation 27(2) of the Listing Regulations with the recognised stock exchange(s) has been proposed to be extended to 21 days from close of the quarter (currently, required to be submitted within 15 days from the close of the quarter).

Comments on the recommendations can be submitted up to 11 October 2020.

(Source: SEBI's consultation paper on 'Review of SEBI (Listing Obligation and Disclosure Requirements) Regulation,2015' dated 11 September2020)

SEBI issued system driven disclosures under PIT regulations

Background

Currently, Regulation 7(2) of the SEBI (Prohibition of Insider Trading) Regulations, 2015 (PIT Regulations) requires a promoter, an employee and a director of a listed company to disclose about the transaction relating to the acquisition or disposal of securities to the company within two trading days, if the value of such transaction exceeds INR10 lakh over any calendar quarter. Also, a listed company is required to notify the particulars of such trading to the stock exchange within two trading days of receipt of the disclosure of such information.

New development

SEBI through a circular dated 9 September 2020 has decided to implement system driven disclosures for member(s) of promoter group and designated person(s) in addition to the promoter(s) and director(s) of a company (referred to as 'entities') under Regulation 7(2) of the PIT Regulations.

As per the circular, system driven disclosures under PIT Regulations would pertain to trading in equity shares and equity derivative instruments i.e. futures and options of the listed company (wherever applicable) by the entities. The process for implementation of the system has been specified in the circular.

As per the process, listed companies should provide the information including Permanent Account Number (PAN) of their promoters, designated person(s) and director(s) to the designated depository in a format and manner prescribed by the depositories within 10 days from the date of this circular. Any subsequent update in the details of entities need to be updated by the listed company on the same day.

Further, the system would continue to run parallel with the existing system i.e. entities would continue to independently comply with the disclosure obligations under PIT Regulations as applicable to them till 31 March 2021.

(Source: SEBI circular no. SEBI/HO/ISD/ISD/CIR/P/2020/168 dated 9 September2020)

The Companies (Amendment) Act, 2020 received Presidential assent

On 28 September 2020, the Companies (Amendment) Act, 2020 (Amendment Act, 2020) received the assent of the President of India. The Amendment Act, 2020 make significant amendments to the provisions of the 2013 Act. Some of the key amendments relates to the following:

- **Exclusion of listed companies:** The Amendment Act, 2020 empowers Central Government (CG) to exclude companies issuing specified classes of securities from the definition of a listed company in consultation with SEBI.
- **Direct listing in foreign jurisdictions:** The Amendment Act, 2020 empowers CG to permit certain class of public companies to list their securities on permitted stock exchanges in permissible foreign jurisdictions or such other jurisdictions as may be prescribed.
- **Financial results by unlisted companies:** The Amendment Act, 2020 empowers CG to require prescribed class of unlisted companies to prepare the financial results of the company on such periodical basis and in such form as may be prescribed. It may also require such companies to obtain approval of the board of directors and complete audit or limited review of the periodical financial results in such manner as may be prescribed.
- **Corporate Social Responsibility (CSR):** The Amendment Act, 2020 exempts companies with a CSR liability of up to INR50 lakh from the requirement of constituting a CSR committee under the 2013 Act. In such cases, functions of the committee would be discharged by the board of directors of the company. Also, it allows a company which spends an amount in excess of the prescribed amount of two per cent on CSR activities, to set-off excess amount against the requirement to spend for such number of succeeding financial years and in such manner, as may be prescribed.
- **Remuneration to independent directors:** As per the Amendment Act, 2020, if a company has no profits or its profits are inadequate, then an independent director may receive remuneration, exclusive of any fees payable under Section 197(5) of the 2013 Act, in accordance with the provisions of Schedule V of the 2013 Act.

The Amendment Act, 2020 will come into force on such date as the CG may, by notification in the Official Gazette, appoint. Different dates may be appointed for different provisions of the Amendment Act, 2020 and any reference in any such provision to the commencement of the Amendment Act, 2020 shall be construed as a reference to the coming into force of that provision.

(Source: The Companies (Amendment) Act, 2020 issued by the Ministry of Law and Justice on 28 September 2020)

Relaxations under the Companies Act, 2013

- **Conduct of board meetings through VC:** Board meetings to discuss the matters specified in Rule 4 of the Companies (Meetings of Board and its Powers) Rules, 2014 (i.e. those relating to approval of financial statements, board's report, prospectus, etc.) can be held through Video Conferencing (VC) or Other Audio-Visual Means (OAVM) up to 31 December 2020 (earlier allowed up to 30 September 2020).

