KPMG

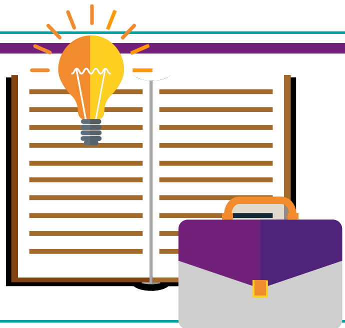
Voices on Reporting

Quarterly updates

July 2017

Contents

In this newsletter, we aim to summarise important topics relating to the quarter ending 30 June 2017 from the Ministry of Corporate Affairs (MCA), the Securities and Exchange Board of India (SEBI), the Reserve Bank of India (RBI), the Institute of Chartered Accountants of India (ICAI) and the Central Board of Direct Taxes (CBDT).



Updates relating to Ind AS

Ind AS road map for corporates – Phase II implementation

The MCA through a notification dated 16 February 2015 issued the Companies (Accounting Standards) Rules, 2015 (Ind AS Rules) which laid down a road map for entities (other than insurance entities, banking entities and Non-Banking Financial Companies (NBFCs)) (corporate road map) for implementation of Ind AS converged with IFRS in a phased manner.

Phase II

The following table provides the Ind AS corporate road map applicability thresholds for Phase II:

Type of entities	Applicability thresholds
Entities listed or in process of being listed (including holding, subsidiary, joint venture or associate of such entities)	Net worth of less than INR500 crore
Unlisted entities (including holding, subsidiary, joint venture or associate of such entities)	Net worth of INR250 crore or more but less than INR500 crore

(Source: KPMG in India's analysis, 2017)

(Note: Any entity not covered in the corporate road map (and its holding, subsidiary, joint venture or associate entity) may voluntarily adopt Ind AS.)

Important Ind AS transition dates for phase II entities are as follows:

- **Date of transition to Ind AS:** 1 April 2016
- **First Ind AS reporting period:** Accounting period beginning 1 April 2017
- **Comparative Ind AS information:** 2016-17

Phase II entities having equity listed securities: SEBI relaxations

The SEBI through its circular dated 5 July 2016, provided certain relaxations in reporting of Ind AS financial results for the first three quarters when adopting Ind AS for the first time. The disclosure requirements and relaxations relevant for listed entities covered under phase II of the corporate road map for the quarter ended 30 June 2017 have been outlined as follows:

- Timelines extended: SEBI provided relaxation to equity listed entities to submit financial results for the quarter ended 30 June 2017 upto 14 September 2017 (earlier upto 14 August 2017).
- New formats for financial results: The listed entities are required to comply with Schedule III of the Companies Act, 2013 (2013 Act) (excluding notes) for the submission of Ind AS compliant quarterly financial results.

  Further, SEBI has revised the formats of the financial results to be published in the newspapers and has prescribed that the comparatives filed along with the quarterly/annual financial results should be Ind AS compliant.
- Consolidated financial results: The equity listed entities could opt to present quarterly/Year-To-Date (YTD) consolidated financial results from the second quarter instead of the first quarter.

- Reporting relaxation: The table below highlights the quarterly disclosure requirements for listed entities

Reporting requirements	3 months ended	Preceding 3 months ended	Corresponding 3 months ended in the PY	YTD figures for current period ended	YTD figures for the PY	PY ended 31 March 2017	Audit/review of PY comparative period	Audit/review of period ended 31 March 2017	Disclosure of reserves (excluding revaluation reserves) as at 31 March 2017
30 June 2017	√	x (Note a and b)	√	N. A.	N. A.	x (Note a)	x (Note b)	x (Note b)	Optional

(Source: KPMG in India's analysis, 2017 based on SEBI circular dated 5 July 2016)

Notes:

a. Entities may voluntarily provide Ind AS compliant financial results for the preceding quarter and previous year ended 31 March 2017.

b. Ind AS financial results for the periods are not required to be audited or reviewed. Entities should disclose the fact that the financial results have not been audited/reviewed. Additionally, the management should disclose that it has exercised necessary due diligence to ensure that the financial results provide a true and fair view of its affairs.

c. Reconciliation of the net profit/loss as mentioned in the unaudited/audited quarterly financial results should be provided for the corresponding quarter of the previous year.

