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Foreword

The European Securities and Markets Authority (ESMA) has issued its latest annual public financial statement which prescribes the common enforcement priorities for the 2021 annual financial reports of listed entities. They relate to financial and non-financial impacts of COVID-19 and climate related matters, expected credit losses disclosures of credit institutions and certain important matters related to Alternative Performance Measures (APMs) for IFRS financial statements and non-financial statements. ESMA, together with the national enforcers, will pay particular attention to these areas when monitoring and assessing the application of the relevant reporting requirements. In this edition of Accounting and Auditing Update (AAU), we will discuss in detail each of the key priority areas along with the recommendations provided by ESMA in its statement to be considered by the listed entities while filing their financial results.

Non-Banking Finance Companies (NBFCs) have played a significant complementary role in financial intermediation, along with banks in India. The sector has witnessed a tremendous growth in terms of size, complexity, and interconnectedness within the financial sector. With a view to align the regulatory framework of NBFCs with their changing risk profiles, recently the Reserve Bank of India (RBI) has prescribed a revised 'scale-based' regulatory framework for the NBFC sector. The regulatory framework bifurcates all the NBFCs into four layers based on their size, activity, and perceived riskiness. The revised regulatory framework is applicable with effect from 1 October 2022. In our article on the topic, we will discuss the key features of the revised regulatory framework including basis of classification of NBFCs in each of the specified layers.

Recently, the Securities and Exchange Board of India (SEBI) has issued a slew of amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR). The amendments introduced key revisions to the related party framework prescribed under the LODR. Those, *inter alia*, include revised definition of related party and Related Party Transactions (RPTs), revision of materiality threshold for identification of material RPTs and revised norms related to approval of RPTs by shareholders and audit committee. Internationally, the International Accounting Standards Board (IASB) has proposed narrow-scope amendments to IAS 1, *Presentation of Financial Statements*. The amendments are expected to improve the information companies provide about long-term debt with covenants. Our regulatory updates article covers these and other important regulatory developments 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.

Sai Venkateshwaran
Partner - Assurance
KPMG in India

Ruchi Rastogi
Partner - Assurance
KPMG in India

Chapter 1

ESMA issued enforcement priorities for 2021 annual financial reports

This article aims to:

Discuss the key priority areas for the 2021 annual financial reports of listed entities as envisaged by ESMA in its latest annual public statement.

Introduction

On 29 October 2021, the European Securities and Markets Authority (ESMA) has issued its annual public statement. The statement prescribes the common enforcement priorities for the 2021 annual financial reports of listed entities. Following key topics have been considered as the common enforcement priorities for IFRS financial statements and non-financial statements:

Impacts of COVID-19 and related matters (Financial and non-financial impacts)	**Climate related matters (Financial and non-financial impacts)**
Expected Credit Losses (ECL) disclosures of credit institutions (Financial impacts)	**Other considerations related to Alternative Performance Measures (APMs)**

ESMA, together with the national enforcers, will pay particular attention to these areas when monitoring and assessing the application of the relevant reporting requirements. In this article, we will discuss each of the key priority areas along with the recommendations provided by ESMA in its statement.

Impacts of COVID-19 and related matters

Financial impacts

ESMA requires entities to carefully assess the longer-term impacts of COVID-19 on their activities, financial performance, financial position and cash flow. ESMA also reiterated the guidance given in its 2020 public statement[1].

In accordance with the guidance, some of the key considerations vis-à-vis long-term impact of COVID-19 includes:

Going concern assumptions

- Entities should provide sufficiently detailed disclosures on the going concern assessment pertaining to a company, when such assessment requires significant judgement. While making such an assessment, entities should consider all available information about the future, which is at least, but not limited to,12 months from the end of the reporting date.
- Entities should disclose material uncertainties related to events or conditions that may cast significant doubt upon their ability to continue as a going concern (such as restricted access to financial resources due to the impacts of COVID-19). These disclosures should also include close call scenarios, where the entities conclude that there are no material uncertainties that would impact the going concern assumption.

1. Enforcement priorities for 2020 annual financial reports issued by ESMA on 28 October 2020.

- Entities should assess and disclose if material uncertainties exist related to events or conditions that may cast significant doubt upon the issuers' ability to continue as a going concern if relevant beyond the 12-month period after the reporting period.

Significant judgements and estimation uncertainty

- Entities should disclose the assumptions underlying significant judgements and estimates made while applying their accounting policies, and the impact of COVID-19 on such judgements and estimates. For example, assumptions underlying impairment of assets, recoverability of deferred tax assets and valuation, and how the consequences of COVID-19 (such as market price volatility) have impacted these assumptions.
- Entities should also provide information about the sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculations.

Presentation of COVID-19 related items

Considering the pervasiveness of the impact of COVID-19 on the financial performance of a company, ESMA cautions entities that a separate presentation of COVID-19 impact may not faithfully represent a company's current and future overall financial performance. Therefore, ESMA encourages entities to provide quantitative and qualitative information and a clear and unbiased picture of the multiple areas affected by COVID-19 either in a single note or in multiple notes, with appropriate cross references.

Impairment of assets

Impact of COVID-19 should be considered while assessing the indicators of impairment. ESMA emphasised that the scale of reasonably possible changes in the key assumptions used in impairment testing may be larger than usual. It also reminds entities that the annual impairment test for a Cash Generating Unit (CGU) to which goodwill has been allocated is performed at the same time every year.

Other considerations

ESMA reminds entities to provide full transparency of any material arrangements that take the form of supply chain financing (e.g., management judgements in accordance with IAS 1, *Presentation of Financial Statements*, of financial position and of cash flow as well as impacts).

ESMA also recommended that entities should provide transparent information regarding their liquidity risk as required by IFRS 7, *Financial Instruments: Disclosures* and that this information is, as for all disclosures, sufficiently entity-specific. Both qualitative and quantitative information is necessary to enable investors to evaluate an entity's exposure to liquidity risk.

Recovery from COVID-19

ESMA expects issuers, in particular those operating in sectors that are severely impacted by the longer-term impacts of COVID-19 (e.g., transportation, hospitality, retail), to disclose information on the judgements, estimates and assumptions that were updated as a result of any recent changes in their economic and financial situation together with the basis for those changes, where this is necessary for an understanding of the financial statements. These include, but are not limited to, the main assumptions used (and respective sensitivity analyses) to determine whether an impairment or reversal of impairment of non-financial assets should be recognised or whether the useful life of non-financial assets should be revised.

ESMA also reminded entities to assess at the end of each reporting period whether there is any indication that an impairment loss recognised in prior periods for an asset other than goodwill may no longer exist or may have decreased. While making such an assessment, issuers should consider, at a minimum, the internal and external indications as specified in paragraph 111 of IAS 36, *Impairment of Assets* and that an impairment loss recognised in prior periods for an asset other than goodwill is reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the period in which the last impairment loss was recognised.

Additionally, there should be utmost transparency on the criteria and assumptions used in the recognition of deferred tax assets arising from the carry forward of unused tax losses and unused tax credits due to COVID-19 (e.g., analysis of the origin of the losses and nature of convincing evidence required in the specific circumstances).

Government support measures

ESMA expects entities to include a description of the nature and extent of any significant public support measure received by category (e.g., loans, tax relief, compensation schemes) in the financial statements. ESMA also expects entities to give information on the main characteristics of the support measures (e.g., expected duration, reimbursement and main conditions) as well as on the effects of their termination. Additionally, ESMA expects entities to make a link with the going concern assumptions or other planned actions, wherever relevant.

Non-financial impacts

ESMA has recommended entities to provide transparency on how the consequences of the pandemic are affecting their plans to meet any sustainability targets and whether any new or adjusted goals have been determined. Entities are also encouraged to provide disclosures on how they foresee the development of their business in response to the changing conditions arising from the pandemic, in particular, in relation to any expected structural changes to the way they conduct their business (e.g., restructuring of supply chains and distribution channels) and arrange the working conditions for their employees.

It also recommended that issuers provide transparency on any material effects that the pandemic might have had on non-financial Key Performance Indicators (KPIs) as well as on any new non-financial KPIs which may have been developed to reflect any long-term effects of the pandemic.

Climate related matters

Financial impacts

Climate risks and consistency between IFRS financial statements and non-financial information

ESMA observed that investors are increasingly interested in information regarding the impacts that climate-related matters may have on entities as well as information on the entities' impacts on the mitigation of the effects of climate-related matters. Accordingly, ESMA requires entities and auditors to consider climate risks when preparing and auditing IFRS financial statements to the extent that the effects of those risks are material to those financial statements, even if IFRS standards do not explicitly refer to climate-related matters.

Additionally, all entities (irrespective of the extent of impact) should consider the climate-related matters holistically in their communications to the market by ensuring consistency in the information disclosed across the management report, the non-financial statement, the financial statements, and, where applicable, the prospectus. To ease reporting, entities are encouraged to include all information required to be disclosed by the IFRS standards on climate-related matters, including those concerning ECL, in one single note or alternatively to provide a mapping of where different notes address climate-related matters.

ESMA has also encouraged issuers to consider the requirements of the educational material on the effects of climate-related matters on financial statements issued by the International Accounting Standards Board (IASB) in November 2020[2].

Significant judgements and estimation uncertainty

In accordance with the requirements of IAS 1, ESMA urges entities, in particular those belonging to the most affected sectors, to consider disclosure of management judgements related to climate risks (for example those related to any climate scenarios on which assumptions have been made). ESMA also expects issuers to disclose in the financial statements how the forward-looking assumptions, estimates and judgements applied in preparing the financial statements are consistent with the information included in the corresponding management report and non-financial statement.

Entities should also clearly explain why apparently significant climate-related risks have not had a material impact on the financial statements.

ESMA also expects entities to consider climate change when assessing whether the expected useful lives of non-current assets and the estimated residual values in IAS 16, *Property, Plant and Equipment* and IAS 38, *Intangible Assets* should be revised.

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2. For a detailed overview of the guidance given in the educational material, please refer KPMG in India's AAU article *'Climate change: Implications on financial reporting'* issued in November 2020 (Issue no. 52/2020).