  (Source: MCA notification no. G.S.R. 590(E) dated 28 September 2020)

- **Enrolment in the data bank of independent directors:** Every individual who has been appointed as an independent director in a company as on 1 December 2019 can apply online to the Indian Institute of Corporate Affairs (institute) up to 31 December 2020 (earlier up to 30 September 2020) for inclusion of his/her name in the data bank maintained by the institute.

  (Source: MCA notification no. G.S.R. 589(E) dated 28 September 2020)

- **Conduct of EGMs through VC:** The MCA through a circular dated 28 September 2020 has extended the timeline for conduct of Extraordinary General Meetings (EGMs) by companies through VC/OAVM or transact items through postal ballot in accordance with the framework provided in the circulars dated 8 April 2020, 13 April 2020 and 15 June 2020 up to 31 December 2020.

  (Source: MCA general circular no. 33/2020 dated 28 September 2020)

- **Companies Fresh Start Scheme, 2020:** The Companies Fresh Start Scheme, 2020 (the scheme) introduced by the MCA in March 2020 permits a defaulting company to file belated documents in the MCA-21 registry which were due for filing on any given date in accordance with the provisions of the scheme. It also provides an opportunity to inactive companies to get their companies declared as 'dormant company' under Section 455 of the 2013 Act by filing a simple application.

  The scheme was made applicable from 1 April 2020 up to 30 September 2020.

  Relaxation

  The MCA has extended the applicability of the scheme up to 31 December 2020.

  (Source: MCA general circular no. 30/2020 dated 28 September 2020)

Extension of timeline for holding AGM

As per the provisions of Section 96(1) of the 2013 Act, the Registrar of Companies (ROC) may, for any special reason, extend the time within which any Annual General Meeting (AGM) (other than the first AGM) should be held, by a period not exceeding three months.

Accordingly, the Ministry of Corporate Affairs (MCA) (ROC of various states) have issued an order on 8 September 2020 to extend the time for holding AGM for the financial year ended 31 March 2020 by three months from the due date by which AGM ought to have been held in accordance with the 2013 Act. Further, it has been clarified that the companies are not required to file application in Form GNL-1 for seeking this extension.

Additionally, the extension would cover applications filed in Form GNL-1 for the extension of AGM for the financial year ended 31 March 2020 which are yet to be approved and also applications which were rejected.

(Source: ICAI announcement dated 10 September 2020)

Amendments to the Deposit Rules

The MCA through a notification dated 7 September 2020 has issued certain amendments to the Companies (Acceptance of Deposits) Rules, 2014 (Deposit Rules). As per the amendments, an amount of INR25 lakh or more received by a start-up company by way of convertible note which is convertible into equity shares or repayable **within 10 years** (earlier five years) from the issue date would not be treated as a deposit.

Additionally, a private company which is a start-up for **10 years** (earlier five years) from the date of its incorporation can accept/renew deposits from its members in excess of the specified limits[1].

(Emphasis added to highlight the changes)

The amendments are effective from 7 September 2020.

(Source: MCA notification no. G.S.R 548(E) dated 7 September 2020)

Amendments relating to annual return of a company

The Companies (Amendment) Act, 2017 made certain amendments to the provisions relating to annual return of a company under the 2013 Act. However, these were not notified by the government. On 28 August 2020, MCA notified one of the amendments from the Companies (Amendment) Act, 2017 which requires a company to place a copy of the annual return on its website, if any, and the web link of such annual return to be disclosed in the board's report.

Additionally, MCA has made an amendment to the Companies (Management and Administration) Rules, 2014 effective 28 August 2020. As per the amendment, a company is not required to attach the extract of the annual return with the board's report in Form No. MGT-9, in case the web link of such annual return has been disclosed in the board's report.

(Source: MCA notification no. S.O.2920(E) and G.S.R.538(E) dated 28 August 2020)

Extension of timeline for filing cost audit report

Currently, a cost auditor is required to forward his/her duly signed report to the Board of Directors (BoDs) of the company within a period of 180 days from the closure of the financial year as per the provisions of the Companies (Cost Records and Audit) Rules, 2014 (Cost Audit Rules). Further, the company is required to submit the report to the Central Government within a period of 30 days from the date of receipt of a copy of the cost audit report in Form CRA-4.