Key takeaways

- The entities transitioning to Ind AS under phase II of the corporate road map should seek learning from the implementation efforts done by the entities transitioned under phase I of the road map. Also the entities should consider all the clarifications issued by regulators such as MCA, SEBI, ICAI, etc. and interpretations issued by ITFG of ICAI while transitioning to Ind AS.
- The SEBI circular provides significant relief to listed entities that are implementing Ind AS for filing of the quarterly financial results. However, the entities should consider and evaluate the requirements of the revised formats.

(Source: MCA notification dated 16 February 2015 and SEBI circular no. CIR/CFD/FAC/62/2016 dated 5 July 2016 and KPMG in India's IFRS Notes dated 13 July 2016.)

Road map for banks

The RBI on 11 February 2016 issued a circular RBI/2015-16/315 requiring scheduled commercial banks to comply with Ind AS for accounting periods beginning from 1 April 2018 onwards. This circular reiterates the timeline for Ind AS implementation by banks that was issued by MCA in its press release dated 18 January 2016. Ind AS would be applicable to both standalone financial statements and Consolidated Financial Statements (CFS). As per this, Ind AS has become applicable to the following class of banks from financial year 2018-19:

a. Scheduled Commercial Banks (excluding Regional Rural Banks)

b. All-India Term Lending Refinancing Institutions

c. Holding, subsidiary, joint venture or associate companies of banks to follow this road map (even if covered under road map applicable for other companies).

Important Ind AS transition dates for banks are as follows:

Date of transition to Ind AS: 1 April 2017

First Ind AS reporting period: Accounting period beginning 1 April 2018

Comparative Ind AS information: 2017-18

Road map for NBFCs – Phase I companies

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

a. NBFCs having net worth of INR500 crore or more, and

b. Their holding, subsidiary, joint venture or associate companies, other than those companies already covered under the corporate road map issued by MCA in February 2015.

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

Date of transition to Ind AS: 1 April 2017

First Ind AS reporting period: Accounting period beginning 1 April 2018

Comparative Ind AS information: 2017-18

Voluntary adoption of Ind AS: Banks and NBFCs would apply Ind AS when preparing their financial statements only if they meet the specified criteria and are not permitted to voluntarily adopt Ind AS. However, financial information based on Ind AS can be provided for preparation of CFS by the parent company/an investor as required by law.

Key takeaway

- The banks and NBFCs transitioning to Ind AS from 1 April 2017 would have an organisation-wide impact due to the pervasive nature of the new standards. Therefore, companies covered under this road map should commence identifying the necessary changes required to their financial reporting and regulatory policies, processes and systems to prepare for this change.

(Source: MCA notification dated 16 February 2015, MCA Press Release dated 18 January 2016 and MCA issued Companies (Indian Accounting Standards) (Amendment) Rules, 2016 dated 30 March 2016)

Road map for insurance companies

Background

As per the MCA notification dated 30 March 2016, insurance companies were required to implement Ind AS from 1 April 2018 onwards. The Insurance Regulatory and Development Authority (IRDA) also constituted an Implementation Group (IG) on 17 November 2015 to facilitate Ind AS convergence for the Indian insurance sector. Additionally, insurance companies were directed to submit pro forma Ind AS financial statements from the quarter ended 31 December 2016 in the specified formats (IRDAI circular no. IRDA/F&A/CIR/ACTS/262/12/2016 dated 30 December 2016).

