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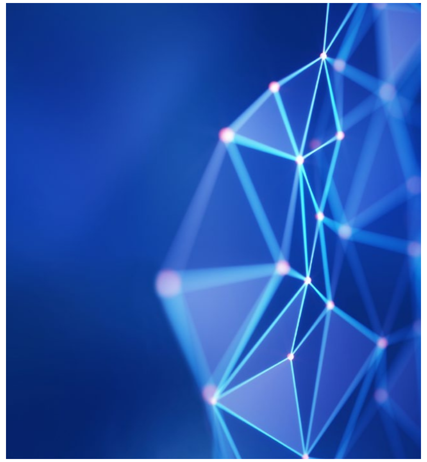

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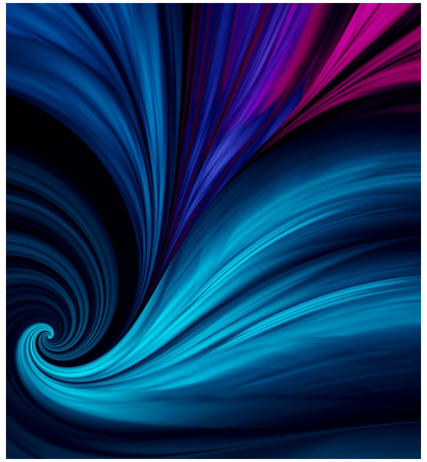

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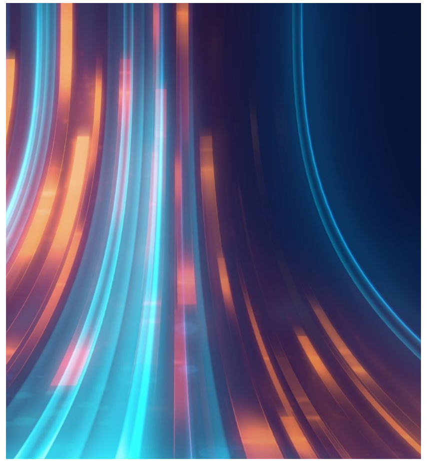

Foreword

As the corporate reporting evolves, there has been a continuous rise in demand for non-financial information and disclosures by companies depicting long-term value creation, sustainability reporting, corporate social responsibilities and alike. Such information facilitates informed decision making by various stakeholders, in particular investors. Companies report such non-financial information in various forms (voluntarily or as required by the statue) such as sustainability or Environmental, Social and Governance (ESG) reporting, integrated reporting, reporting on corporate social responsibility, greenhouse gas statements, and service performance reporting in the public sector (commonly referred to as 'Extended External Reporting (EER)'). There is a corresponding increase in demand for assurance engagements on such extended types of reporting. International Standard on Assurance Engagement (ISAE) 3000, *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information issued* by the International Auditing and Assurance Standards Board (IAASB) establishes requirements and other explanatory material specific to reasonable and limited assurance attestation engagements (including application to direct engagements) other than audits or reviews of historical financial information. Recently, IAASB has also issued 'Non-Authoritative Guidance on applying ISAE 3000 (Revised) to EER assurance engagements'.

In this edition of Accounting and Auditing Update (AAU), we aim to highlight key considerations for the management/preparers in preparation of the EER report as envisaged in the guidance issued by IAASB.

In response to the growing interest of investors, ESG is also quickly moving to the forefront of the regulators including U.S. Securities and Exchange Commission's (SEC) agenda. This is apparent from the recent statement issued by the Acting Chair of the SEC, Allison Herren Lee, which indicated that the SEC Division of Corporation Finance will enhance its focus on climate-related disclosure in public company filings. Additionally, the staff of the SEC Division of Corporation Finance has issued guidance about disclosure considerations for Special Purpose Acquisition Companies (SPACs) in connection with their Initial Public Offering (IPO) and subsequent business combination transactions. Our article covers these and other accounting and financial reporting developments under the US GAAP that would be relevant for the companies in the current period or near term.

There have been various regulatory developments in India and internationally during the month. The Ministry of Corporate Affairs (MCA) has clarified that spending of funds earmarked for Corporate Social Responsibility (CSR) for setting up makeshift hospitals and temporary COVID-19 care facilities would be an eligible CSR activity under Schedule VII of the Companies Act, 2013. Internationally, the International Accounting Standards Board (IASB) has issued an exposure draft to seek comments on the proposed amendments to IFRS 13, *Fair Value Measurement* and IAS 19, *Employee Benefits* consequent to the application of IASB's proposed guidance explaining IASB's approach of modification of the disclosure requirements in IFRS. Our regulatory updates section provides an overview of these and other financial reporting updates in India and internationally.

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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CHAPTER 1

IAASB's new guidance on EER Assurance Engagements

This article aims to:
Provide an overview of the guidance issued by IAASB regarding assurance engagements such as sustainability or Environmental, Social and Governance (ESG) reporting, integrated reporting, reporting on corporate social responsibility, etc.

Introduction

Over the past decade, corporate reporting around the world has continuously been evolving. Investors and other stakeholders in the corporate ecosystem have increased their focus on non-financial information and disclosures relating to long-term value creation, sustainability reporting and the corporate social responsibilities reported by a company.

Many companies across the world provide Extended External Reporting (EER) e.g. sustainability or Environmental, Social and Governance (ESG) reporting, integrated reporting, reporting on corporate social responsibility, greenhouse gas statements, and service performance reporting in the public sector.

Currently, the EER reports are prepared under regulatory requirements or voluntary frameworks in accordance with the standards or guidance issued by organisations ranging from sector specific industry bodies to national or international standard setters.

As reporting evolves, there is a corresponding increase in demand for assurance engagements on such extended types of reporting.

ISAE 3000 – An assurance standard

The International Auditing and Assurance Standards Board (IAASB) issued the International Standard on Assurance Engagement (ISAE) 3000, *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information*. The ISAE 3000 was the first standard issued by a standard setter which provided guidance to practitioners over assurance engagements other than audits or reviews of historical financial information. The standard establishes requirements and application and other explanatory material specific to reasonable and limited assurance attestation engagements (including application to direct engagements) other than audits or reviews of historical financial information.