Relaxation

The MCA through a circular dated 10 September 2020 has clarified that the submission of the cost audit report for the financial year ended 31 March 2020 by the cost auditor to the BoDs up to 30 November 2020 would not be construed as violation of the provisions of the Cost Audit Rules.

1. Amount of deposits from members together with the amount of other deposits outstanding as on the date of acceptance or renewal of deposits exceeding 35 per cent of the aggregate of the paid-up share capital, free reserves and securities premium account of the company.

Accordingly, the timeline for filing of e-Form CRA-4 for the year ended 31 March 2020 would be 30 days from date of the receipt of copy of the cost audit report. However, if a company has availed extension of time for holding AGM, then e-Form CRA-4 may be filed within the timeline as specified under proviso to Rule 6(6) of the Cost Audit Rules.

(Source: MCA general circular no.29/2020 dated 10 September 2020)

Revision to the Long Form Audit Report (LFAR)

The Reserve Bank of India (RBI) through a notification dated 5 September 2020 has issued revised LFAR formats for Statutory Central Auditors (SCA) and branch auditors along with an additional questionnaire applicable to specialised branches.

The revised LFAR formats are required to be put into operation for the period covering FY2020-21 and onwards. Accordingly, the LFAR format and other instructions issued through the RBI circular[2] dated 17 April 2002 has been repealed.

With regard to the operational issues relating to submission of LFAR, RBI has advised the following:

- Timely receipt of LFARs from the auditors should be ensured.
- LFAR on the bank should be placed before the Audit Committee of Board (ACB)/Local Advisory Board (LAB) of the bank indicating the action taken or proposed to be taken for rectification of the irregularities, if any, mentioned in the report.
- A copy of each of the LFAR (i.e. for the bank/all Indian offices of foreign bank as a whole) and the relative agenda note together with the board's views or directions should be forwarded to the concerned Senior Supervisory Manager (SSM) in the Department of Supervision, RBI within 60 days of submission of the LFAR by the statutory auditors.

(Source: RBI notification no. RBI/2020-21/33 dated 5 September 2020)

Resolution framework for COVID-19-related stress - Financial parameters

Background

The RBI through a notification dated 6 August 2020 had introduced a 'Resolution Framework for COVID-19-related Stress' (the framework) with an aim to mitigate the impact of the COVID-19 pandemic on the ultimate borrowers[3].

The framework envisaged constitution of an expert committee by RBI to make recommendations on the required financial parameters with sector specific benchmark ranges for such parameters to be factored in the resolution plans in respect of eligible borrowers. RBI constituted the expert committee under the chairmanship of Mr. K.V. Kamath on 7 August 2020. The Committee was required to submit its recommendations on the financial parameters to the RBI which, in turn, was required to notify the same along with modifications, if any, in 30 days.

On 4 September 2020, the expert committee submitted its recommendations to RBI.

New development

Basis the recommendations of the expert committee, RBI through a circular dated 7 September 2020 has issued key ratios which are mandatorily required to be considered by the lending institutions while finalising the resolution plans in respect of eligible borrowers under the framework.

Those are as follows:

a. Total Outside Liabilities/Adjusted Tangible Net Worth (TOL/ATNW)
b. Total debt/EBITDA[4]
c. Current ratio
d. Debt service coverage ratio
e. Average debt service coverage ratio.

2. Circular no. DBS.CO.PP.BC.11/11.01.005/2001-2002
3. Circular no. RBI/2020-21/16-DOR.No.BPBC/3/21.04.048/2020-21
4. Earnings Before Interest, Tax, Depreciation and Amortisation