On 18 May 2017, the International Accounting Standards Board (IASB) issued the much awaited comprehensive international standard on insurance i.e. IFRS 17, *Insurance Contracts*. IFRS 17 replaces IFRS 4, *Insurance Contracts* which was in the nature of an interim standard pending the completion of the project on insurance contracts by the IASB.

The release of IFRS 17 standard led to IRDAI to review its position in the matter of implementation of Ind AS in the insurance sector.

New development

The IRDAI through its circular no. IRDA/F&A/CIR/ACTS/146/ 06/2017 dated 28 June 2017 deferred the implementation of Ind AS in the insurance sector in India for a period of two years. Accordingly, Ind AS for Indian insurance companies would be applicable from 1 April 2020 (instead of 1 April 2018).

However, insurance companies would still be required to submit the pro forma Ind AS financial statements to IRDAI on a quarterly basis (effective from 31 December 2016). Therefore, the requirement to submit pro forma Ind AS financial statements on a quarterly basis has not been deferred.

Important Ind AS transition dates for insurance companies are as follows:

Date of transition to Ind AS: 1 April 2019

First Ind AS reporting period: Accounting period beginning 1 April 2020

Comparative Ind AS information: 2019-20

Key takeaways

- Though the deferment of applicability of Ind AS is expected to provide some relief to the insurers in India, they should utilise this time to identity and address the key challenges involved in the implementation of Ind AS and IFRS 17.
- For insurance companies that are subsidiaries or associates of banking or other companies, the requirement to report on an Ind AS basis for consolidation purposes will continue despite the announcement by IRDAI. Additionally, they are still required to submit pro forma Ind AS financial statements to IRDAI.

(Source: IRDAI circular no. IRDA/F&A/CIR/ACTS/146/ 06/2017 dated 28 June 2017 and KPMG in India's IFRS Notes dated 29 June 2017)

ITFG clarifications bulletin 8 and 9

The Ind AS Transition Facilitation Group (ITFG) formed by the ICAI issues clarification bulletin to provide clarifications on issues arising due to applicability and/or implementation of Ind AS.

Over the last quarter ITFG issued two clarification bulletins – bulletin 8 and 9 to provide guidance on the issues relating to the application of Ind AS.

Overview of the bulletin 8

a. Property, Plant and Equipment (PPE): The ITFG has provided following guidance on issues relating to PPE in the bulletin 8:

- **Capitalisation of an item of PPE not falling under the definition of an asset:** A first-time adopter that has elected to continue with carrying value as per the previous GAAP as the deemed cost for its PPE may have capitalised an item under previous GAAP even though it did not meet the definition of an asset.

  In this context, ITFG clarified that the deemed cost exemption (carrying value as per previous GAAP) is only available for PPE items and it cannot be availed for those items that do not meet the definition of asset as per previous GAAP and the definition of PPE as per Ind AS 16, *Property, Plant and Equipment.*

  Additionally the capitalisation of an asset which does not meet the definition of tangible asset, will be considered as an error made under AS (previous GAAP) and as per principles given under Ind AS 101, *First-time Adoption of Indian Accounting Standards* (paragraph 26 of Ind AS 101) an entity should make a separate disclosure of such an error under the reconciliation required from previous GAAP to Ind AS. Such disclosure should distinguish the correction of those errors from changes in accounting policies.

- **Reversal of impairment:** The ITFG considered a case where an entity elects to measure its PPE at its previous GAAP revaluation amount measured before the date of transition. An issue was raised whether the past provision of impairment can be reversed when an entity elects to measure its PPE at its previous GAAP revaluation amount measured before the date of transition.

  The ITFG clarified that as per the principles of Ind AS 101, the amount so elected as deemed cost is the cost under Ind AS and any (past) accumulated depreciation and provision for impairment under previous GAAP would have no relevance under Ind AS. Accordingly, provision for impairment provided before the date of deemed cost measurement (i.e. previous GAAP revaluation amount) cannot be reversed in later years.