Additionally, in accordance with IAS 36, entities should:

a. Assess whether indications exist that non-financial assets are impaired as a result of climate risk

b. Use assumptions reflecting climate risks

c. Adapt the sensitivity analysis disclosed to consider climate risks and commitments in the assumptions used. For instance, external information about significant changes with an adverse effect on the company, such as significant changes in the environment in which a company operates, is an indication that an asset may be impaired as per IAS 36

d. Consider the significant impacts on future expected cash flows for a particular asset or CGU, when making disclosures of assumptions used to determine the recoverable amount of assets or CGUs.

ESMA also requires entities to carefully consider the requirements in IAS 37, *Provisions, Contingent Liabilities and Contingent Assets* with regard to contingent liabilities for potential litigation, regulatory requirements to remediate environmental damage, additional levies or penalties related to environmental requirements, contracts that may become onerous, or restructurings to achieve climate-related targets.

ESMA also calls for transparency in the accounting treatment applied regarding carbon and greenhouse gas emission trading schemes. In particular, entities are encouraged to provide information on their accounting policies and information on how these schemes affect their financial performance and financial position.

Materiality

Entities are expected to consider the requirements of IAS 1 and IFRS Practice Statement 2, *Making Materiality Judgements* issued by IASB relating to material financial information while evaluating need to disclose information about climate risks. In accordance with the guidance provided by IAS 1 and practice statement, entities should consider quantitative and qualitative factors as well as the interaction among different factors while assessing whether or not an information is material.

Non-financial impacts

ESMA emphasised the importance of providing transparency on policies pursued in relation to non-financial matters and the related outcomes in the area of climate-related matters. It reminded entities to consider the guidance provided by the European Commission in its Guidelines on reporting climate-related information which, notwithstanding its non-binding nature, is also consistent with the disclosures envisaged by the Task-Force on Climate-Related Financial Disclosures (TCFD)[3].

ESMA emphasised the importance of disclosing which policies, if any, issuers have put in place to address climate change, both in terms of any identified risks and opportunities that climate-related matters may give rise to for the undertakings' activities as well as on the impact (positive or negative) that the undertaking's actions may have on such matters. Disclosure of such policies should include reference to the most significant transitional risks and physical risks that entities have identified with a current or future expected material impact on their business model and activities and disclose how those risks are managed and which climate change mitigation or adaptation actions are put in place to address those risks.

Entities should provide transparency of the process leading to the identification of such risks and on the outcomes of their climate-related policies also by providing specific indicators and explaining how the entity's performance on such indicators is consistent with any pre-defined targets. Entities should also disclose the progress made towards achieving any such targets. An entity's strategy, plans, targets and current performance in relation to climate-related matters should be taken into account both in terms of non-financial disclosures as well as financial information.

ESMA also highlights the importance of ensuring consistency and connectivity between the information provided within the non-financial statements in relation to climate-related matters with the information provided in the financial statements, including the judgements made and estimates which should duly consider any financial implications of climate-related matters.

ECL disclosures of credit institutions

Management over-lays

As per ESMA, when material adjustments (also referred to as 'management over-lays') are used in the measurement of ECL, enhanced transparency should be provided by issuers in order to fulfil the overarching objectives and principles of IFRS 7. ESMA has observed that such adjustments either take the form of ECL model revisions, including updates of the model inputs (in-model adjustments), or are applied outside the primary models (post-model adjustments).

ESMA acknowledged that it may often be difficult to quantify the effect of the in-model adjustments, though following considerations apply in substance to both types of adjustments:

- For each material adjustment, ESMA expects issuers to disclose detailed and specific information on its impact on the ECL estimate, the rationale and the methodology applied. These disclosures should be provided at an appropriate level of granularity, for example by explaining to which specific type of products, exposures, sectors or geographic areas the adjustments

3. Guidelines on reporting climate-related information, European Commission, 17 June 2019.

relate to, if relevant. In order to increase transparency and meet the requirements of IFRS 7, a corresponding breakdown of the quantitative impact of the adjustments may be appropriate.

The rationale should clearly specify the reasons for the adjustment (e.g., to include the latest macroeconomic outlook, or to address model limitations resulting from insufficient inclusion of certain risks). The description of the methodology should include significant inputs and assumptions.

- ESMA expects entities to provide information on whether the adjustments relate to a specific impairment stage and, if applicable, what impact they have on staging of the underlying instruments.
- Entities should consider how their ECL sensitivity disclosures in the notes to the financial statements can incorporate material management overlays and provide rationale for the chosen method, if relevant.
- Entities should explain any significant changes in methodologies and assumptions from the previous reporting period and the reasons for those changes. This information should enable users to understand the extent of the movements, their nature (i.e., changes in underlining assumptions) and the reasons for the development of adjustments (i.e., incorporation of the post-model adjustments in the core model, if applicable).

Significant changes in credit risk (stage transfers)

- Entities should disclose the basis for the inputs and assumptions and the estimation techniques used to determine whether a significant increase in credit risk (SICR) has occurred for financial instruments since their initial recognition or whether a financial asset is credit impaired.
- Entities should explain the quantitative and qualitative factors applied, including the length of the 'cure' period, and any material differences in the application of the factors across portfolios.
- ESMA has recommended that issuers disclose any quantitative SICR-thresholds applied, such as probability of default (PD) deterioration triggers. If there are significant differences in thresholds depending on portfolio type, additional explanations are required.
- If, during the reporting period, any significant relief measures were provided to borrowers by issuers, ESMA expect entities to explain how these measures have impacted the assessment of SICR.

  If the relief measures do not result in a derecognition of the financial instrument, credit institutions should include a description of how they determined SICR or whether these instruments are impaired in these specific circumstances providing, for example, information on related significant judgements, type of (new) indicators applied and the level of assessment (e.g., counterparty, sector, type of financial instruments, etc.) at an appropriate level of detail.
- Any significant changes in the assessment of SICR or on whether a financial asset is credit-impaired (i.e., changes in the methodology or significant assumptions) during the reporting period should be disclosed and explained.

Forward-looking information

While explaining how forward-looking information has been incorporated into the determination of ECL, ESMA encouraged credit institutions to provide specific disclosures on the main judgements and estimations related to uncertainties that have been taken into account when defining the scenarios and their weight. ESMA emphasised the importance of providing granular disclosures on the sensitivity analysis (e.g., regarding each scenario) and the quantitative impact of this analysis on the ECL and, where appropriate, on staging.

Transparency on changes in loss allowances, credit risk exposures and collateral

ESMA highlighted that the tabular reconciliation of the loss allowance (impairment amount) from the opening balance to the closing balance in accordance with IFRS 7 should be disaggregated by class of financial instrument and it should separately provide information about the changes in loss allowances for off-balance sheet commitments. To provide sufficient transparency, reconciliations should be disclosed both at the entity level and for significant portfolios with shared credit risk characteristics.

Additionally, ESMA has encouraged credit institutions to disclose a joint reconciliation of the loss allowance and the gross carrying amount. Quantitative disclosures and the narrative descriptions provided in different parts of the financial statements or of the management report should be clearly linked to each other.

Disclosures on credit enhancements should be sufficiently granular to enable users to understand material concentrations of credit risk. Where appropriate, disaggregation of exposures by loan to value (LTV) ranges can be provided.

Effect of climate-related risk on the ECL measurement

ESMA expects credit institutions to disclose whether material climate-related and environmental risks are taken into account in credit risk management, including information about the related significant judgements and estimation uncertainties. Wherever applicable, credit institutions should provide explanations on how these risks are incorporated in the calculation of ECL, on any credit risk concentrations related to environmental risks and how those risks affect the amounts recognised in the financial statements.

Other considerations related to APMs

ESMA calls for caution when adjusting APMs used and/or when including new APMs solely with the objective of depicting the impacts that COVID-19 may have on their financial performance.

ESMA noted that, at this point, it is more likely that the impacts of COVID-19 rather represent a general development that has been induced by the pandemic than the result of a one-off event. Therefore, as per ESMA, in most cases, these impacts should not necessarily be presented separately in APMs but in the accompanying narrative information.

Further, APMs disclosed should be given meaningful labels reflecting their content and basis of calculation to avoid conveying misleading messages to users. For example, entities or persons responsible for the prospectus should not use the term 'EBITDA' if items other than interest, taxes, depreciation, and amortisation are adjusted from the net result (adjusted EBITDA).

Also, APMs presented should be neutral. In accordance with ESMA presenting biased APMs which are adjusted to exclude only one-off losses (e.g., impairment losses) but include one-off gains of the same nature (e.g., reversal of impairments or grants) may violate the principles set out in articles 4 and 5 of the Transparency Directive relating to fair review of the development and performance of the business and the position of the issuer.

Conclusion

The priority areas highlighted by ESMA, especially COVID-19 and climate related matters requires immediate attention by companies in India as well due to significant disruption on account of climate related matters and COVID-19. There is an increase in demand for disclosures on these areas from all stakeholders, in particular, investors and regulators to enable them to assess the financial and operational performance of the companies.

Needless to mention, assessment of the potential impact areas and effective reporting requires timely deliberation of management with the audit committees and other supervisory bodies of listed entities which is key to ensure the overall internal consistency of the annual financial report and contribute to high-quality annual financial reports. Entities must also consider other international developments in the sustainability area, for instance, formation of a new International Sustainability Standards Board (ISSB) by IFRS foundation to develop a comprehensive global baseline of high-quality sustainability disclosure standards to meet investors' information needs.

Chapter 2

RBI introduces scale-based regulation for NBFCs

This article aims to:

Provide an overview of the scale-based framework prescribed by RBI and regulatory provisions applicable for NBFCs in each layer within the framework.

Introduction

The Non-Banking Finance Companies (NBFC) sector plays a significant complementary role in financial intermediation, along with banks, and caters to the unmet and exclusive credit needs of various segments, such as infrastructure, factoring, leasing, etc. Considering the lower scale of operations of NBFCs vis-à-vis banks, and with an aim of providing them with greater operational flexibility to grow, NBFCs have been enjoying the freedom to undertake a wider spectrum of activities and have less stringent regulatory provisions applicable as compared to banks (often referred to as the regulatory arbitrage in favour of NBFCs).

Over the years, the NBFC sector has shown tremendous growth. However, stress has been observed in the NBFC sector which has generated vulnerabilities by giving rise to systemic risk through the NBFC sectors' interlinkages within the financial system.