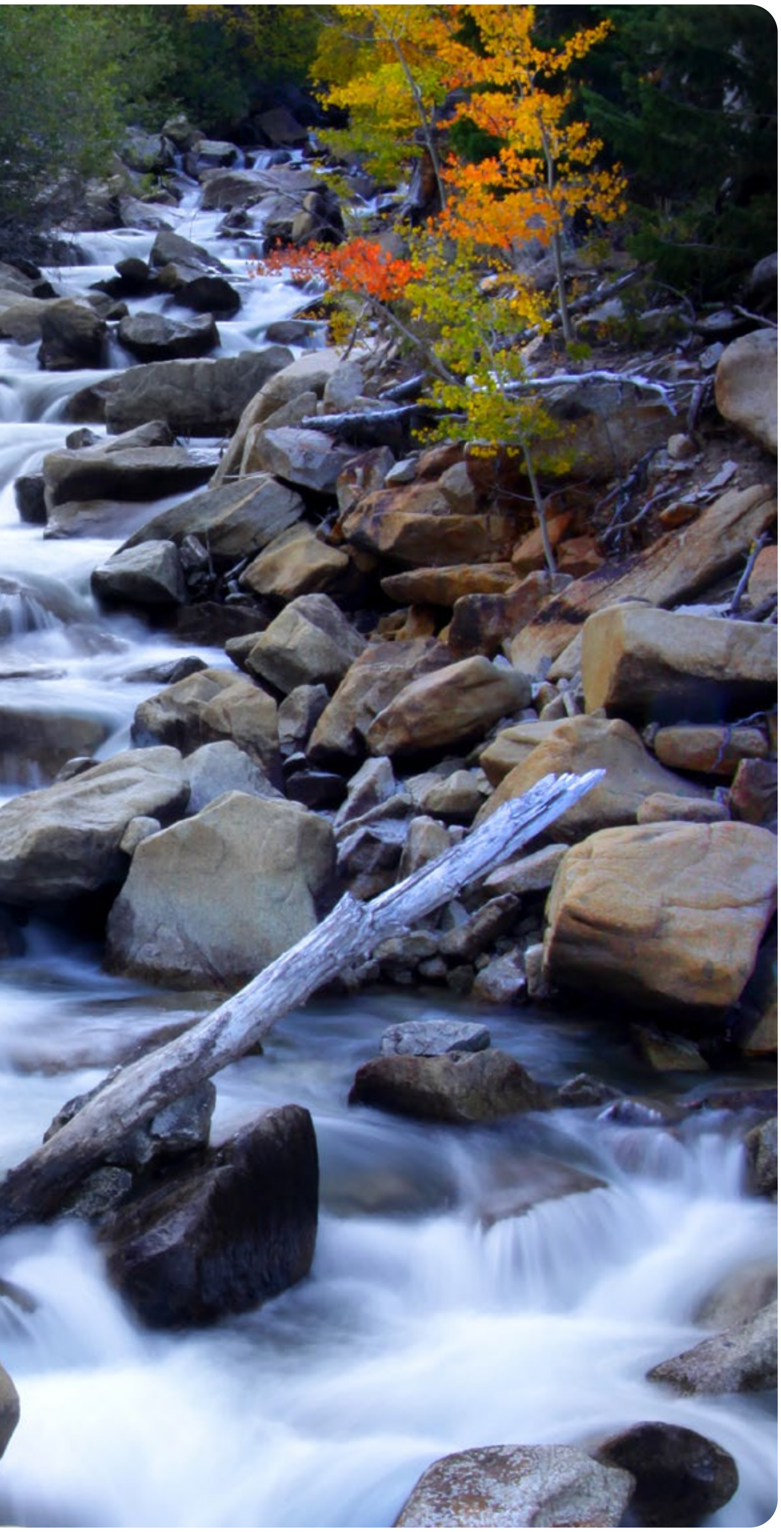
The circular also specifies sector-specific thresholds for each of the above key ratios that should be considered by the lending institutions in the resolution assumptions with respect to an eligible borrower.

In addition to the key ratios and the sector-specific thresholds, lending institutions can consider other financial parameters while finalising the resolution assumptions.

Other key requirements relating to financial parameters are as follows:

- The resolution plan should take into account pre-COVID-19 operating and financial performance of the borrower and resultant impact on its operating and financial performance at the time of finalising the resolution plan in order to assess the cashflows in subsequent years, while stipulating appropriate ratios in each case.
- Lending institutions may adopt a graded approach depending on the severity of the impact on the borrowers which may include classification of the impact on borrowers into mild, moderate and severe.
- Lending institutions are expected to ensure compliance to TOL/ATNW agreed as per the resolution plan at the time of implementation itself. In all cases, TOL/ATNW and other key ratios have to be maintained as per the resolution plan by 31 March 2022 and on an ongoing basis thereafter.

(Source: RBI circular no. RBI/2020-21/34 dated 7 September 2020)



Amendment in 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.

Amendment

The RBI through a notification dated 1 September 2020 has 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 which should be reviewed thereafter.

(Source: RBI notification no. RBI/2020-21/29 dated 1 September 2020)

ICAI publications

Compendium of Indian Accounting Standards (Year 2020-2021)

The Institute of Chartered Accountants of India (ICAI) has issued a compendium of Indian Accounting Standards (Ind AS) (Volume I and Volume II) which provides a comprehensive literature for all those entities that prepare financial statements under Ind AS. The compendium contains updated Ind AS applicable for accounting period beginning 1 April 2020 including amendments to Ind AS made by MCA on 24 July 2020.