However, certain challenges were highlighted to IAASB regarding ISAE 3000 (Revised) in EER assurance engagements.

Non-Authoritative Guidance on applying ISAE 3000 (Revised) to EER assurance engagements – an overview

Recently, on 6 April 2021, the IAASB issued 'Non-Authoritative Guidance on applying ISAE 3000 (Revised) to EER assurance engagements'. This guidance responds to 10 key stakeholder identified challenges commonly encountered in assurance engagements other than audits or reviews of historical financial information. Two additional non-authoritative support material viz. 'Credibility and trust model relating to EER reporting' and 'Illustrative examples of selected aspects of EER assurance' have also been issued by the IAASB.

While the intended audience of the guidance is practitioners carrying out EER assurance engagements, other parties such as preparers and users of EER reports or regulators may take aid from the guidance.

Management is responsible for establishing suitable criteria for preparing the EER in accordance with an applicable framework. User's perception of the credibility of an EER report can be influenced by the qualities and transparency of the EER framework used in preparation. Similarly, a sound EER framework guides management in producing an EER report that is effective in communicating and gives users confidence of end use.

Key consideration for the management/preparer

In the section below, we have highlighted some of the key considerations which would enable management/preparers of EER report in identification of relevance and suitability of potential process/procedures or systems, competence of assurance provider, forms of presentation of EER information, expectation over type of assurance in terms of limited or reasonable, diverse underlying subject matters, etc.:

a. **Applying appropriate competence and capabilities:** Preparers of the EER should have the subject matter competence since EER reporting can be complex comprising of both qualitative and quantitative disclosures. Also, the management and Those Charged With Governance (TCWG) should evaluate the competence of the EER assurance team and their skills and techniques in the underlying subject matter and their measurement or evaluation process. The more complex the engagement, the more necessary it would be for the management to consider the work of practitioners and specialists in performing the assurance engagement.

   Without reasonable oversight and governance, EER may not be viewed in the same lens as reporting financial performance. Lack of oversight function by TCWG may lead to risks of material misstatements of fraud or errors.

b. **Selection of suitable criteria:** There exists numerous possible EER frameworks (such as the IIRC[1], GRI[2], SASB[3] etc.), criteria or bases of preparation for each underlying subject matter. The management should assess and evaluate to select the most suitable reporting criteria including appropriate assumptions and methods to be used. This may pose challenge when the EER subject matter information is voluntarily reported without regulatory oversight. It is important that the criteria a company chooses for EER should also be relevant and consistent with those generally recognised in the context of the company's sector or industry. Further, the criteria selected is required to be complete so that the intended user is able to make informed decisions by having access to subject matter information in the context of the circumstances of the entity and the purpose of the EER report. Other factors to keep in mind in selecting a suitable criteria include reliability, neutrality and understandability of the criteria.

c. **Recognise unusual circumstances or omissions of information:** EER reporting frameworks are still evolving and allowing for different interpretations or applications of the criteria. While an entity's systems, processes and controls may still be developing or there may be less participation by management around EER related matters as compared to financial performance and strategy, robust process may be implemented by the management to prevent/detect/correct misstatements of information forming part of EER including omissions.

d. **Determining the scope of EER assurance engagement:** The company needs to clearly define the scope of the EER engagement including that there is a rational purpose to the engagement. In the initial stages of an entity's EER reporting, the company may not be able to provide assurance on all of the information included in the EER report. The company (preparer) may propose a scope for the EER assurance engagement that increases from period to period or one that varies in a 'rolling program' of assurance. Scope of the EER reporting can vary, for example - the whole EER report, specific topics or areas of information within the EER report (for example environmental or social matters) or individual items within specific topics or areas of information within the EER report (for example waste generated within the 'environmental' topic or area, or gender pay within the 'social' topic).

e. **Process to identify reporting topics:** In certain cases, companies may have to deal with absence of an EER framework to follow or insufficient detailed direction in the framework to make reliable judgements about what reporting topics to address in an EER report. In those cases, the company ordinarily should establish a process to decide how to make judgements about what to include in their EER information considering the information needs of intended users. The entities may consider following process to identify reporting topics:

   i. Identify purpose, intended users and framework
   ii. Develop list of reporting topics that may potentially be relevant, complete and neutral
   iii. Consider and document factors that may be relevant, complete and neutral in the light of matters such as interest and impact
   iv. Identify reporting topics
   v. Make criteria available and where required, disclose details of the process.

   Intended users may find it helpful to understand the process the preparer has been through to identify reporting topics, even if disclosure of the process is not required by the EER framework. It is important that the criteria to identify reporting topics are made available to the intended users along with other applicable criteria.

1. IIRC – International Integrated Reporting Council
2. GRI – Global Reporting Initiative
3. SASB – Sustainability Accounting Standards Board

f. **Internal control and governance matters:** A company's process to prepare EER information needs to provide a reasonable basis for the subject matter information. The company may involve the use of IT to collect or process data and information. As a company gains more experience in EER reporting, the company's internal control may become more sophisticated and new technologies may be used to record, process and report their EER information. The nature of the company's processes, controls and records in the company's system of internal control may vary with the size and complexity of the company.

   The governance structure arrangements of a company preparing EER report over the management and reporting of its EER information may be less developed or less 'embedded' into its operations as compared to managing and reporting its financial performance. Therefore, it is important that the company establishes a formal level of the oversight and governance arrangements including the process of risk assessment to monitor the system of internal control.

g. **Qualitative and future-oriented EER information:** Qualitative information may be future-oriented or historically-oriented, and future-oriented information may be expressed in either qualitative or quantitative terms. A number of challenges may also arise in the context of providing evidence for qualitative subject matter information because it may be difficult for the entity's process to prepare the EER information to capture data and information about the subject matter information. Although the process to prepare the subject matter information and related controls, may be sufficient to provide the company with a reasonable basis for the subject matter information, it may not be sufficient to provide the practitioner with the evidence needed to support the practitioner's conclusion.

h. **The assurance report:** The expression of an assurance conclusion is the objective of the assurance engagement. It is designed to enhance the degree of confidence of the intended users about the subject matter information. The standard provides guidance on how practitioners may communicate effectively to the users of EER report. This is done by issuing a written assurance report that complies with the requirements of ISAE 3000 so that users can understand to whom the assurance report has been issued, what is the subject of the EER assurance engagement, how the engagement was performed, what was the underlying subject matter and finally what has been the assurance conclusion. The guidance provides illustrative formats of various types of assurance reports for reference of companies and practitioners.