In case the deemed cost determination date is different from the date of transition, the entity should apply appropriate Ind AS accounting policies and depreciation policies to that asset from the deemed cost determination date to the date of transition. The depreciation policy applied during the intervening period from the deemed cost determination date to the date of transition would have to be in accordance with the requirements of applicable Ind AS. Accordingly, the impairment loss for the period between the deemed cost determination date to the date of transition can be reversed, if permitted as per the principles of Ind AS 36, *Impairment of Assets.*

However, if the entity does not opt for the deemed cost exemption given under Ind AS 101 but elects to apply Ind AS 16 retrospectively, then impairment loss can be reversed, if permitted as per the principles of Ind AS 36.

- **Treatment of revaluation reserve when revalued amount of PPE is considered as deemed cost:** The ITFG considered a situation wherein an entity had in the past revalued its PPE and opts to continue with the revalued carrying value of its PPE as at the date of transition to Ind AS and elected to apply the cost model (i.e. to carry the PPE at cost less accumulated depreciation and impairment losses) for the subsequent measurement of the PPE.

  The ITFG clarified that in such a case, since the entity had deemed the revalued amount of PPE as its cost on the date of transition to Ind AS, it would not be permitted to carry a revaluation reserve under Ind AS. Therefore, the balance outstanding in the revaluation reserve would be transferred to retained earnings or if appropriate, another category of equity. Accordingly, the entity would be required to disclose the details of this adjustment in the financial statements and provide a description of the nature and purpose of such an amount. Additionally, since the PPE had been revalued, there was a difference between its carrying value in the financial statements and the tax base, hence a deferred tax would be recognised on the PPE to the extent of this difference.

  The ITFG also pointed out that the requirements of the 2013 Act for declaration of dividend should be evaluated separately.

b. **Accounting for accumulated losses of subsidiaries:** Ind AS 110, *Consolidated Financial Statements,* requires entities to attribute the total comprehensive income of their subsidiaries to the owners of the parent and to the Non-Controlling Interest (NCI), even if this results in the NCI having a deficit balance.

   The ITFG considered a situation where a first-time adopter has multiple subsidiaries with a negative net worth as on 31 March 2015. The issue under consideration was on how to deal with the accumulated losses of the subsidiaries where:

   - **Past business combinations not restated:** In this case, the entity will be required to attribute the total profit or loss and each component of other comprehensive income to the owners of the parent and to the NCI prospectively from the date of transition.
   - **Past business combinations restated:** In this case, the entity should attribute the accumulated losses of the subsidiaries, to the owners of the parent and to the NCI from the date of application of Ind AS 103, *Business Combinations* in its CFS, on the date of transition.

c. **Recognition of deferred taxes on capitalised exchange differences:** The ITFG considered a situation where a company had availed the option to continue with the accounting policy as para 46A of AS 11, *The Effects of Changes in Foreign Exchange Rates* for exchange differences i.e. to capitalise foreign exchange gains or losses for those long-term foreign currency loans that were taken for the construction of PPE before the beginning of the first Ind AS reporting period i.e. 1 April 2016 in the case of a company falling in phase I of the Ind AS adoption road map. However, such exchange differences may not be allowed to be capitalised as part of the cost of an asset as per the Income-tax Act, 1961 (IT Act).

   The issue under consideration was whether the company should recognise deferred taxes on differences arising from the adjustment of exchange differences to the cost of the asset.

   Also whether the company would be able to avail the benefit under paragraph 15(b) of Ind AS 12, *Income Taxes,* which stated that no deferred tax liability would be recognised on the initial recognition of an asset or a liability in a transaction, which was not a business combination and at the time of the transaction, neither affected the accounting profit nor the taxable profit.