ICAI has also issued related guidance material and a publication which highlights differences between Ind AS and International Financial Reporting Standards (IFRS) along with the rationale for such differences.

(Source: Compendium of Indian Accounting Standards (Ind AS as on 1 April 2020) issued by ICAI on 25 August 2020 and ICAI publication on 'Major differences between Ind AS and IFRS and reason for the differences' issued on 27 August 2020)

Guidance note on report under Section 92E of the Income-Tax Act, 1961

Recently, ICAI has issued a Guidance Note (GN) on report under Section 92E of the Income-Tax Act, 1961 (IT Act) (Revised 2020) relating to transfer pricing. The revised GN incorporates all amendments made up to Finance Act, 2020 and provide an insight into the intricate issues while discharging the reporting requirements under Section 92E of the IT Act.

(Source: 'Guidance Note on Report under section 92E of the Income-Tax Act, 1961' issued by ICAI on 20 August 2020)

Exposure draft of guidance note on accrual basis of accounting

The ICAI has issued an exposure draft of GN on accrual basis of accounting. The GN highlights the need for accrual basis of accounting and provides guidance in respect thereof. It also provides guidance in respect of transition from cash basis to accrual basis of accounting.

The exposure draft is open for comments up to 18 October 2020.

(Source: Exposure draft of 'Guidance Note on accrual basis of accounting' issued by ICAI on 18 September 2020)

IBOR reform – Phase 2 amendments issued by IASB

The IASB has finalised its response to the ongoing reform of Inter-Bank Offered Rates (IBOR) and other interest rate benchmarks and has issued amendments to IFRS 9, *Financial Instruments,* International Accounting Standard (IAS) 39, *Financial Instruments: Recognition and Measurement,* IFRS 7, *Financial Instruments*: *Disclosures,* IFRS 4, *Insurance Contracts* and IFRS 16, *Leases.*

The amendments focus on the effects on financial statements when a company replaces the old interest rate benchmark with an alternative benchmark rate as a result of the reform.

The amendments in the final phase relate to:

- **Changes to contractual cash flows:** A company will not have to derecognise or adjust the carrying amount of financial instruments for changes required by the reform, but will instead update the effective interest rate to reflect the change to the alternative benchmark rate
- **Hedge accounting:** A company will not have to discontinue its hedge accounting solely because it makes changes required by the reform, if the hedge meets other hedge accounting criteria and
- **Disclosures:** A company will be required to disclose information about new risks arising from the reform and how it manages the transition to alternative benchmark rates.

These amendments are effective for annual reporting periods beginning on or after 1 January 2021 with early adoption permitted.

(Source: IASB announcement dated 27 August 2020)

Discussion paper on fraud and going concern in an audit of financial statements

On 15 September 2020, the International Auditing and Assurance Standards Board (IAASB) has issued a discussion paper on *'Fraud and going concern in an audit of financial statements: Exploring the differences between public perceptions about the role of the auditor and the auditor's responsibilities in a financial statement audit'.*

The discussion paper sets out the issues and challenges related to the expectation gap (the difference between what users of the financial statements expect and the financial statements audit) and explores some possible actions that the IAASB could undertake to help narrow the expectation gap.

The discussion paper is open for comments up to 12 January 2021.

(Source: IAASB announcement dated 15 September 2020)

KPMG in India's IFRS institute

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

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

First Notes

Proposal for top 1,000 listed companies to adopt BRSR voluntarily for FY20-21

26 August 2020

On 11 August 2020, MCA has issued the report of the committee on Business Responsibility Report (BRR). In this report, the committee has prescribed new format for Business Responsibility and Sustainability Report (BRSR) and made recommendations relating to its implementation.

Basis recommendations of the committee, on 18 August 2020, SEBI has also issued a consultation paper and proposed that the BRSR format, as recommended by the committee, should be made applicable to top 1,000 listed companies by market capitalisation.

This issue of First Notes aims to provide an overview of the recommendations made by the MCA committee in its report and proposals made by SEBI in its consultation paper.

Voices on Reporting (VOR)

KPMG in India is pleased to present Voices on Reporting (VOR) - a series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

KPMG in India has scheduled a VOR webinar on 7 October 2020 to discuss key financial reporting and regulatory matters that are expected to be relevant for stakeholders for the quarter ended 30 September 2020.

For registration details, please click here.

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