Way forward

The IAASB have advanced towards a significant step in providing non-authoritative guidance on applying ISAE 3000 to EER engagements. The guidance provided by IAASB will help preparers, practitioner and users of EER report to build trust and credibility in relation to the EER reports and assurance reports thereof. It would further help in providing a consistent framework and open and transparent way of communicating with various stakeholders in the ecosystem. The guidance and the supporting material also provide illustrative examples for a user in the practical application of ISAE 3000 to EER reports and assurance engagements.

In India, recently on 25 March 2021, the Securities and Exchange Board of India (SEBI) in its board meeting approved amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations). The amendment requires the new report Business Responsibility and Sustainability Report (BRSR) to be applicable to the top 1,000 listed entities instead of existing Business Responsibility Report (BRR) on a voluntary basis for financial year 2021- 22 and on a mandatory basis from financial year 2022-23 in the prescribed format. Large corporates in India and practitioners are likely to benefit from the new guidance provided by IAASB in seeking assurance on their EER reports.

CHAPTER 2

US GAAP updates - SEC's focus on ESG and SPAC disclosures

This article aims to:
Provide an overview of the recent accounting and financial reporting developments under the US GAAP relevant for the companies in the current period or near term.

In this article, we shall focus on some of the guidance/disclosures released by the U.S. Securities and Exchange Commission (SEC) relating to climate and Environmental, Social and Governance (ESG) disclosures, Special Purpose Acquisition Companies (SPACs) related disclosures, clarifying what is income in connection with the income test at the time of disposition of business and Public Company Accounting Oversight Board's (PCAOB's) conversation with the audit committee chairs of companies during 2020 inspection cycle.

Climate and ESG related disclosures

ESG refers to a framework to integrate environmental, social and governance risks and opportunities into a company's strategy. ESG is playing an increasingly important role in the strategy and operations of companies, and investment decisions are increasingly being driven by ESG metrics.

On 24 February 2021, SEC Acting Chair, Allison Herren Lee issued a statement which indicated that the SEC Division of Corporation Finance will enhance its focus on climate-related disclosure in public company filings. Specifically, the SEC staff will review the extent to which a company's disclosures address the 2010 interpretive guidance on climate change-related disclosures, assess companies' compliance with disclosure obligations under the federal securities laws, and develop an understanding of how the market is managing climate-related risk. The staff will use these insights to update the 2010 guidance.

Following Lee's statement, on 4 March 2021, the SEC announced the creation of a Climate and ESG Task Force in the Division of Enforcement that will develop initiatives to identify ESG-related misconducts. The task force's initial focus will be on material gaps or misstatements in a company's disclosures on climate risks and ESG issues under existing rules. The task force will also analyse disclosure and compliance issues relating to investment advisers' and funds' ESG strategies.

The SEC's announcement is a call to action for registrants to refresh their understanding of the 2010 disclosure guidance-which explains how the Regulation S-K requirements apply to climate-related matters-and to carefully analyse the quality of their disclosures.

Current reporting requirements under 2010 SEC's interpretive guidance

The guidance released in 2010 highlighted various Regulation S-K disclosure requirements that may be relevant to climate-related matters. These disclosures summarise the risks, events or circumstances that are material to an investor's understanding of the registrant's business, including the following:

- **Item 101, *Description of Business***: It requires a narrative description of the business, including disclosure of the material effects that compliance with federal, state and local environmental laws may have on the capital expenditures, earnings and the registrant's competitive position.
- **Item 103, *Legal Proceedings***: It requires a description of material pending legal proceedings, including matters arising from federal, state or local laws intended to protect the environment.
- **Item 105, *Risk Factors***: It requires disclosure of the material factors that make an investment in the registrant speculative or risky.
- **Item 303, *Management's Discussion and Analysis of Financial Condition and Results of Operations***: It requires disclosure of known trends or uncertainties that have had or are reasonably likely to have a material impact on the registrant's continuing operations and known material events and uncertainties that are reasonably likely to cause the financial information not to be indicative of future operating results or financial condition.

Potential impact of disclosure requirements

The SEC staff cited following areas where climate change may require disclosure as per its 2010 guidance:

- **Impact of legislation and regulation:** A registrant should consider the impact of existing and pending climate-change laws and regulations. If material, it should also consider the difficulties of assessing the timing and effect of pending legislation and regulation; both positive and negative consequences of actual or pending legislation or regulatory actions should be considered. Some of these possible consequences include:
  - Costs to purchase, or profits from sales of, allowances or credits under a cap-and-trade system
  - Costs required to improve facilities and equipment to reduce emissions to comply with regulatory limits or to mitigate the financial consequences of a cap-and-trade regime
  - Changes to profit or loss arising from increased or decreased demand for goods and services produced by the registrant arising directly from legislation or regulation, and indirectly from changes in costs of goods sold.
- **Impact of international accords:** A registrant should consider the risks or effects of international accords and treaties related to climate change. The disclosure requirements for foreign legislation and regulation are the same as for domestic and should include both negative and positive consequences.

  For example, the Paris Climate Agreement was adopted by 196 countries, but each country is responsible for developing its own plans for climate action. This means that companies with multinational operations should fully understand the environmental actions wherever they operate to evaluate possible negative or positive consequences.
- **Indirect consequences of regulation or business trends:** A registrant should evaluate the legal, technological, political and scientific developments related to climate change, or other trends in the business environment that may directly or indirectly pose risks or create new opportunities. Some of the indirect negative consequences or opportunities might include:
  - Decreased demand for goods that result in significant greenhouse gas emissions.
  - Increased demand for goods that result in lower emissions than competing products
  - Increased competition to develop innovative new products.