   The ITFG clarified that capitalisation of exchange differences represents subsequent measurement of the foreign currency loan liability which has been adjusted to the cost of the asset i.e. it does not arise on initial recognition of an asset or liability. Hence, the initial recognition exemption under Ind AS 12 will not be available and deferred tax is required to be recognised on temporary difference arising from such capitalised exchange differences.

d. **Recognition of dividend income on an investment in debt instrument:** The ITFG clarified that dividend income on an investment in debt instrument would be recognised in the form of 'interest income' by an investor. However, the manner in which the income would be computed and recognised would depend on whether the debt instrument is classified as subsequently measured at amortised cost, Fair Value Through Other Comprehensive Income (FVOCI) or Fair Value Through Profit or Loss (FVTPL).

   Interest income where debt instrument is subsequently measured at amortised cost: Where the debt instrument is measured at amortised cost, the interest revenue would be calculated using the Effective Interest Rate (EIR) method. The interest would be computed as below:

   - Where the debt instrument is not credit impaired, the interest income should be computed by applying the EIR to its gross carrying amount
   - Where the debt instrument is a purchased or originated credit-impaired financial asset, the entity should apply the credit adjusted EIR to the amortised cost of the financial asset from initial recognition to compute the interest income
   - Where the debt instrument is not a purchased or originated credit impaired financial asset, but subsequently has become credit-impaired, the entity should apply the EIR to the amortised cost of the financial asset in subsequent reporting periods. Where the credit risk on the financial instrument improves so that the financial asset is no longer credit-impaired, the interest revenue is computed by applying the EIR to the gross carrying amount of the debt instrument. The improvement should be related objectively to an event occurring after the requirements in Ind AS 109, *Financial Instruments* (para 5.4.1(b)) have been applied.

   Interest income where debt instrument is classified and measured at FVOCI: Where a debt instrument is classified and measured at FVOCI, the interest revenue thereon is recognised in the statement of profit and loss in accordance with the EIR method, as explained above.

   Interest income where debt instrument is classified and measured at FVTPL: Where a debt instrument is classified and measured at FVTPL, the interest income thereon is recognised in the statement of profit and loss as under:

   - The interest income may form part of the fair value gains or losses arising from changes in fair value of the instrument, or
   - The interest income is presented separately.

   The entity is required to adopt its accounting policy for recognition of the interest income, considering whether any statute or regulatory authority governing the entity prescribes the manner of presentation.

Overview of the ITFG bulletin 9

a. **Treatment of dividend and Dividend Distribution Tax (DDT) in CFS**

   The ITFG considered a situation where a company, which is a wholly owned subsidiary (S Ltd.) of an Indian company (P Ltd.) paid dividend to its parent and a DDT thereon to the tax authorities. In the financial statements, following accounting treatment would take place:

   - *In the CFS of parent* - DDT incurred by subsidiary (S Ltd.) towards dividend paid to parent (P Ltd.)

     Principle laid in Ind AS

     The ITFG clarified that the dividend paid by subsidiary, which was recorded as an income by parent in its stand-alone financial statements and which was recorded by subsidiary in its equity in its stand-alone financial statements, will be eliminated in the CFS as a result of consolidation adjustments. Further, the DDT paid outside the consolidated group to the tax authorities will be charged as an expense in the consolidated statement of profit and loss in case the parent is unable to claim an offset of such DDT against its own DDT liability, otherwise such DDT will be reflected in the consolidated statement of changes in equity of the parent.

     Deferred tax on undistributed reserves

     In case where a parent is likely to claim the DDT paid by a subsidiary as an offset against its own DDT liability, the ability to claim offset is subject to approval from the shareholders of the parent (at the annual general meeting). While ITFG clarified that, P Ltd. would recognise deferred tax liability in the CFS (measured based on the DDT expense of subsidiary) to the extent of proposed dividend of subsidiary, recognition of deferred tax asset to the extent of offset may not be recognised pending receipt of approval from shareholders of the parent.