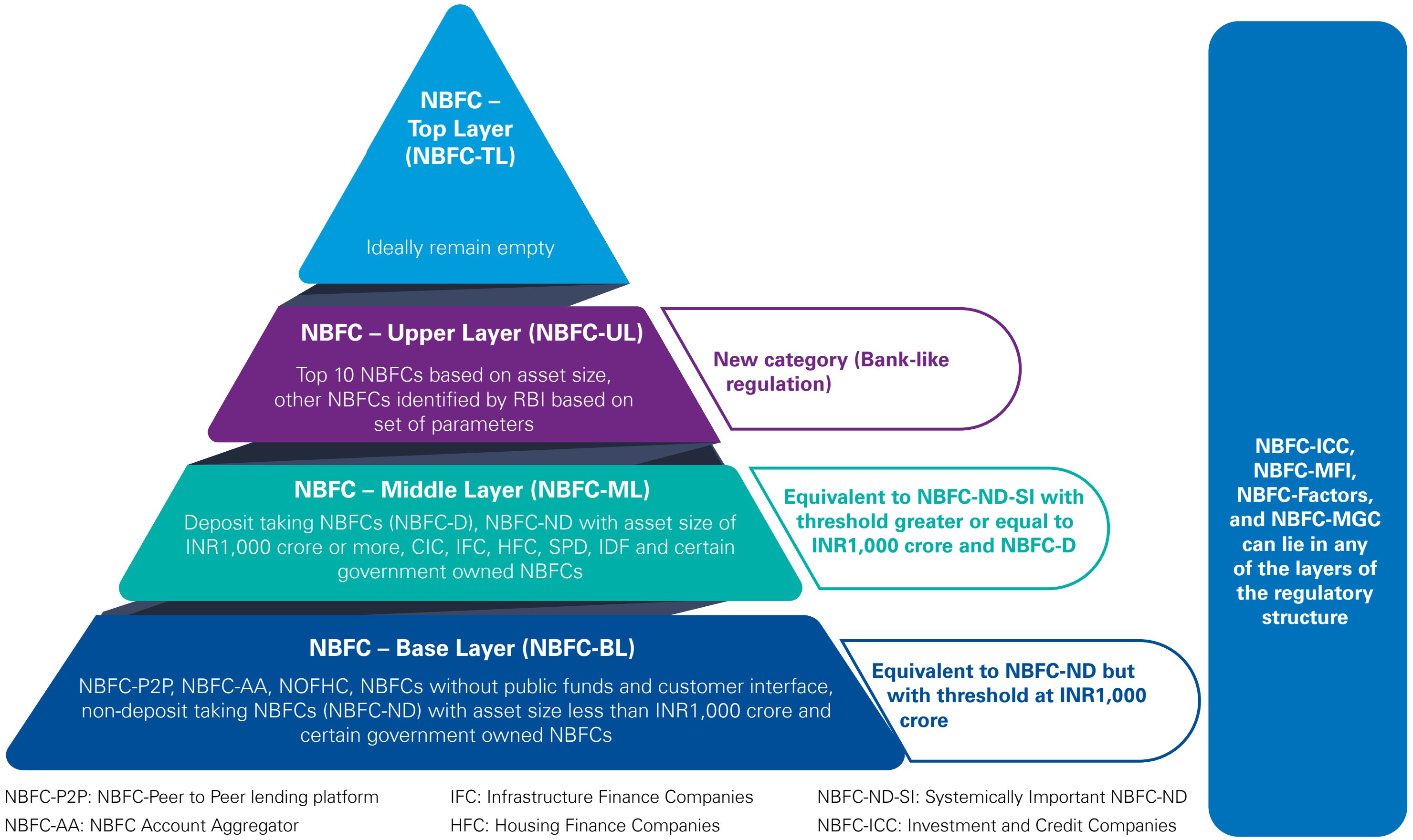
With a view to develop a strong and resilient financial system, in January 2021, the Reserve Bank of India (RBI) had issued a discussion paper on revised regulatory framework for NBFCs. Basis the inputs received from stakeholders, RBI, vide a notification dated 22 October 2021 has prescribed a 'scale-based' regulation for the NBFC sector. The scale-based regulatory approach renders the regulation and supervision of the NBFCs to be a function of their size, activity and perceived riskiness. Thereby, a higher degree of regulation would be applicable for NBFCs that have greater size and complexity and pose a higher risk for the financial system, and a lower degree of regulation would be applicable to NBFCs that pose a lower risk for the financial system, allowing them operational flexibility. These regulations will be applicable to NBFCs effective 1 October 2022. However, the provision with regard to ceiling on IPO funding will be applicable from 1 April 2022.

In this article, we aim to provide an overview of the different layers in the scale-based regulation introduced by RBI, the NBFCs that will be classified in each of these layers, and the revisions in the structural and regulatory framework applicable to the NBFCs in each of the layers.

The scale-based regulatory approach

The scale-based regulatory framework can be visualised as a pyramid with regulatory intervention being the least at the bottom of the pyramid and increasing as one moves up. This is depicted in figure 1 below:

Figure 1: Scale-based regulatory framework



NBFC-P2P: NBFC-Peer to Peer lending platform
NBFC-AA: NBFC Account Aggregator
NOFHC: Non-Operative Financial Holding Company
CIC: Core Investment Companies
IFC: Infrastructure Finance Companies
HFC: Housing Finance Companies
SPDs: Standalone Primary Dealers
IDF: Infrastructure Debt-Fund- NBFCs
NBFC-ND-SI: Systemically Important NBFC-ND
NBFC-ICC: Investment and Credit Companies
NBFC-MFI: Micro Finance Institutions
NBFC:MGC: Mortgage Guarantee Companies

(Source: KPMG in India's analysis, 2021, read with Scale Based Regulation (SBR): A Revised Regulatory Framework for NBFCs issued by RBI on 22 October 2021)

The regulatory structure

Base layer (NBFC-BL)

The **Base Layer** will be equivalent to existing non-deposit taking non-systemically important NBFCs (NBFC-NDs), but with an asset size less than INR1,000 crore. It will specifically include:

- NBFC-P2P,
- NBFC-AA,
- NOFHC and
- NBFCs without public funds and customer interface[1].

While higher level of prudential regulations will not be applicable to such entities, there will be an increase in the transparency requirements by way of greater disclosures and improved governance standards.

Middle layer (NBFC-ML)

The **Middle layer** will be equivalent to the existing deposit taking NBFCs (NBFC-D) and systemically important non-deposit taking NBFCs (NBFC-ND-SI). It will specifically include the SPD and IDF (which will always remain in the middle layer). It will also include NBFC-D, irrespective of their asset size, NBFC-ND-SI with asset size greater than INR1,000 crore, CIC, IFC and HFCs[2]. Government owned NBFCs will not be placed in the upper layer, till further notice, and accordingly, will be placed in NBFC-BL or NBFC-ML.

There will be higher regulatory supervision in this layer, which aims to plug the areas of regulatory arbitrage between banks and NBFCs.

Upper layer (NBFC-UL)

The **Upper layer** has been conceived as a new category of NBFCs, in which a chosen few, systemically significant NBFCs would be specifically identified by RBI through parametric analysis of certain quantitative and qualitative criteria[3], which will be reviewed periodically. Accordingly, entities that meet the specified criteria will move from the middle layer to the upper layer of the scale-based framework. The top 10 eligible NBFCs in terms of their asset size will always reside in the upper layer, irrespective of any other factor. Higher prudential regulations and intensive supervision will be applicable for such entities proportionate to their systemic significance.

1. RBI is expected to come out with separate regulations for such NBFCs in due course.
2. These NBFCs can either be a part of NBFC-ML or NBFC-UL, as the case may be.
3. The quantitative criteria majorly consist of size and leverage, interconnectedness and complexity, and the qualitative criteria majorly consists of nature and type of liabilities, group structure and segment penetration.

Transition path to the upper layer

NBFCs would be advised about their classification to the upper layer

Once an NBFC is identified for inclusion as NBFC-UL, it would be advised about its classification by the Department of Regulation, RBI, and will be placed under the regulation applicable to the upper layer. For this purpose, the following timelines should be adhered to:

- **Board approved policy and implementation plan to be prepared within three months:** Within three months of being advised by the RBI regarding its inclusion in the NBFC-UL, the NBFC should put in place a board approved policy for adoption of the enhanced regulatory framework and chart out an implementation plan for adhering to the new set of regulations. This board approved implementation plan will be submitted to RBI and be subject to supervisory review
- **Adherence with stipulations for NBFC-UL within 24 months:** The Board of Directors (BoD) of the NBFC should ensure that the stipulations prescribed for NBFC-UL are adhered to, and the board approved implementation plan should be subsumed within a maximum time-period of 24 months from the date of advise of the NBFC's classification in the upper layer.

Transition of NBFCs in the upper layer

Once an NBFC is identified as NBFC-UL, it will be subject to enhanced regulatory provisions at least for a period of five years from its classification in this layer, even if it does not meet the parametric criteria in the subsequent year(s). However, an NBFC classified in the upper layer would be allowed to move out of the enhanced regulatory framework only if the movement is reflected as a voluntary strategic move as clearly laid out by its BoD. Therefore, NBFCs classified in the upper layer that have scaled down operations due to adverse situations specific to the NBFC will not be permitted to move down to a lower regulatory regime.

Intimation to NBFCs close to meeting the NBFC-UL parameters

NBFCs which are close to meeting the parameters and benchmarks that would render them eligible for classification as NBFC-UL, will be intimated about the same in advance to enable them to initiate measures and readjust operations in case they intend to continue in the NBFC-ML on a long-term basis and do not want to feature in the upper layer.

Top layer

The **top layer** would ideally remain empty and NBFCs will be slotted into this layer from the upper layer of the scale-based framework at the discretion of the supervisor if it is of the opinion that the entity is contributing significantly to systemic risk. Such entities would be required to comply with significantly higher regulatory and supervisory requirements.