  Companies need to consider where the indirect consequences or opportunities should be disclosed. For example, if a company plans to take advantage of potential opportunities through material acquisitions of plant or equipment, disclosure may be required by Item 101. The potential impact of business trends or risks may need to be disclosed in Items 105 or 303.
- **Physical impact of climate change:** Significant physical effects of climate change e.g., severity of the weather, rising sea levels, the arability of farmland, water availability and quality, scarcity of resources have the potential to affect a registrant's financial condition and business.

  Companies should consider both the actual and potential impact of environmental matters stemming from climate change to their business and operations including personnel, physical assets, and supply and distribution chains.

SPACs – Disclosure considerations

A SPAC is a company with no operations that offers securities for cash and places substantially all the offering proceeds into a trust or escrow account for future use in the acquisition of one or more private operating companies. Following its Initial Public Offering (IPO), the SPAC will identify acquisition candidates and attempt to complete one or more business combination transactions after which the company will continue the operations of the acquired company or companies (combined company) as a public company.

The economic interests of the entity or management team that forms the SPAC (sponsor(s)) and the directors, officers and affiliates of a SPAC often differ from the economic interests of public shareholders which may lead to conflicts of interests as they evaluate and decide whether to recommend business combination transactions to shareholders. Clear disclosure regarding these potential conflicts of interest and the nature of the sponsors', directors', officers' and affiliates' economic interests in the SPAC is particularly important because these parties are generally responsible for negotiating the SPAC's business combination transaction. Unlike the traditional IPO process where a private operating company sells its securities in a manner in which the company and its offered securities are valued through market-based price discovery, these individuals are solely responsible for deciding how to value the private operating company and how much the SPAC will pay for it.

The staff of the SEC Division of Corporation Finance has issued guidance about disclosure considerations for SPACs in connection with their IPO and subsequent business combination transactions.

In accordance with the guidance issued by SEC, a SPAC preparing to conduct an IPO or present a business combination transaction to shareholders should consider carefully its disclosure obligations under the federal securities laws as they relate to conflicts of interest, potentially differing economic interests of the SPAC sponsors, directors, officers and affiliates and the interests of other shareholders and other compensation-related matters.

The SEC highlighted certain considerations for a SPAC while preparing to conduct an IPO or present a business combination transaction to its shareholders. These are as follows:

Disclosure considerations - IPO

- Relationships that the sponsors, directors and officers have with other entities which may be target acquirees of the SPAC.
- Financial incentives of SPAC sponsors, directors and officers to complete a business combination and/or possible losses for failure to complete a business combination, including quantitative information to the extent practicable.
- Amount of control that the sponsors, directors and officers have over approval of a business combination.
- Ability for the SPAC to amend its governing documents to facilitate the completion of a business combination or extend the period of time it has to complete the transaction.
- Deferral of compensation owed to underwriters of the SPAC IPO and any additional services to be provided by such party relating to the identification of a target acquiree (e.g. financial advisor, placement agent in a private offering, arranger of debt financing).
- Economic terms of the investments made by SPAC sponsors, directors, officers and their affiliates, including security ownership, compensation arrangements or relationship with affiliated entities.

Disclosure considerations – Business combinations

- Terms of additional financing necessary to complete the business combination and how the terms may impact the public shareholders.
- Approach taken to evaluate and decide to proceed with the identified transaction including how alternative targets may have been considered.
- Material factors that the board of directors considered in approving the identified transaction and the price paid to acquire the target operating company.
- Conflicts of interest of the sponsors, directors, officers and affiliates in presenting the opportunity to the SPAC, and how the SPAC addressed such matters.
- Qualitative and quantitative information about the consideration that the sponsors, directors, officers and their affiliates will receive upon completion of the transaction and the retained ownership they will have in the combined entity.
- Underwriting fees payable upon the completion of the business combination and the additional services the underwriter provided.

Determining ‘income’ for the income test in connection with the disposition of a business

The Center for Audit Quality (CAQ) SEC Regulations Committee asked the SEC staff to provide its view on how the numerator of the income test of significance should be calculated in connection with the disposition of a business. As per the SEC staff, the numerator should be calculated based on the income statement effects that would be removed from the registrant’s income statement during the tested period (similar to the requirements for presenting discontinued operations under ASC 205-20-45), rather than determining pre-tax income on a carve-out basis.

Conversations with audit committee chairs

The PCAOB released a summary of their conversations with audit committee chairs of almost 300 US issuers whose audits they inspected in 2020. The conversations focus broadly on how COVID-19 created unprecedented challenges for auditors, audit committees and public companies. In addition to the effects of COVID-19 pandemic on the audit, PCAOB discussed following three core topics:

- Auditor and communications with the audit committee
- New auditing and accounting standards and
- Emerging technologies.

This section summarises the discussion under each of these heads.

Auditor and communications with the audit committee

Audit committee chairs frequently cited communications with their auditors-both verbal and written-as extremely important to audit quality and their overall relationship with their auditors. Most audit committee chairs commended their auditors' communications, commonly sharing that they were thorough, timely, and at the right level of detail and frequency. Several also highlighted their appreciation for dashboards provided by their auditors that highlighted real-time data on audit progress and other topics.

Audit committee chairs noted that their auditors performed well in areas such as assigning resources with expertise on complex accounting issues, consulting their national offices as appropriate, offering practical approaches to problem-solving (as opposed to being highly theoretical), and providing continuity on audit teams.

Innovation and partner rotation were areas where some audit committee chairs praised their auditors, but others flagged them as areas needing improvement. Other potential areas of improvement that were identified included:

- Managing global audit operations
- Helping more junior audit team members learn the company's business
- Independence communications
- Guidance around auditing of certain controls for third-party vendors
- 'Over-auditing' and/or 'over-documentation' and
- Increased visibility into and discussion around fee changes.

The PCAOB sought to gauge the understanding of audit committee chairs about the activities or initiatives that they observed audit firms undertaking to prevent audit deficiencies, which is a significant area of strategic focus for the PCAOB. Their responses largely centered on the following:

- Audit firms' use of emerging technologies
- Audit firms' emphasis on tone at the top
- The role of robust training as a guard against deficiencies and
- The importance of auditors staying focused on implementation of new accounting and auditing standards.