- *In the stand-alone financial statements of parent and its subsidiary* – The treatment of DDT in the stand-alone financial statements of the parent entity and its subsidiary has been dealt in the FAQ issued by the Accounting Standards Board of ICAI dated 3 November 2016.

b. **Accounting for business combinations of entities under common control:** The issue under consideration was whether the carrying amount of assets and liabilities of the combining entities should be reflected as per the stand-alone financial statements of the entities transferred or as appearing in the financial statements of the ultimate parent. The ITFG explained the same with the help of the following situations:
   - Situation 1: Where a company has two subsidiaries and both the subsidiaries merges with each other, in such case, the carrying values of the assets and liabilities of the entities being combined in the resulting company's separate financial statements would be carrying values as appearing in their stand-alone financial statements.
   - Situation 2: When a subsidiary merges with its parent, the carrying values of the assets, liabilities and reserves pertaining to subsidiary as appearing in the CFS of parent should be recognised. Further, separate financial statements to the extent of this common control transaction should be considered as a continuation of the consolidated group.

   The legal merger of a subsidiary with its parent or legal merger of fellow subsidiaries is an intra-group transaction. As per Ind AS 110, *Consolidated Financial Statements,* all intra-group transactions should be eliminated in preparing CFS. Hence, in both the given situations, the effect of legal merger is required to be eliminated while preparing the CFS of A Ltd.

3. **Treatment of government grant in the case of a government company:** ITFG clarified the following accounting treatment for grants received under Ind AS 20, *Accounting for Government Grants and Disclosure of Government Assistance* by a government company
   - Where the entity concludes that the contribution is in the nature of a government grant, it would apply the principles of Ind AS 20 retrospectively, as required by Ind AS 101. The amount of grant would be recognised as income on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate.
   - Where the entity concludes that the contribution is in the nature of 'shareholder contributions', Ind AS 20 would not apply, since it specifically scopes out the participation by the government in the ownership of an entity. Thus, in accordance with Ind AS 101, the entity is required to reclassify the contribution received, from capital reserve to an appropriate category under 'other equity' at the date of transition to Ind AS.

Key takeaway

- The ITFG clarifications are expected to resolve various practical implementation issues faced by several companies transitioning to Ind AS. The companies should consider the interpretations provided by ITFG in their implementation efforts.

(Source: ICAI – ITFG Bulletin 8 and 9 dated 8 May 2017 and 16 May 2017 and KPMG in India's IFRS Notes dated 16 May and 29 May 2017)

ICAI issued an Exposure Draft (ED) on limited amendment to Ind AS 101

Background

Entities adopting Ind AS for the first time are required to apply Ind AS 101. Ind AS 101 sets out the procedures that an entity would follow when it adopts Ind AS for the first time as the basis for preparing its financial statements. Ind AS 101 allows entities to measure the PPE, at the date of transition to Ind AS at 'deemed cost'. Under this exemption, an entity may measure its PPE at the date of transition by electing to apply any one of the following approaches to compute the 'deemed cost':

- Fair value of PPE at the date of transition
- Previous GAAP revalued amount of PPE (if certain conditions are met)
- Carrying value of PPE as per previous GAAP at the date of transition
- Event-driven valuation.

(The above options can also be availed for intangible assets covered by Ind AS 38, *Intangible Assets* and investment property, covered by Ind AS 40, *Investment Property,* if certain conditions are met.)

The 'carrying value of PPE as per previous GAAP' as deemed cost is a carve-in in Ind AS. IFRS does not specify this approach.

New development

The ICAI on 27 April 2017 issued an ED for limited amendment to Ind AS 101 with regard to 'carrying value of PPE as per previous GAAP' as the deemed cost approach. The proposed amendment would result in the following:

- **Cherry picking by class:** Allow entities to apply the 'carrying value of PPE as per previous GAAP' as the deemed cost for a class of assets instead of all its PPE. For example, an entity may choose to apply 'carrying value of PPE as per previous GAAP' as the deemed cost approach to plant and machinery and apply fair value as deemed cost approach for land and building.
- **Related adjustments:** Earlier, if an entity had availed the 'carrying value of PPE as per previous GAAP' as the deemed cost for PPE, it was not allowed to make any other transition related adjustment to the PPE carrying value. Now, the amendment has revered this stand and allows an entity to make adjustments to the deemed cost which may arise due to application of other Ind AS.