Regulatory changes under the scale-based regulatory framework

The scale-based regulatory framework envisages a progressive increase in the intensity of regulations. Therefore, regulatory revisions[4] applicable to lower layers of NBFCs will automatically be applicable to NBFCs residing in higher layers, unless stated otherwise. The regulatory revisions applicable to the various layers of NBFCs are given in the table below, the notes annexed to the tables provide further explanations of these changes:

Regulatory revision	Regulatory revisions applicable to			Further clarification awaited from RBI	Reference
	NBFC-BL[5]	NBFC-ML[6]	NBFC-UL[7]		
A. Regulatory revisions applicable to all layers of NBFCs					
Revisions in regulatory guidelines					
• Raising net owned fund for certain NBFCs	Raised minimum NOF requirement for NBFC-ICC, NBFC-MFI and NBFC-factors to INR10 crore. A glide path to achieve this requirement has been provided.				Note A.1
• Harmonising Non-Performing Assets (NPA) classification norms	NBFC-ND are now required to classify assets with an overdue period of more than 90 days as NPA. A glide period for complying with this norm has been provided.	No impact, since NBFCs classified under these layers are already required to follow the 90-days NPA norm.			Note A.2
• Experience of the board	At least one of the directors in the BoD should have relevant experience of having worked in a bank/NBFC. This is a new requirement for all NBFCs.				
• Ceiling on Initial Public Offer (IPO) funding	A limit of INR1 crore per borrower has been set for financing subscription to IPOs (currently, NBFCs have no ceiling on IPO funding). Ceiling on IPO funding will be applicable from 1 April 2022.				
Revisions in governance guidelines					
• Risk Management Committee (RMC)	Could be at board or executive level, as per discretion of BoD	Board-level RMC	Board-level RMC		Note A.3
• Disclosures	Expanded disclosure requirements for NBFCs.			✓	Note A.4
• Loans to directors, senior officers and relatives of directors	NBFCs to have a board approved policy on these matters.			✓	Note A.5

4. The regulatory provisions discussed in this article are the revisions that will be made in the existing regulatory framework.
5. NBFC-BL would largely continue to be subjected to regulation that is currently applicable for NBFC-ND. Since NBFC-ND with asset size upto INR1,000 crore will now be classified as NBFC-BL (as per extant regulations, non-deposit taking NBFCs with an asset size of less than INR500 crore are considered as non-systemically important NBFCs. Under the scale-based regulations, non-deposit taking NBFCs with an asset size of upto INR1,000 crore will be classified in the base layer of the regulatory framework. The existing regulatory framework should be supplemented by enhanced governance and disclosure standards. The specific changes in regulations for NBFC-BL is given hereunder.
6. NBFCs in the middle layer will be governed by the extant regulations applicable to NBFC-ND-SIs, NBFC-Ds, CICs, SPDs and HFCs.
7. NBFCs in the upper layer will be subject to regulations applicable to NBFC-ML and to the regulatory revisions sexplained in the table:

Regulatory revision	Regulatory revisions applicable to			Further clarification awaited from RBI	Reference
	NBFC-BL	NBFC-ML	NBFC-UL		
B. Regulatory revisions applicable to NBFC-ML and NBFC-UL					
Revisions in capital guidelines					
• Introduction of Internal Capital Adequacy Assessment Process (ICAAP)	Not applicable	NBFCs in middle and upper layer to make a thorough internal assessment of the need for capital, commensurate with the risks in their business, on similar lines as ICAAP for banks.			Note B.1
Revisions in prudential guidelines					
• Concentration of credit/investment	Extant norms applicable	Merged lending and investment exposure limits into a single exposure limit. Limit to be computed as a percentage of Tier 1 capital.			Note B.2
• Sensitive Sector Exposure (SSE)	Not applicable	BoD approved internal limits to be fixed for SSE, separately for capital market and commercial real estate exposures. HFCs are required to follow extant regulations applicable.			Note B.3
• Regulatory restrictions on loans	Not applicable	Regulatory restrictions applicable on loans to directors, senior officers and on appraising loan proposals involving real estate.		✓	Note B.4
Revisions in governance guidelines					
• Key managerial personnel	Not appliable	Restrictions on KMPs from holding any office (including directorships) in any other NBFC-ML or NBFC-UL.			Note B.5
• Independent director	Not applicable	IDs are restricted from being on the BoD of more than **three NBFCs** at the same time.			Note B.6
• Disclosures in annual financial statements	Not applicable	With effect from **31 March 2023**, NBFCs are required to make the following additional disclosures in annual financial statements: • Corporate governance report • Disclosure on modified opinion • Exceptional income or expenses • Breaches in terms of covenants or defaults • Divergence in asset classification and provisioning.		✓	Note B.7

Regulatory revision	Regulatory revisions applicable to			Further clarification awaited from RBI	Reference
	NBFC-BL	NBFC-ML	NBFC-UL		
Revisions in governance guidelines					
• Chief compliance officer	Not applicable	Mandatory	Mandatory	✓	Note B.8
• Compensation guidelines	Not applicable	NBFCs to put in place a BoD approved compensation policy, which includes: • Constitution of remuneration committee • Principles for fixed/variable pay structures • Malus/claw back provisions.			Note B.6
• Additional governance matters	Not applicable	Additional governance matters to be complied with include: • Delineate the role of various committees • Formulate a whistle blower mechanism • Ensure good corporate governance practices in subsidiaries.		✓	Note B.10
• Introduction of core banking solution	Not applicable	Mandatory for NBFCs with 10 or more branches	Mandatory for NBFCs with 10 or more branches	✓	Note B.11
C. Regulatory revisions applicable only to NBFC-UL					
Revisions in capital guidelines					
• Common Equity Tier 1	Not applicable	Not applicable	CET 1 of at least **nine per cent of risk weighted assets**[8]	✓	-
• Leverage	Not applicable	Not applicable	Leverage requirement will be applicable.	✓	Note C.1
• Differential standard asset provisioning	Not applicable	Not applicable	Differential standard asset provisioning applicable, similar to provisions applicable to banks.	✓	Note C.2

8. Currently, the provisions with regard to maintenance of CET 1 is not applicable to NBFCs.

Regulatory revision	Regulatory revisions applicable to			Further clarification awaited from RBI	Reference
	NBFC-BL	NBFC-ML	NBFC-UL		
Revisions in prudential guidelines					
• Large Exposure Framework (LEF)	Not applicable	Not applicable	Guidelines on LEF to be issued by RBI. Credit concentration norms (under Note B.2) to be followed till these norms are made applicable	✓	Note C.3
• Internal exposure limits	Not applicable	Not applicable	BoD approved internal exposure limits to be set for important sectors to which credit is extended[9]. This is in addition to SSE limits (refer note B.3)		-
Revision in governance guidelines					
• Qualification of board members	Not applicable	Not applicable	Composition of BoD to include a mix of educational qualification and experience		Note C.4
• Listing and disclosures	Not applicable	Not applicable	NBFCs to get listed within three years of identification as NBFC-UL. Disclosure requirements applicable even before entity is listed		Note C.5
• Removal of independent directors	Not applicable	Not applicable	NBFC-UL to report to supervisors in case any ID is removed/resigns before the completion of his/her normal tenure. Such reporting was not required by NBFCs earlier		-

9. This is a new provision, NBFCs were not required to set such internal limits earlier.

Note A: Revisions in regulatory guidelines applicable to all layers of NBFCs

Revisions in regulatory guidelines

1. **Raising Net Owned Fund (NOF) for certain NBFCs:** As per the extant regulatory framework applicable to the NBFC sector, certain NBFCs (such as NBFC-MFI, NBFC-Factors, NBFC-ICC) have a minimum NOF requirement of less than INR10 crore.

   RBI assessed that the ability of NBFCs to perform their role effectively and efficiently requires them to be adequately capitalised, financially resilient, and well-regulated so that they retain the confidence of their stakeholders, including their lenders and borrowers. In this regard, RBI felt the need to have stronger entry point norms that would lower the chances of failure arising from poor governance of non-serious players. Accordingly, RBI requires the minimum NOF for NBFC-ICC, NBFC-MFI and NBFC-factors to be increased to INR10 crore[10].

   In order to ensure non-disruptive transition, a well-defined glide path has been provided for the existing NBFCs to achieve the NOF. The glide path is given below:

NBFCs	Current NOF	NOF By 31 March 2025	NOF by 31 March 2027
NBFC-ICC	INR2 crore	INR5 crore	INR10 crore
NBFC-MFI	INR5 crore (INR2 crore in north-east region)	INR7 crore (INR5 crore in north-east region)	INR10 crore
NBFC-Factors	INR5 crore	INR7 crore	INR10 crore

2. **Harmonisation of NPA classification norms:** Currently the NBFCs-ND with an asset size of less than INR500 crore (i.e., non-systemically important, non-deposit taking NBFCs) classify assets with an overdue period of more than 180 days as NPA (NPA norm). All other NBFCs have an NPA norm of 90 days.

   RBI has now harmonised the NPA norms for all NBFCs to 90 days. This amendment will impact the NBFC-BL, which includes the NBFCs-ND. Accordingly, a glide path has been provided to NBFCs in the base layer to adhere to the 90 days NPA norm, as given below:

NPA norms	Timeline
> 150 days	By 31 March 2024
> 120 days	By 31 March 2025
> 90 days	By 31 March 2026

Clarifications issued by RBI on NPA classification

On 1 October 2021, RBI issued a Master Circular on Prudential Norms on Income Recognition, Asset Classification and Provisioning (IRACP)[11], which is applicable to all Commercial Banks (excluding Regional Rural Banks). Subsequently, on 12 November 2021, RBI issued a circular, providing certain clarifications on IRACP norms to ensure uniformity in its implementation and harmonising certain requirements for all lending institutions[12]. Some clarifications that will impact NPA classification for NBFCs, include:

- **Classification as Special Mention Account (SMA) and NPA:** The 'Prudential Framework for Resolution of Stressed Assets' requires lenders to recognise incipient stress in borrower accounts, immediately on default by classifying them as SMA. Further, these assets will be classified as NPA when they are overdue for more than 90 days. The general practice amongst NBFCs is to report SMAs/ NPAs based on position of the loan accounts at month end or quarter end.

  RBI has now clarified that borrower accounts should be flagged as overdue as part of the day end process for the 'due date' (and not at month end). This clarification is effective on an immediate basis.

- **SMA classification applicable to NBFC-ND:** Currently, the requirement to classify overdue borrower accounts as SMA as prescribed by the 'Prudential Framework for Resolution of Stressed Assets' is applicable to NBFC-ND-SI and NBFC-D, however, it is not applicable to NBFC-ND (i.e. non-systemically important, non-deposit taking NBFCs).

  With the clarifications issued by RBI, these provisions will now apply even to NBFC-ND. However, references to '90 days' for SMA-2/ NPA classification may be read as per the NPA norms applicable to NBFC-ND.

- **Upgradation of accounts classified as NPAs:** The IRACP norms specify that banks should upgrade accounts classified as NPA to 'standard' account, if arrears of interest and principal are paid by the borrower. RBI observed that many lending institutions upgrade NPA accounts to 'standard' category upon payment of only interest overdues, partial overdues, etc.