New accounting and auditing standards

Audit committee chairs oversaw implementation of a variety of new accounting standards during the period covered by PCAOB's 2020 inspections. New accounting standards for revenue recognition, lease accounting, and where applicable, preparing for implementation of Current Expected Credit Losses (CECL), stood out as particularly challenging and time consuming for many audit committee chairs.

Implementation of the Critical Audit Matter (CAM) requirements by auditors was generally viewed as smooth, with audit committee chairs noting that dry runs and other early preparation with their auditors led to few surprises.

The PCAOB's new requirements related to auditing accounting estimates, including fair value measurements, and using the work of specialists took effect for audits of fiscal years ending on or after 15 December 2020. PCAOB observed that the audit committees have not yet discussed the new requirements in detail with their auditors.

Emerging technology

Many audit committee chairs cited the potential benefits from the use of emerging technologies to improve both the audit and overall financial reporting quality. Specifically, they shared their belief that the use of data analytics, workflow automation, cloud computing, and other tools will allow auditors to reduce manual work, obtain better evidence, and become more efficient. Other audit committee chairs noted that technology, if deployed properly, can (1) cut down on opportunities to manipulate or falsify financial information and (2) provide auditors with the ability to more easily identify anomalies.

On the other hand, audit committee chairs also discussed numerous challenges associated with emerging technologies. For example, several audit committee chairs highlighted the gap between the technological capabilities of the company and those of the audit firm. While some audit committee chairs noted that their companies had more sophisticated technology than their auditors, others said the opposite. Either way, audit committee chairs largely agreed that companies and auditors need similar levels of technological capabilities for the benefits of using emerging technologies to be fully realised.

Audit committee chairs were also wary of the risks that come with emerging technologies. They commonly flagged cybersecurity risk as the thing that keeps them up at night, especially with the shift to remote work during the COVID-19 pandemic. Another risk cited was overreliance on technology leading to less attention to or emphasis on preparer and auditor judgement, experience, or professional skepticism.

Finally, concerns were expressed about technology unknowns, given that many technologies have only recently been adopted or put into use. The audit committee chairs noted that while the benefits of emerging technologies are often immediately clear, the risks involved can take longer to become apparent or to understand.

(Source: Quarterly Outlook, KPMG in the US, March 2021, SEC's Disclosure Guidance Topic No 11 on Special Purpose Acquisition Companies dated 22 December 2020 and PCAOB's 2020 Conversations with Audit Committee Chairs issued in February 2021)

CHAPTER 3

Regulatory updates

Eligibility of CSR funds for setting up makeshift hospitals and temporary COVID-19 care facilities

The Ministry of Corporate Affairs (MCA) through a circular dated 22 April 2021 has clarified that spending of funds earmarked for Corporate Social Responsibility (CSR) for setting up makeshift hospitals and temporary COVID-19 care facilities is an eligible CSR activity under Schedule VII of the Companies Act, 2013 (2013 Act) (item no. (i) and (xii). These items relate to promotion of healthcare, including preventive health care and disaster management respectively.

Companies may undertake these activities in consultation with state governments subject to the fulfillment of the Companies (CSR Policy) Rules, 2014 and circulars issued by MCA relating to CSR from time to time.

(Source: MCA general circular no. 05/2021 dated 22 April 2021)

Amendments relating to the maintenance of an accounting software with audit trail feature and related reporting in an auditor's report deferred up to 1 April 2022

Background

On 24 March 2021, MCA had issued certain amendments to the provisions of the Companies (Accounts) Rules, 2014 (Accounts Rules) and the Companies (Audit and Auditors) Rules, 2014 (Audit Rules) under the 2013 Act.

The amendments, *inter alia*, include the following:

- **Use of accounting software with audit trail feature (Rule 3 of Accounts Rules):** The amendment require every company which uses an accounting software for maintaining its books of account to use only such accounting software which has the following features:

  a. Records an audit trail of each and every transaction

  b. Creates an edit log or each change in books of account along with the date when such changes were made.

  Additionally, companies would need to ensure that audit trial is not disabled.

- **Additional matters to be reported in an auditor's report (Rule 11 of Audit Rules):** Basis the above mentioned requirement of a company to use an accounting software with audit trail features, MCA requires an auditor to, *inter alia*, include his/her views and comments as to the fact that the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility. Further, an auditor should also comment on whether:

  a. The audit trail feature has been operated throughout the year for all transactions recorded in the software

  b. The audit trail feature has not been tampered with and

  c. The audit trail has been preserved by the company as per the statutory requirements for record retention.

These amendments were to be effective from financial year commencing on or after 1 April 2021.

New development

The MCA through a notification dated 1 April 2021 has deferred the applicability of the above mentioned amendments. Accordingly, the amendments would now be applicable from financial year commencing on or after 1 April 2022.

For a detailed overview of the amendments, please refer KPMG in India's First Notes on 'Accounting software for maintaining books of account, changes to board's report and additional reporting in an auditor's report – New norms' dated 14 April 2021.

(Source: MCA notifications dated 1 April 2021)

Pre-packaged insolvency resolution process for MSMEs

The Ministry of Law and Justice has issued certain amendments to the Insolvency and Bankruptcy Code, 2016 (IBC) through the IBC (Amendment) Ordinance, 2021 dated 4 April 2021. This will address the specific requirements of Micro, Small and Medium Enterprises (MSMEs) relating to the resolution of their insolvency and provide an efficient alternative insolvency resolution process for corporate persons classified as MSME under IBC. The amendments introduced a pre-packaged insolvency resolution process for corporate persons classified as MSME.

Additionally, the MCA has issued the Insolvency and Bankruptcy (pre-packaged insolvency resolution process) Rules, 2021 effective from 9 April 2021. The Rules prescribe the manner of filing an application for initiating pre-packaged insolvency resolution process.

Further, in accordance with the amendments, the MCA has prescribed INR10 lakh as the minimum amount of default for the matters relating to the pre-packaged insolvency resolution process of corporate debtors under Chapter III-A of the IBC (pre-packaged insolvency resolution process).