  RBI has now clarified that loan accounts classified as NPAs may be upgraded as 'standard' asset only if entire arrears of interest and principal are paid by the borrower. This clarification is effective on an immediate basis.

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10. NOF for NBFC-P2P, NBFC-AA and NBFCs with no public funds and no customer interface should continue to be INR2 crore. Further, there is no change in the existing regulatory minimum NOF for NBFCs-IDF, IFC, MGCs, HFC and SPD.

11. Earlier, the master circular on IRACP norms issued on 1 July 2015 was applicable to banks.

Revisions in governance guidelines

3. **Risk management committee (RMC):** NBFCs are currently required to set up a RMC that would be responsible for evaluating the overall risks faced by the NBFC including liquidity risk and report to the BoD of the NBFC. The regulatory revisions now require the decision on composition of the RMC as a board-level committee or executive-level committee to be left to the discretion of the BoD of the NBFC.

4. **Disclosures[12]:** Disclosure requirements for NBFCs will be expanded to, *inter alia*, include types of exposures, related party transactions, loans to directors/senior officers and customer complaints. Currently, NBFCs are not required to make such disclosures.

5. **Loans to directors, senior officers and relatives of directors[13]:** NBFCs will be required to have a BoD approved policy on grant of loans to directors, senior officers, relatives of directors and to entities where directors or their relatives have major shareholding. Currently, NBFCs do not have any such policy.

Note B: Regulatory revisions applicable to NBFC-ML and NBFC-UL

In addition to Note A, the following regulatory revisions will be applicable to NBFCs in the middle and upper layer of the scale-based framework:

Revisions in Capital guidelines

1. **Introduction of Internal Capital Adequacy Assessment Process (ICAAP):** The objective of ICAAP is to ensure availability of adequate capital to support all risks in the business and also to encourage NBFCs to develop and use better risk management techniques for monitoring and managing their risks.

   As per the extant regulatory norms, NBFC-ND-SI and NBFC-D are on Basel I type framework (i.e., uniform risk weights for counterparties, market risk or operations risk is not considered when determining capital requirements) and are required to have a minimum capital of 15 per cent of the Risk Weighted Assets (CRAR).

   The regulatory revisions now require NBFCs in the middle and upper layer to make a thorough internal assessment of the need for capital, commensurate with the risks in their business. This internal assessment would be on similar lines as ICAAP prescribed for commercial banks under Pillar 2. For this purpose, NBFCs should consider credit risk, market risk, operational risk and all other residual risks as per methodology to be determined internally. This will facilitate an active dialogue between RBI and NBFCs on the assessment of risks and monitoring as well as mitigation of the same.

Revisions in prudential guidelines

2. **Concentration of credit/investment:** The extant regulatory norms prescribe separate limits for lending and investment exposures (concentration limits) for a single borrower and a group of connected borrowers. These concentration limits are computed as a percentage of owned funds.

   The regulatory revision has now merged the separate lending and investment exposure limit into a single exposure limit of 25 per cent for single borrower/party, and 40 per cent for single group of borrowers/parties[14]. Further, the concentration limits will be determined with reference to the NBFC's Tier 1 capital (instead of owned fund), as is currently applicable to banks.

   NBFC-UL should follow these norms till 'Large Exposure Framework' is put in place for them.

3. **Sensitive Sector Exposure (SSE):** Exposure to capital market (direct and indirect) and commercial real estate is reckoned as sensitive sector exposure for NBFCs. Currently, only HFCs are subject to specific regulation on SSE.

   RBI considered that the concentration risk resulting from undiversified portfolios, particularly in sensitive sectors, could prove detrimental to an NBFC's health. However, specifying hard coded sector-specific exposure limits may tantamount to altering the basic business model and risk appetite of certain NBFCs.

   Accordingly, regulatory revisions now require NBFCs to fix BoD approved internal limits for SSE separately for capital market and commercial real estate exposures. Further, NBFCs should conduct periodic dynamic vulnerability assessments of various sectors, which would help them determine such internal limits. While BoD of NBFCs are free to determine various sub-limits within the overall SSE internal limits, a sub-limit within commercial real estate exposure should be fixed for financing land acquisition.

   HFCs are required to follow specific regulations on SSE as per extant regulations[15].

4. **Regulatory restrictions on loans:** Currently, regulatory restrictions on loans and advances have not been imposed on NBFCs.

   The regulatory revisions have now extended regulatory restrictions in respect of:

   - **Loans to directors:** Granting loans and advances to directors, their relatives and to entities where directors or their relatives have major shareholding
   - **Loans to senior officers:** Granting loans to senior officers of NBFCs

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12. This includes all commercial banks, co-operative banks, All-India Financial Institutions and all NBFCs (including HFCs).
13. RBI will be issuing a detailed circular on these provisions.
14. Extant instructions on concentration norms for different categories of NBFC, other than the changes above, will continue to remain applicable.
15. These regulations are specified in paragraph 22 and 23 of Master Direction – Non-Banking Finance Company – Housing Finance Company (Reserve Bank) Directions, 2021

- **Appraising loan proposals involving real estate:** While appraising loan proposals involving real estate, NBFCs should ensure that borrowers have obtained prior permission from government/statutory authorities. Further, disbursements should be made only after the borrower has obtained requisite clearances form the government authorities.

(A detailed circular on these provisions will be issued by RBI in due course).

Revisions in governance guidelines

5. **Key Managerial Personnel (KMP):** The extant regulations do not lay any restriction on the offices and directorships that KMPs[16] of NBFCs can hold.

   The regulatory revisions have now restricted KMPs from holding any office (including directorships) in any other NBFC-ML or NBFC-UL. However, directorship in the subsidiary of the NBFC in which the individual is a KMP and directorship in NBFC-BL will be permitted. A timeline of two years, with effect from 1 October 2022 has been provided to KMP to ensure compliance with these norms.

6. **Independent Directors (ID):** The extant regulations do not lay any restriction on the number of directorships of IDs in NBFCs.

   In order to ensure that there is no conflict arising out of IDs being on the BoD of various NBFCs at the same time, including those of competing NBFCs, RBI has now restricted IDs from being on the BoD of more than **three NBFCs** at the same time[17] (restriction is applicable for IDs from being on the BoD of NBFC-ML and NBFC-UL, however there is no restriction on number of directorships in NBFC-BL). The onus of ensuring that there is no conflict will lie with the BoD of the NBFC.

7. **Disclosures in annual financial statements[13]:** As per the extant regulations, NBFCs are required to make certain regulatory disclosures in the annual financial statements.

   In addition to the existing disclosure requirements, NBFCs are required to make the following disclosures with effect from 31 March 2023:

   - **Corporate governance report** containing composition and category of directors, shareholding of non-executive directors, etc.
   - **Disclosure on modified opinion** (if any) expressed by auditors, its impact on various financial items and views of management on audit qualifications
   - **Exceptional income or expenses** during the period
   - **Breaches in terms of covenants or defaults** in respect of loans availed by NBFC or debt securities issued
   - **Divergence in asset classification and provisioning** above a certain threshold to be prescribed by RBI.

8. **Chief Compliance Officer (CCO)[13]:** There is no current provision for appointment of a CCO by NBFCs.

   RBI observed that a compliance function has to be adequately enabled and made sufficiently independent so that it can ensure strict observance of all statutory and regulatory provisions.

   In this view, the regulatory revisions require NBFCs to appoint a CCO who would be sufficiently senior in the organisation hierarchy. NBFCs should also put in place a BoD approved policy laying down the role and responsibilities of the CCO with the objective of promoting better compliance culture in the organisation.

9. **Compensation guidelines[13]:** Currently, there are no compensation guidelines in place for NBFCs.

   In order to address issues arising out of excessive risk taking caused by misaligned compensation packages, it has been decided that NBFCs should put in place a BoD approved compensation policy. The guidelines should at the minimum include:

   - Constitution of remuneration committee
   - Principles for fixed/variable pay structures
   - Malus/claw back provisions.

   The Nomination and Remuneration Committee should ensure that there is no conflict of interest.

10. **Additional governance matters[13]:** RBI requires some additional governance matters to be complied with by NBFCs, these include:

    - BoD should delineate the role of various committees (audit committee, nomination and remuneration committee, risk management committee or any other committee) and lay down a calendar of reviews
    - NBFCs should formulate a whistle blower mechanism for directors and employees to report genuine concerns
    - BoD should ensure good corporate governance practices in subsidiaries of NBFCs.

11. **Introduction of Core Banking Solution (CBS)[13]:** Banks have implemented CBS which has brought significant benefits, including transparency, efficiency, reducing the scope of fraudulent flow and enhanced customer service experiences. NBFCs are currently not required to adopt CBS. With a view to inculcate similar benefits in NBFCs, RBI now requires NBFCs in the middle and upper layer of the scale-based framework, with 10 or more branches to mandatorily adopt CBS. A glide path of three

16. As defined in Section 2(51) of the Companies Act, 2013.
17. Limits permitted by the Companies Act, 2013 should be considered.

years with effect from 1 October 2022 has been provided for the same.

Note C: Regulatory revisions applicable to NBFC-UL

In addition to Notes A and B, the following regulatory revisions will be applicable to NBFCs in the upper layer of the scale-based framework:

Revisions in capital guidelines

1. **Leverage[13]:** NBFCs are currently required to maintain a CRAR of 15 per cent. However, there is no leverage ratio[18] applicable to them.

   As per RBI, the NBFC-UL should be subjected to leverage requirement to ensure that their growth is supported by adequate capital, among other factors. A suitable ceiling will be prescribed subsequently by RBI.

2. **Differential standard asset provisioning[13]:** Systemically important NBFCs are currently subject to a flat rate of 0.40% as standard asset provision, whereas banks are subject to differential rate of standard asset provisioning for different sectors they lend to[19].

   In order to tune the regulatory framework for NBFC-UL to greater sensitivity, RBI now prescribes differential standard asset provisioning for NBFC-UL which would be similar to provisions applicable to banks.

Revisions in prudential guidelines

3. **Large Exposure Framework:** RBI has decided to introduce Large Exposure Framework for NBFCs placed in the upper layer. This framework is currently applicable to banks. Accordingly, large exposure of an NBFC to all counterparties and groups of connected counterparties (as will be defined by RBI) will be considered for exposure ceilings. Simplified and separate guidelines on this will be issued in due course.

Revision in governance guidelines

4. **Qualification of board members:** Currently, NBFCs should ensure that the directors appointed in the BoD meet the 'fit and proper' criteria as specified in the extant regulatory provisions.

   RBI now requires NBFCs in the upper layer to ensure that the composition of BoD include a mix of educational qualification and experience. Specific expertise of BoD members should be a prerequisite depending on the type of business pursued by the NBFC.

5. **Listing and disclosures:** Currently, there is no specific requirement for NBFCs to mandatorily get listed on a stock exchange, however, certain banks are required to get listed within a prescribed period.

   NBFCs lying in the upper layer of the scale-base framework have the ability to cause adverse systemic risks, and hence need to maintain higher corporate governance standards and a diffused ownership structure to minimise the possibility of abuse of dominance. Accordingly, RBI has mandated such NBFCs to get listed within three years of identification as NBFC-UL. Disclosure requirements would be put in place on the same lines as applicable to a listed entity, even before the actual listing.

Our comments

- Over the years, the NBFC sector has evolved in terms of its size, operations, technological sophistication with entry into newer areas of financial services and products. To keep pace with the same, regulations also need to evolve to address the accompanying risks and concerns. With the revised scale-based framework, RBI aims to increase regulatory supervision, governance and disclosures of NBFCs, the aim of which is to keep in check the vulnerabilities posed by NBFCs with large scale operations and pose systemic risk in the financial system.
- RBI has introduced some significant regulatory guidelines for NBFCs in the middle and upper layer of the scale-based framework. This, *inter alia*, includes introducing ICAAP, ceiling on IPO funding, having BoD approved policies for SSE and large exposure frameworks, adoption of CBS for certain NBFCs, mandatory listing for NBFCs in the upper layer, capping the maximum number of directorships for IDs of NBFCs and the directorships and other interests of KMP of NBFCs. Some of these requirements will require significant restructuring in the governance and operating norms of NBFCs. However, RBI has provided adequate transition period to meet these requirements.
- The institution of IDs plays a crucial role in governance of entities. Provisions pertaining to IDs have been under constant review by all regulators. Companies and IDs of companies will need to consider the provisions of all regulations while appointing or accepting the appointment as IDs in companies. The maximum number of directorships prescribed for IDs under the Companies Act, 2013, the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR) and the scale-based framework has been given below:
  - As per the **Companies Act, 2013**, a person can hold directorship, including alternative directorship in not more than 20 companies, and not more than 10 public companies
  - As per **LODR,** directors of entities that have listed their specified securities[20] on a recognised stock exchange (listed entities) or directors of high value debt listed entities[21] should not hold directorship in more than seven listed entities. Further, a person should

18. The Basel Committee on Banking Supervision introduced 'leverage ratio' in the 2010 Basel III package of reforms. The leverage ratio is defined as the capital measure divided by exposure measure, expressed as a percentage. The leverage ratio basically calculates a bank's health.
19. For example, farm credit and SME @ 0.25%, CRE @ 1.0%, CRE-RH @ 0.75%, and all other loans @ 0.4%
20. Specified securities are defined as equity shares and convertible securities in the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirement) Regulations, 2015.
21. Entities that have listed their non-convertible debt securities exceeding INR500 crore

not serve as an ID in more than seven listed entities. Additionally, a person who is serving as a whole-time director/managing director in any listed entity should not serve as an ID in more than three listed entities

- As per the scale-based framework, IDs of NBFCs in the middle and upper layer of the scale-based framework should not be on the BoD of more than three NBFCs at the same time (restriction is for NBFC-ML and NBFC-UL only, and not to directorships in NBFC-BL). Further, the KMP of NBFCs in the middle and upper layer of the scale-based framework should not hold any office (including directorships) in any other NBFC-ML and NBFC-UL (directorship in NBFC-BL is permitted).

- As per the scale-based regulations, once NBFCs have been identified to be classified in the upper layer of the scale-based framework, they will need to get listed within three years of such classification. Therefore, it seems that the listing requirements will be applicable to NBFCs even when they don't meet the parametric requirements in subsequent years (post the NBFC-UL classification), unless they strategically reduce the scale of their operations.

- RBI, in its circular dated 12 November 2021, provided a clarification on IRACP norms i.e. loan accounts classified as NPAs may be upgraded as 'standard' assets only if entire arrears of interest and principal are paid by the borrower. Till date most NBFCs have been upgrading accounts classified as NPA on partial payment, such as payment of only interest or only one installment. However, with this clarification, loans accounts classified as NPA will remain as such till the time the entire outstanding amount of interest and principal is repaid. Accordingly, accounts classified as NPA cannot be upgraded to SMA, they will directly be classified as zero days past due. This will result in a higher number of accounts being classified as NPAs, and thereby a higher asset provisioning and capital requirements for NBFCs.

Chapter 3

Regulatory updates

SEBI issued amendments to the related party framework under LODR

SEBI through a notification dated 9 November 2021 has issued certain amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR). Consequent disclosure obligations have been laid down in a separate circular dated 22 November 2021[1].

Key amendments are as follows:

- **Definition of related parties:** The definition of related party has been amended, and would include:
  - a. A 'related party' as defined under Section 2(76) of the Companies Act, 2013 (2013 Act) and the applicable accounting standards or Ind AS,
  - b. Any person or entity forming a part of the 'promoter' or promoter group' of the listed entity (effective from 1 April 2022)
  - c. Any person or any entity, holding equity shares in the listed entity either directly or on a beneficial interest basis as prescribed under Section 89 of the 2013 Act at any time during the immediately preceding financial year:
    - of 20 per cent or more, or (effective from 1 April 2022)
    - of 10 per cent or more (effective from 1 April 2023).
- **Definition of RPTs:** The definition of Related Party Transactions (RPTs) has been amended to include transactions carried out between:

  a. A listed entity or any of its subsidiaries on one hand and a related party of the listed entity or any of its subsidiaries on the other hand or (effective from 1 April 2022)

  b. A listed entity or any of its subsidiaries on one hand, and any other person or entity on the other hand, the purpose and effect of which is to benefit a related party of the listed entity or any of its subsidiaries (effective from 1 April 2023).

  The above transactions would be considered as RPTs regardless of whether a price has been charged.

  Additionally, following transactions are excluded from the definition of RPTs (effective 1 April 2022):

  a. The issue of specified securities on a preferential basis subject to compliance of the requirements under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018

  b. Corporate actions by the listed entity which are uniformly applicable/offered to all shareholders in proportion to their shareholding such as payment of dividend, subdivision or consolidation of securities, issuance of securities by way of a rights issue or a bonus issue and buy-back of securities.

  c. Acceptance of fixed deposits by banks/ Non-Banking Finance Companies (NBFCs) at the terms uniformly applicable/offered to all shareholders/public, subject to disclosure of the same along with the disclosure of RPTs every six months to the stock exchange(s), in the specified format.

  d. Units issued by mutual funds which are listed on a recognised stock exchange.
- **Shareholders' approval for RPTs:** The amendment requires prior approval of the shareholders of a listed entity for all material RPTs and **subsequent material modifications of such transactions** (effective 1 April 2022).

  (Emphasis added to highlight the change)

  However, a prior approval of the shareholders would not be required if the transaction is entered into by a listed subsidiary of the listed entity, and the subsidiary is subject to compliance with Regulation 23 and Regulation 15(2) of the LODR. Further, for RPTs of unlisted subsidiaries of a listed subsidiary, prior approval of the shareholders of the listed subsidiary would suffice.

1. The provisions of the circular shall come into force with effect from 1 April 2022.

Information to be provided to shareholders

The notice being sent to the shareholders seeking approval for any proposed RPT shall, in addition to the requirements under the 2013 Act, include the following information as part of the explanatory statement:

a. A summary of the information provided by the management of the listed entity to the audit committee

b. Justification for why the proposed transaction is in the interest of the listed entity

c. Percentage of the counter party's annual consolidated turnover that is represented by the value of the proposed RPT on a voluntary basis

d. A statement that the valuation or other external report, if any, relied upon by the listed entity in relation to the proposed transaction will be made available through the registered email address of the shareholders

e. Percentage of the counter-party's annual consolidated turnover that is represented by the value of the proposed RPT on a voluntary basis.

- **Materiality threshold:** In accordance with the revised definition of materiality, an RPT would be considered material, if the transaction entered into individually or taken together with previous transactions during a financial year, exceeds **INR 1,000 crore** or 10 per cent of the consolidated annual turnover of the listed entity as per last audited financial statements, whichever is lower (effective from 1 April 2022).

  (Emphasis added to highlight the change)

- **Audit committee approval:** The amendment requires prior approval of the audit committee of the listed entity in the following circumstances:

  a. All RPTs and subsequent material modifications as defined by the audit committee (effective from 1 April 2022)

  b. A RPT to which the subsidiary of a listed entity is a party, but the listed entity is not a party if the value of such transaction whether entered into individually or taken together with previous transactions during a financial year exceeds threshold of:

     i. 10 per cent of the annual consolidated turnover in accordance with the last audited financial statements of the listed entity (effective from 1 April 2022)

     ii. 10 per cent of the annual standalone turnover in accordance with the last audited financial statements of the subsidiary (effective from 1 April 2023).

Additionally, audit committee approval would not be required if the listed subsidiary is subject to compliance with Regulation 23 and Regulation 15(2) of the LODR. Furthermore, the amendments clarify that for RPTs of unlisted subsidiaries of a listed subsidiary, prior approval of the audit committee of the listed subsidiary would suffice.

Information to be reviewed by the audit committee for approval of RPTs

The listed entity shall provide the following information, for review of the audit committee for approval of a proposed RPT:

a. Type, material terms and particulars of the proposed transaction

b. Name of the related party and its relationship with the listed entity or its subsidiary, including nature of its concern or interest (financial or otherwise)

c. Tenure of the proposed transaction (particular tenure shall be specified)

d. Value of the proposed transaction

e. The percentage of the listed entity's annual consolidated turnover for the immediately preceding financial year, that is represented by the value of the proposed transaction. For a RPT involving a subsidiary, such percentage calculated on the basis of the subsidiary's annual turnover on a standalone basis shall be additionally provided.

f. If the transaction relates to any loans, inter-corporate deposits, advances or investments made or given by the listed entity or its subsidiary:

   i. Details of the source of funds in connection with the proposed transaction

   ii. Where any financial indebtedness is incurred to make or give loans, inter-corporate deposits, advances or investments – nature of indebtedness, cost of funds and tenure

   iii. Applicable terms, including covenants, tenure, interest rate and repayment schedule, whether secured or unsecured; if secured, the nature of security and

   iv. The purpose for which the funds will be utilised by the ultimate beneficiary of such funds pursuant to the RPT.

g. Justification as to why the RPT is in the interest of the listed entity

h. A copy of the valuation or other external party report, if any such report has been relied upon

i. Percentage of the counter-party's annual consolidated turnover that is represented by the value of the proposed RPT on a voluntary basis

j. Any other information that may be relevant.