(Source: MCA notification no. G.S.R 256(E) and notification no. S.O. 1543(E) dated 9 April 2021 and the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2021 issued by the Ministry of Law and Justice dated 4 April 2021)

SEBI reduced timelines for refund of application money

Currently, the Securities and Exchange Board of India (SEBI) (Issue of Capital and Disclosure Requirements) Regulations, 2018 requires an issuer to refund application money as per below timelines:

a. In case of non-receipt of minimum subscription, the application money is required to be refunded within a period of **15 days** from the closure of the issue.

b. In case of failure to obtain listing or trading permission from the stock exchanges where the specified securities were to be listed, the application money should be refunded within a period of **seven days** from the date of receipt of intimation of rejection from the stock exchanges.

SEBI through a circular dated 31 March 2021 has reduced the above timelines in relation to refund of application money by the issuer to **four days** from the closure of the issue or from the date of receipt of intimation of rejection from the stock exchanges as the case may be. *(Emphasis added to highlight the change)*

(Source: SEBI circular no. SEBI/HO/CFD/DIL1/CIR/P/2021/47 dated 31 March 2021)

SEBI extends relaxation relating to application for a rights issue

Background

In accordance with the requirements of Regulation 76 of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations), an issuer can make an application for a rights issue only through an Application Supported by Blocked Amount (ASBA) facility.

In view of the pandemic and to ensure that all eligible shareholders are able to apply to the rights issue during such times, SEBI through a notification dated 6 May 2020 had permitted issuers along with lead manager(s) to the issue, the registrar, and other recognised intermediaries (as deemed fit by issuer and lead manager(s)) to institute an optional mechanism (non- cash mode only) to accept the applications of the shareholders subject to ensuring that no third party payments shall be allowed in respect of any application.

In respect of the said mechanism, an issuer along with lead manager(s) needs to ensure the following:

a. The mechanism(s) should only be an additional option and not a replacement of the existing process. As far as possible, attempts will be made to adhere to the existing prescribed framework.

b. The mechanism(s) should be transparent, robust and have adequate checks and balances. It should aim at facilitating subscription in an efficient manner without imposing any additional costs on investors. The issuer along with lead manager(s), and registrar should satisfy themselves about the transparency, fairness and integrity of such mechanism.

c. An FAQ, online dedicated investor helpdesk, and helpline should be created by the issuer company along with lead manager(s) to guide investors in gaining familiarity with the application process and resolve difficulties faced by investors on priority basis.

d. The issuer along with lead manager(s), registrar, and other recognised intermediaries (as incorporated in the mechanism) should be responsible for all investor complaints.

The relaxation was available for rights issue opening up to 31 March 2021.

New development

SEBI through a circular dated 22 April 2021 has further extended the relaxation for rights issue opening up to 30 September 2021. This is subject to the condition that the issuer along with the lead manager(s) should continue to comply with the points given in (a) to (d) above.

(Source: SEBI circular no. SEBI/HO/CFD/DIL2/CIR/P/2021/552 dated 22 April 2021)

Declaration of dividends by banks

The Reserve Bank of India (RBI) through its circular dated 4 December 2020 has prohibited banks from making any dividend payment on equity shares from the profits pertaining to the financial year ended 31 March 2020.

Recently, RBI has decided to review the dividend declaration norms for the year ended 31 March 2021 as follows:

- **Commercial banks:** Banks may pay dividend on equity shares from the profits for the financial year ended 31 March 2021, subject to the quantum of dividend being not more than 50 per cent of the amount determined as per the dividend payout ratio.
- **Cooperative banks:** Banks will be permitted to pay dividend on equity shares from the profits of the financial year ended 31 March 2021.

Further, banks shall continue to meet the applicable minimum regulatory capital requirements after dividend payment. While declaring dividend on equity shares, it shall be the responsibility of the board of directors to, *inter alia*, consider the current and projected capital position of the bank vis-à-vis the applicable capital requirements and the adequacy of provisions, taking into account the economic environment and the outlook for profitability.

(Source: RBI notification no. RBI/2021-22/23 dated 22 April 2021)

Asset classification and income recognition following the expiry of COVID-19 regulatory package

In accordance with the judgement issued by the Hon'ble Supreme Court of India (SCI) dated 23 March 2021 in the matter of Small Scale Industrial Manufacturers Association vs UOI & Ors. and other connected matters, RBI has issued following advisory for the lending institutions[1] vis-à-vis COVID-19 regulatory package:

- **Refund/adjustment of 'interest on interest':** All lending institutions shall immediately put in place a board-approved policy to refund/adjust the 'interest on interest' charged to the borrowers during the moratorium period, i.e. 1 March 2020 to 31 August 2020 in conformity with the above judgement. The methodology for calculation of the amount to be refunded/ adjusted for different facilities shall be finalised by the Indian Banks Association (IBA) in consultation with other industry participants/bodies, which shall be adopted by all lending institutions.

  The above reliefs shall be applicable to all borrowers, including those who had availed of working capital facilities during the moratorium period, irrespective of whether moratorium had been fully or partially availed, or not availed.

  Lending institutions are also required to disclose the aggregate amount to be refunded/adjusted in respect of their borrowers based on the above reliefs in their financial statements for the year ended 31 March 2021.

- **Asset classification:** Asset classification of borrower accounts by all lending institutions would continue to be governed by the following instructions:

  a. *In respect of accounts which were not granted any moratorium in terms of the COVID-19 regulatory package:* Asset classification would be as per the criteria laid out in the 'Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning' dated 1 July 2015 or other relevant instructions as applicable to the specific category of lending institutions (IRAC norms).

  b. *In respect of accounts which were granted moratorium in terms of the COVID-19 regulatory package:* Asset classification for the period from 1 March 2020 to 31 August 2020 would be governed in terms of the RBI circular dated 17 April 2020 (COVID-19 regulatory package - asset classification and provisioning). For the period commencing 1 September 2020, asset classification for all such accounts shall be as per the applicable IRAC norms.