Additionally, the audit committee shall review the status of long-term (more than one year) or recurring RPTs on an annual basis.

- **Enhanced disclosures:** As per the amendment, listed entities will be required to provide RPT disclosures under Regulation 23(9) of the LODR every six months in the format specified by SEBI (vide circular dated 22 November 2021) within the following timelines:

  a. Within 15 days from the date of publication of the standalone and consolidated financial results (effective 1 April 2022)

  b. On the date of publication of its standalone and consolidated financial results (effective 1 April 2023).

(Source: SEBI notification no. SEBI/LAD-NRO/GN/2021/55 dated 9 November 2021 and SEBI circular no. SEBI/HO/CFD/CMD1/CIR/P/2021/662 dated 22 November 2021)

Scheme of arrangement by listed entities

Recently, SEBI has issued certain amendments to its master circular (no. SEBI/HO/CFD/DIL1/CIR/P/2020/249) dated 22 December 2020 which laid down the framework for schemes of arrangement by listed entities. The amendments mainly prescribe additional documents to be submitted with the stock exchanges before the scheme is sanctioned by the NCLT. Those are as follows:

a. In accordance with the master circular, listed entities are required to submit a valuation report with the stock exchange. The amendments additionally require listed entities to submit an undertaking that no material event impacting the valuation has occurred during the intervening period of filing the scheme documents with stock exchange and period under consideration for valuation.

b. Declaration from the listed entity on any past defaults of listed debt obligations of the entities forming part of the scheme.

c. No Objection Certificate (NOC) from the lending scheduled commercial banks/financial institutions/debenture trustees[2].

d. A report from its audit committee and the independent directors certifying that the listed entity has compensated the eligible shareholders.

Both the reports shall be submitted within seven days of compensating the shareholders.

(Source: SEBI circular no. SEBI/HO/CFD/DIL2/CIR/P/2021/0000000657 dated 16 November 2021 and SEBI circular no. SEBI/HO/CFD/DIL2/CIR/P/2021/0000000659 dated 18 November 2021)

FAQs on Share-based and Sweat Equity Regulations

In August 2021, SEBI notified the SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021 (Share-based and Sweat Equity Regulations).

On 16 November 2021, SEBI has issued certain clarifications in respect of terms/concepts related to the Share-based and Sweat Equity Regulations.

Some of the key clarifications are as follows:

- **Definition of employee:** With respect to definition of an employee under the Share-based and Sweat Equity Regulations, term 'exclusively working in India or outside India' means any employee who is exclusively working with such a company, irrespective of whether such person is employed either in India or outside India.
- **Eligibility of contractual employees:** It has been clarified that contractual employees are also eligible to receive benefits under the Share Based Employee Benefits schemes provided they

2. SEBI circular dated 18 November 2021.

are designated as employees by their employers and are exclusively working with such a company or its group company including subsidiary, its associate company, or its holding company.

- **Benefits granted to employees of group companies:** Shareholders are required to approve the grant of options, Stock Appreciation Rights (SAR), shares or other benefits, as the case may be, to employees of a group company including subsidiaries, its associate companies, joint ventures, or holding company.
- **Benefits to directors:** As per the clarification, grants, SARs or other benefits granted and not vested to the directors who have vacated the office due to retirement would continue to vest in accordance with the respective vesting schedules even after the cessation of directorship due to retirement. This is subject to the terms of the company's policies.
- **Employee welfare scheme with no share-based benefits:** General Employee Benefits Scheme (GEBS) has been defined as any scheme of a company framed in accordance with the Share-based and Sweat Equity Regulations dealing in shares of the company or the shares of its listed holding company, for the purpose of employee welfare including healthcare benefits, hospital care or benefits, or benefits in the event of sickness, accident, disability, death or scholarship funds, or such other benefit as specified by such a company. Therefore, any employee welfare scheme holding/dealing in shares of the company or the shares of its listed holding company is covered under the scope of Share-based and Sweat Equity Regulations, including the timelines prescribed thereunder.

(Source: SEBI FAQs on Share-based and Sweat Equity Regulations issued on 16 November 2021)

MCA issued amendments to the IEPF Rules

On 9 November 2021, the Ministry of Corporate Affairs (MCA) has issued certain amendments to the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016 (IEPF Rules). Key amendments are as follows:

- **Documents to be submitted to register transmission of securities:** Currently, Schedule II of the IEPF Rules prescribe list of documents to be submitted to the IEPF authority to register transmission of securities held in physical mode and DEMAT mode. In accordance with Schedule II, certain documents are required to be furnished if the value of securities is up to **INR2 lakh** per issuer company as on date of application including succession certificate or probate of will or will or letter of administration or decree, as may be applicable in terms of Indian Succession Act, 1925.

  The amendments have increased the above-mentioned threshold from INR2 lakh to **INR5 lakh.** Further, the company may enhance the limit of INR5 lakh per issuer company in accordance with Schedule VII of the LODR after taking approval of its board of directors and provide copy of board resolution to IEPF Authority at the time of verification of claim.
- **Documents to be submitted in case of loss of securities held in physical mode:** As per the amendments, in case of loss of securities held in physical mode, claimant is required to submit a copy of advertisement issued in at least one English language national daily newspaper with nationwide circulation and in one regional language daily newspaper published in the place of registered office of company, if the market value of shares is greater than **INR5 lakh** (earlier INR10,000).
- **Revised Form no. IEPF-5: The amendments** have also issued revised format for making an application to the IEPF authority for claiming unpaid amounts and shares out of IEPF in Form no. IEPF-5.

  Effective date: The amendments are effective from the date of their publication in official gazette i.e., 9 November 2021.

(Source: MCA notification no. G.S.R. 785(E) dated 9 November 2021)

Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances

On 1 October 2021, the Reserve Bank of India (RBI) has issued a master circular on matters relating to prudential norms on Income Recognition, Asset Classification and Provisioning (IRACP) pertaining to advances.

With a view to ensure uniformity in the implementation of IRACP norms across all lending institutions, on 12 November 2021, RBI has issued certain clarifications which will be applicable *mutatis mutandis* to all lending institutions. Those are as follows:

- **Specification of due date/repayment date:** The extant instructions on IRACP norms specify that an amount is to be treated as overdue if it is not paid on the due date fixed by the bank. In this context, RBI clarified that the exact due dates for repayment of a loan, frequency of repayment, breakup between principal and interest, etc.

should be clearly specified in the loan agreement. Further, the borrower should be apprised of the same at the time of loan sanction and also at the time of subsequent changes, if any, to the sanctioned terms/loan agreement till full repayment of the loan.

In cases of loan facilities with moratorium on payment of principal and/or interest, the exact date of commencement of repayment should also be specified in the loan agreements.

These instructions shall be complied with at the earliest, but not later than 31 December 2021, in respect of fresh loans. In case of existing loans, compliance to these instructions shall necessarily be ensured as and when such loans become due for renewal/review.

- **Classification as Special Mention Account (SMA) and Non-Performing Asset (NPA):** RBI's 'Prudential Framework for Resolution of Stressed Assets' requires the lenders to recognise incipient stress in borrower accounts, immediately on default, by classifying them as SMA. To remove ambiguity, RBI has clarified that the intervals are intended to be continuous and accordingly, the basis for classification of SMA categories shall be as follows:

Loans other than revolving facilities		Loans in the nature of revolving facilities like cash credit/overdraft	
SMA sub-categories	Basis for classification- Principal or interest payment or any other amount wholly or partly overdue	SMA sub-categories	Basis for classification- Outstanding balance remains continuously in excess of the sanctioned limit or drawing power, whichever is lower, for a period of:
SMA-0	Up to 30 days		
SMA-1	More than 30 days and up to 60 days	SMA-1	More than 30 days and up to 60 days
SMA-2	More than 60 days and up to 90 days	SMA-2	More than 60 days and up to 90 days

Further, it has been clarified that borrower accounts shall be flagged as overdue by the lending institutions as part of their day-end processes for the due date, irrespective of the time of running such processes. Similarly, classification of borrower accounts as SMA as well as NPA shall be done as part of day-end process for the relevant date and the SMA or NPA classification date shall be the calendar date for which the day end process is run. In other words, the date of SMA/NPA shall reflect the asset classification status of an account at the day-end of that calendar date.

The instructions on SMA classification of borrower accounts are applicable to all loans[3], including retail loans, irrespective of size of exposure of the lending institution.

- **Definition of an 'out of order':** An account shall be treated as 'out of order' if:

  a. The outstanding balance in the Cash Credit (CC)/Overdraft (OD) account remains continuously in excess of the sanctioned limit/drawing power for 90 days, or

  b. The outstanding balance in the CC/OD account is less than the sanctioned limit/drawing power but there are no credits continuously for 90 days, or the outstanding balance in the CC/OD account is less than the sanctioned limit/drawing power but credits are not enough to cover the interest debited during the previous 90 days period.

- **Upgradation of accounts classified as NPAs:** Loan accounts classified as NPAs may be upgraded as 'standard' asset only if entire arrears of interest and principal are paid by the borrower. With regard to upgradation of accounts classified as NPA due to restructuring, non-achievement of date of commencement of commercial operations (DCCO), etc., the instructions as specified for such cases shall continue to be applicable.

- **Income recognition policy for loans with moratorium on payment of interest:** In cases of loans where moratorium has been granted for repayment of interest, lending institutions may recognise interest income on accrual basis for accounts which continue to be classified as 'standard'. It is clarified that if loans with moratorium on payment of interest (permitted at the time of sanction of the loan) become NPA after the moratorium period is over, the capitalised interest corresponding to the interest accrued during such moratorium period need not be reversed.