(Source: RBI notification no. RBI/2021-22/17 dated 7 April 2021)

Deferment of reporting under clause 30C and 44 of the Tax Audit Report

The Central Board of Direct Taxes (CBDT) through a notification dated 20 July 2018 made certain amendments to the Form No. 3CD (tax audit report). The amendments, *inter alia*, introduced following new clauses:

- **Clause 44: Break up of total expenditure between GST registered vendors and unregistered vendors:** Clause 44 requires a break-up of total expenditure incurred during the year between expenditure incurred relating to entities not registered under Goods and Service Tax (GST) and expenditure incurred relating to entities registered under GST. Additionally, the expenditure relating to GST registered vendors is required to be further bifurcated between expenditure in relation to exempt supply, expenditure towards entities registered under composition scheme and other registered entities.
- **Clause 30C:** Clause 30C requires a taxpayer to report the nature and tax impact of impermissible avoidance arrangement as referred to in Section 96 of the Income Tax Act, 1961 (IT Act) if any. Section 96 of the IT Act provides that an arrangement would be presumed to be impermissible if the main purpose of whole or part of the arrangement is to obtain a tax benefit.

These new clauses were kept in abeyance up to 31 March 2021.

Relaxation

In view of the ongoing pandemic, CBDT has decided that the reporting under clause 30C and 44 of the tax audit report (Form 3CD) would be kept in abeyance till 31 March 2022.

(Source: CBDT circular no. 05/2021 dated 25 March 2021)

1. Commercial banks (including small finance banks, local area banks and regional rural banks), primary (urban) co-operative banks/state co-operative banks/district central co-operative banks, All-India Financial Institutions (AIFIs), and Non-Banking Financial Companies (NBFCs) (including Housing Finance Companies (HFCs)).

Temporary exceptions to hedge accounting prescribed under guidance note on accounting for derivative contracts due to interest rate benchmark reform

For the entities that do not apply Ind AS, the provisions regarding hedge accounting are prescribed in the guidance note on 'Accounting for Derivative Contracts' issued by the Institute of Chartered Accountants of India (ICAI) in 2015.

Recently, ICAI through an announcement has provided temporary exceptions from applying specific hedge accounting requirements prescribed under the guidance note on Accounting for Derivative Contracts for entities not following Ind AS. The exceptions are in line with those provided in phase I to the entities following Ind AS (i.e. those addressing pre-replacement issues). The temporary exceptions would be applicable to all hedging relationships directly affected by interest rate benchmark reform.

The key exceptions are as follows:

- **The highly probable requirement:** An entity should assume that the interest rate benchmark on which the hedged cash flows (contractually or non-contractually specified) are based is not altered as a result of interest rate benchmark reform.
- **Prospective assessments:** An entity should assess whether the economic relationship between the hedged item and the hedging instrument exists based on the assumptions that the interest rate benchmark on which the hedged item and the hedging instrument are based is not altered as a result of IBOR reform.
- **End of application:** An entity should prospectively cease applying the exceptions at the earlier of:
  a. When the uncertainty regarding the timing and the amount of interest rate benchmark based cash flows is no longer present and
  b. The discontinuation of the hedging relationship (or reclassification of all amounts from the cash flow hedge reserve).

Effective date: The temporary exceptions will be effective for annual reporting periods beginning on or after 1 April 2020.

The requirements will apply only to those hedging relationships that existed at the beginning of the reporting period in which an entity first applies these requirements or were designated thereafter, and to the amount accumulated in the cash flow hedge reserve that existed at the beginning of the reporting period in which an entity first applies these requirements.

(Source: ICAI announcement dated 31 March 2021)

Approved investment for insurers

Currently, an issuer is permitted to invest or keep invested its controlled fund only in approved securities specified in Regulation 3 of the Insurance and Regulatory Development Authority of India (IRDAI) (Investment) Regulations, 2016. These approved securities, *inter alia*, includes:

a. Preference shares of any company which has paid dividends on its equity shares for at least **two consecutive years** immediately preceding

b. Equity shares of any listed company on which not less than 10 per cent dividends have been paid for at least **two consecutive years** immediately preceding.

IRDAI through a circular dated 31 March 2021 has permitted insurers to classify investments in preference shares and equity shares as a part of approved investment if such shares have paid dividend for at least **two years out of three consecutive years** immediately preceding for the period from 1 April 2020 to 30 September 2021.

(Source: IRDAI circular no. IRDAI/F&I/CIR/INV/065/03/2021 dated 31 March 2021)

Investments in debt securities of InvITs and REITs

Investments-Master Circular permits insurers to invest in units of listed Infrastructure Investment Trusts (InvITs) and Real Estate Investment Trusts (REITs) subject to specified conditions.

The Finance Act, 2021 permitted these trusts to issue debt securities. Accordingly, IRDAI through a circular dated 22 April 2021 prescribes certain conditions to be applied by insurers investing in debt securities issued by InvITs / REITs. Those conditions, *inter alia*, includes:

a. An insurer should not invest more than 10 per cent of the outstanding debt instruments (including the current issue) in a single InvIT/REITs issue.

b. The cumulative investments in units and debt instruments of InvITs and REITs should not exceed three per cent of total fund size of the insurer at any point of time.

c. No investment should be made in debt instruments of an InvIT/ REIT where the sponsor is under the promoter group of the insurer.

d. The concurrent auditor in his quarterly report to the audit committee/board of the insurer should specifically confirm compliance to all the specified norms.

(Source: IRDAI circular no. IRDAI/F&I/CIR/INV/098/04/2021 dated 22 April 2021)

Proposed amendments to IFRS 13, *Fair Value Measurement* and IAS 19, *Employee Benefits*

On 25 March 2021, the International Accounting Standards Board (IASB) has issued an exposure draft which comprise of proposed guidance for itself when developing and drafting disclosure requirements in IFRS in future. It also includes proposed amendments to IFRS 13 and IAS 19 consequent to the application of the proposed guidance.

The proposed guidance explains how IASB will modify disclosure requirements in IFRS to enhance the use of judgement. In summary, IASB will:

a. Require entities to comply with **overall disclosure objectives** that describe the overall information needs of users of financial statements. To comply with those objectives, entities would be required to assess whether information provided in the notes by complying with the specific disclosure objectives meets the overall user information needs.

b. Require entities to comply with **specific disclosure objectives** that describe the detailed information needs of users of financial statements. To comply with those objectives, entities would be required to disclose all material information needed to meet the detailed user information needs.

c. Supplement specific disclosure objectives with explanations of what the **information provided to meet those objectives** is intended to help users of financial statements do.

d. Link each specific disclosure objective with items of information an entity may, or in some cases is required to, disclose to satisfy the objective.