3. Agricultural advances governed by crop season-based asset classification norms shall be exempt from this instruction.

- **NPA classification in case of interest payments:** As per the extant instructions of master circular dated 1 October 2021, in case of interest payments, an account is classified as NPA only if the interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter. To fully align with the 90 days delinquency norm as well as the requirement to apply interest at monthly rests, the above instructions are modified as under:

  In case of interest payments in respect of term loans, an account will be classified as NPA if the interest applied at specified rests remains overdue for more than 90 days.

  These instructions are effective from 31 March 2022. Accordingly, in respect of any borrower account which becomes overdue on or after 31 March 2022, its classification as NPA shall be based on the account being overdue for more than 90 days.

- **Consumer education:** With a view to increase awareness among the borrowers, lending institutions should place consumer education literature on their websites, explaining with examples, the concepts of date of overdue, SMA and NPA classification and upgradation, with specific reference to day-end process. Lending institutions may also consider displaying such consumer education literature in their branches by means of posters and/or other appropriate media.

  Further, it shall also be ensured that their front-line officers educate borrowers about all these concepts, with respect to loans availed by them, at the time of sanction/disbursal/renewal of loans. These instructions shall be complied with at the earliest, but not later than 31 March 2022.

(Source: RBI notification no. RBI/2021-2022/125 dated 12 November 2021)

PCA framework for scheduled commercial banks

In 2002, RBI notified the Prompt Corrective Action (PCA) framework for Scheduled Commercial Banks (SCBs) which is reviewed by RBI on a continuous basis. The objective of the PCA framework is to enable supervisory intervention at appropriate time and require the supervised entity to initiate and implement remedial measures in a timely manner, so as to restore its financial health. The PCA framework does not preclude the RBI from taking any other action as it deems fit at any time, in addition to the corrective actions prescribed in the framework.

On 2 November 2021, RBI has issued certain revisions to the PCA framework which are effective from 1 January 2022. Key features of the revised framework are as follows:

- Capital, asset quality and leverage will be the key areas for monitoring in the revised framework.
- Indicators to be tracked for capital, asset quality and leverage would be CRAR/Common Equity Tier I Ratio, net NPA ratio and Tier I Leverage Ratio respectively.
- A bank will generally be placed under the PCA framework based on the audited annual financial results and the ongoing supervisory assessment made by RBI. RBI may impose PCA on any bank during the course of a year (including migration from one threshold to another) in case the circumstances so warrant.
- The PCA framework would apply to all banks operating in India including foreign banks operating through branches or subsidiaries based on breach of risk thresholds of identified indicators.
- Some of the actions that can be taken under the framework are:

  a. **Strategy related actions:** RBI to advise the bank's board to:

     i. Activate the recovery plan that has been duly approved by the supervisor

     ii. Undertake a detailed review of business model in terms of sustainability of the business model, profitability of business lines and activities, medium and long-term viability, etc.

iii. Review short term strategy focussing on addressing immediate concerns

iv. Undertake restructuring of operations as appropriate.

b. **Governance related actions:**

i. RBI to recommend to owners (government/ promoters/parent of foreign bank branch) to bring in new management/board

ii. RBI to remove managerial persons or supersede the board

iii. RBI to impose restrictions on directors or management compensation, as applicable.

c. **Capital related actions:**

i. Restriction on investment in subsidiaries/ associates

ii. Requiring the bank to bolster reserves through retained profits

iii. Restriction in expansion of high risk-weighted assets to conserve capital.

d. **Credit risk related actions:**

i. Preparation of time bound plan and commitment for reduction of stock of NPAs

ii. Strengthening of loan review mechanism

iii. Restrictions/reduction in total credit risk weight density

iv. Sale of assets.

(Source: RBI notification no. RBI/2021-22/118 dated 2 November 2021)

IASB proposed amendments to IAS 1

On 19 November 2021, the International Accounting Standards Board (IASB) has proposed narrow-scope amendments to IAS 1, *Presentation of Financial Statements* through an Exposure Draft (ED) - *Non-current Liabilities with Covenants*. The amendments are expected to improve the information companies provide about long-term debt with covenants.

Currently, IAS 1 requires a company to classify a liability as non-current only if the company has a right to defer settlement of the liability for at least 12 months after the reporting date. However, such a right is often subject to the company complying with covenants after the reporting date. For example, a company might have long-term debt that could become repayable within 12 months if the company fails to comply with covenants after the reporting date.

The proposed amendments would specify that, in such a situation, covenants would not affect the classification of a liability as current or non-current at the reporting date. Instead, a company would:

- Present non-current liabilities that are subject to covenants on the statement of financial position separately from other non-current liabilities and
- Disclose information about the covenants in the notes to its financial statements, including their nature and whether the company would have complied with them based on its circumstances at the reporting date.

Comments on the ED are invited up to 21 March 2022.

(Source: IASB announcement dated 19 November 2021)

FASB updates

ASU on Topic 842, *Leases*

On 11 November 2021, the Financial Accounting Standards Board (FASB) has issued an Accounting Standards Update (ASU) which intends to improve discount rate guidance for lessees that are not public business entities - including private companies, not-for-profit organisations, and employee benefit plans.

Currently, Topic 842 provides lessees that are not public business entities with a practical expedient that allows them to elect, as an accounting policy, to use a risk-free rate as the discount rate for all leases.

The amendments in the ASU allow those lessees to make the risk-free rate election by class of underlying asset, rather than at the entity-wide level. An entity that makes the risk-free rate election is required to disclose which asset classes it has elected to apply a risk-free rate.

The amendments require that when the rate implicit in the lease is readily determinable for any individual lease, the lessee use that rate (rather than a risk-free rate or an incremental borrowing rate), regardless of whether it has made the risk-free rate election.

Effective date: The effective date for this ASU is different for entities that have not yet adopted Topic 842 as of 11 November 2021, and those that have. Accordingly:

- *Entities that have adopted Topic 842 as of 11 November 2021:* The amendments are effective for fiscal years beginning after 15 December 2021, and interim periods within fiscal years beginning after 15 December 2022. Earlier application is permitted.
- *Entities that have not yet adopted Topic 842 as of 11 November 2021:* Such entities are required to adopt the amendments at the same time that they adopt Topic 842.

(Source: FASB's ASU no. 2021-09 on Topic 842 issued on 11 November 2021)

ASU on Topic 832, *Government Assistance*

FASB through an announcement dated 17 November 2021 has issued an ASU which is expected to increase transparency in financial reporting by requiring business entities to disclose, in notes to their financial statements, information about certain types of government assistance they receive. Examples of such government assistance include cash grants and grants of other assets.

The amendments in the ASU require following annual disclosures about transactions with a government that are accounted for by applying a grant or contribution accounting model by analogy to other accounting guidance such as a grant model within FASB's Accounting Standards Codification Topic 958, *Not-for-Profit Entities*, or International Accounting Standards (IAS) 20, *Accounting for Government Grants and Disclosure of Government Assistance:*

- Information about the nature of the transactions and the related accounting policy used to account for the transactions.
- The line items on the balance sheet and income statement that are affected by the transactions, and the amounts applicable to each financial statement line item.
- Significant terms and conditions of the transactions, including commitments and contingencies.

Effective date: The amendments in the ASU are effective for all entities within their scope, which excludes not-for-profit entities and employee benefit plans, for financial statements issued for annual periods beginning after 15 December 2021. Early application is permitted.

(Source: FASB's ASU no. 2021-10 on Topic 832 issued on 17 November 2021)

Proposed ASU on Topic 270, *Interim Reporting*

The Financial Accounting Standards Board (FASB) through an announcement dated 1 November 2021 has issued an Accounting Standards Update (ASU) which intends to modify the disclosure requirements for interim financial reporting in Topic 270, *Interim Reporting*. The proposed ASU is part of the FASB's disclosure framework project to improve the effectiveness of disclosure to the notes to financial statements.

The proposed amendments relate to the following:

- **Disclosure principle:** The amendments in this proposed ASU add a new principle, based on the removed portion of Regulation S-X, Rule 10-01. That principle requires disclosures for a significant event or transaction that has a material effect on an entity and results in disclosures that are transaction or event specific.
- **Presentation and disclosure alternatives in interim reporting:** The amendments would clarify that interim reporting can take the following three forms:

  a. Financial statements prepared with the same level of detail as the previous annual statements subject to all the presentation and disclosure requirements in GAAP

  b. Financial statements prepared with the same level of detail as the previous annual statements subject to all the presentation requirements in GAAP and limited notes subject to the disclosure requirements in Topic 270

  c. Condensed financial statements and limited notes subject to the disclosure requirements in Topic 270.

The amendments in this proposed ASU would apply to all entities that provide interim financial statements and notes in accordance with GAAP.

Comments on the proposed ASU are invited up to 31 January 2022.

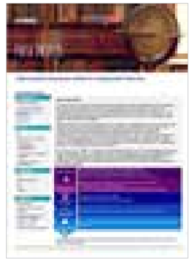
(Source: FASB's proposed ASU on Topic 270 issued on 1 November 2021)

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



SEBI mandates additional compliances for issuers of non-convertible securities

10 November 2021

With a view to improve transparency and enhance the robustness of the corporate bond market, on 7 September 2021, the Securities and Exchange Board of India (SEBI) issued amendments to the Listing Regulations through the SEBI (Listing Obligations and Disclosure Requirements) Fifth Amendment Regulations, 2021 (amendments). The amendments mainly pertain to the following areas:

- Corporate governance regulations applicable to High Value Debt Listed Entities (HVDLE) (Applicable from 8 September 2021 on 'comply or explain' basis and mandatory from 1 April 2023)
- Financial reporting (Applicable from 8 September 2021)
- Additional disclosures to stock exchanges, debenture trustees and on websites (Applicable from 8 September 2021)
- Other amendments (Applicable from 8 September 2021).
- This issue of First Notes aims to provide an overview of the key amendments introduced by SEBI (Listing Obligations and Disclosure Requirements) Fifth Amendment Regulations, 2021.

In this issue of First Notes, we aim to provide an overview of the key amendments made by SEBI in the Listing Regulations relating to IDs.

Voices on Reporting (VOR)

On 28 October 2021, KPMG in India issued VOR - Quarterly 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) relevant for stakeholders for the quarter ended 30 September 2021.

To access the publication, please click here.

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KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011 Phone: +91 22 3989 6000, Fax: +91 22 3983 6000.