Proposed amendments to IFRS 13 include:

- **Assets and liabilities measured at fair value in the statement of financial position after initial recognition:** An overall disclosure objective that enables user of financial statements to evaluate the entity's exposure to uncertainties associated with fair value measurements of classes of assets and liabilities measured at fair value in the statement of financial position after initial recognition. The information shall enable users of financial statements to understand:

  a. The significance of those classes of assets and liabilities for the entity's financial position and performance

  b. How their fair value measurements have been determined and

  c. How changes in those measurements could have affected the entity's financial statements at the end of the reporting period.

  IASB also proposes specific disclosure objectives that require an entity to disclose information about the:

  a. Assets and liabilities within each level of the fair value hierarchy

  b. Measurement uncertainties associated with their fair value measurements

  c. Reasonably possible alternative fair value measurements

  d. Reasons for changes in their fair value measurement.

- **Assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes:** A specific disclosure objective that requires an entity to disclose information that enables users of financial statements to understand:

  a. The amount, nature and other characteristics of each class of assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes and

  b. How the characteristics relate to the categorisation of those classes of assets and liabilities in the fair value hierarchy.

Proposed amendments to IAS 19 include:

- **Defined benefit plans:** An overall disclosure objective that requires an entity to disclose information that enables users of financial statements to:

  a. Assess the effect of defined benefit plans on the entity's financial position, financial performance and cash flows and

  b. Evaluate the risks and uncertainties associated with the entity's defined benefit plans.

  IASB also proposes specific disclosure objectives that require an entity to disclose information about:

  a. Amounts in the primary financial statements relating to defined benefit plans

  b. The nature of, and risks associated with, defined benefit plans

  c. Expected future cash flows relating to defined benefit plans

  d. Future payments to members of defined benefit plans that are closed to new members

  e. Measurement uncertainties associated with the defined benefit obligation

  f. Reasons for changes in the amounts recognised in the statement of financial position for defined benefit plans.

- **Defined contribution plans:** An overall disclosure objective that requires an entity to disclose information that enables users of financial statements to understand the effect of defined contribution plans on the entity's financial performance and cash flows.
- **Other types of employee benefit plans:** An overall disclosure objective that requires an entity to disclose information that enables users of financial statements to understand:
  a. The effect of short-term employee benefits on the entity's financial performance and cash flows
  b. The nature of other long-term employee benefits and the effect of those benefits on the entity's financial position, financial performance and cash flows
  c. The nature of termination benefits and the effect of those benefits on the entity's financial position, financial performance and cash flows.

The exposure draft also proposed consequential amendments to IAS 34, *Interim Financial Reporting* and IFRIC 17, *Distributions of Non-cash Assets to Owners.*

Comments have been invited up to 21 October 2021.

(Source: ED/2021/3, Disclosure Requirements in IFRS Standards - A Pilot Approach issued by IASB in March 2021)

FASB issued an Accounting Standard Update (ASU) on Topic 350, *Intangibles - Goodwill and Other*

Under the current guidance in subtopic 350-20, *Intangibles-Goodwill and Other-Goodwill*, an entity is required to monitor and evaluate goodwill impairment triggering events throughout the reporting period. The triggering event analysis and resulting goodwill impairment test, if any, are required to be performed when a triggering event occurs without the use of hindsight or known changes to facts and circumstances after the triggering event date.

Certain stakeholders have expressed concern about the cost and complexity of private companies evaluating triggering events and potentially measuring a goodwill impairment during the reporting period, rather than completing the analysis as of the end of the reporting period. The issue had become more apparent during COVID-19 pandemic because of the uncertainty in the economic environment and the significant changes in facts and circumstances, quarter over quarter.

To address the said issues, the Financial Accounting Standards Board (FASB) has issued certain amendments which provide private companies and not-for-profit entities with an accounting alternative to perform the goodwill impairment triggering event evaluation as of the end of the reporting period, whether the reporting period is an interim or annual period. In accordance with the amendments:

- An entity that elects this alternative is not required to monitor for goodwill impairment triggering events during the reporting period but, instead, should evaluate the facts and circumstances as of the end of each reporting period to determine whether a triggering event exists and, if so, whether it is more likely than not that goodwill is impaired.
- An entity that does not elect the accounting alternative for amortising goodwill and that performs its annual impairment test as of a date other than the annual reporting date should perform a triggering event evaluation only as of the end of the reporting period.

Effective date: The amendments are effective on a prospective basis for fiscal years beginning after 15 December 2019. Early adoption is permitted for both interim and annual financial statements that have not yet been issued or made available for issuance as of 30 March 2021.

The amendments also include an unconditional one-time option for entities to adopt the alternative prospectively after its effective date without assessing preferability under Topic 250, *Accounting Changes and Error Corrections.*

(Source: FASB ASU No. 2021-03 issued in March 2021)

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

Accounting software for maintaining books of account, changes to board’s report and additional reporting in an auditor’s report – New norms

14 April 2021

On 24 March 2021, the Ministry of Corporate Affairs (MCA) has issued certain amendments to the provisions of the Companies (Accounts) Rules, 2014 and the Companies (Audit and Auditors) Rules, 2014 under the Companies Act, 2013.

The amendments mainly relate to the following:

- Manner of books of account to be kept in electronic mode
- Additional disclosures in the board’s report
- Additional matters to be reported in the auditor’s report.

On 1 April 2021, MCA amended the circulars issued on 24 March 2021 regarding the applicability date of the newly prescribed requirements on the ‘manner of books of account to be kept in electronic mode’ and ‘related auditor’s report’ changes. Now these two requirements would be applicable from the financial year commencing on or after 1 April 2022.

This issue of First Notes aims to provide an overview of these amendments.

Voices on Reporting (VOR) – Annual updates publication

On 20 April 2021, KPMG in India released the VOR - Annual updates publication. 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) that are expected to be relevant for stakeholders for the year ended 31 March 2021.

To access the publication, please click here.

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