The ED specifies that an entity would apply the amendments relating to 'carrying value as per previous GAAP as deemed cost' for annual periods beginning on or after 1 April 2017.

Key takeaway

- Since the effective date of the limited amendment to Ind AS 101 is expected to be from 1 April 2017, it would apply to entities covered in phase II of the Ind AS corporate road map. This could however, pose a question whether companies who are covered in phase I of the Ind AS corporate road map could avail the benefit of this amendment.

(Source: ED of amendments to Ind AS 101 issued by ICAI dated 27 April 2017 and KPMG in India's First Notes dated 9 May 2017)

Updates relating to the Companies Act, 2013

MCA issued further relaxations from certain provisions of the 2013 Act

Background

The MCA through its notifications dated 5 June 2015, provided certain exceptions/modifications/adaptations from some of the provisions of the 2013 Act for the following class of companies:

- Private companies
- Companies formed with the charitable objects, etc. (Section 8 companies)
- Government companies.

New development

The MCA through its notifications dated 13 June 2017 and 22 June 2017, provided further exceptions/modifications/adaptations to the provisions of the 2013 Act for the above mentioned class of companies (i.e. private companies, Section 8 companies and government companies).

These exceptions/modifications/adaptations would be available to the companies which have not defaulted in filing of its financial statements under Section 137 or annual returns under Section 92 of the 2013 Act with the Registrar of Companies (ROC).

Overview of the exceptions/modifications/adaptations to the 2013 Act

Private companies

The table below provides an overview of the exceptions/modifications/adaptations made to the 2013 Act for private companies:

Sections/sub-sections that are amended for private companies which are start-up companies

Sections	Particulars
Section 2(40)	Definition of financial statements: As per the amendment, apart from the financial statements of a one person company, small company, dormant company, **a private company which is a start-up company[1]** is not required to include a cash flow statement. *(Emphasis added to highlight the change)*
Section 92(1)(g) and proviso to Section 92(1)	Annual return: Private companies which are small companies[2] are required to provide details of **aggregate amount of remuneration drawn by directors** instead of providing details of remuneration of directors and key managerial personnel of the company. Additionally, apart from the one person company and small company, the annual return is required to be signed by the company secretary, or where there is no company secretary, by the director of the company of **private company which is a start-up.** *(Emphasis added to highlight the changes)*
Section 173(5)	Meetings of board: As per the amendment, apart from the one person company, small company, dormant company, a **private company which is a start-up** would also be deemed to have complied with the provision of Section 173, if at least one board meeting has been conducted in each of a calendar year and the gap between two meetings is not less than 90 days. *(Emphasis added to highlight the change)*

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1. Start-up or start-up company means a private company incorporated under the 2013 Act or the Companies Act, 1956 and recognised as start-up in accordance with the notification issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry
2. Small company means a company, other than a public company which meets both the given conditions:
   a. Paid-up share capital does not exceed INR50lakh or such higher amount as may be prescribed which should not be more than INR5 crore and
   b. Turnover as per last statement of profit and loss does not exceed INR2 crore or such higher amount as may be prescribed which should not be more than INR20 crore.

   However, these conditions would not be applicable to the following class of companies:
   a. A holding company or a subsidiary company
   b. A company registered under Section 8 of the 2013 Act or
   c. A company or body corporate governed by any special Act.

Sections/sub-sections that are amended for all private companies

Sections	Particulars
Section 139(2) read with Rule 5 of the Companies (Audit and Auditors) Rules, 2014	Mandatory rotation of auditors: As per the recent notification, all private limited companies having paid-share capital of **INR50 crore** or more cannot appoint or reappoint an audit firm as auditor for more than two consecutive terms of five years each and in case of an individual for more than one term of five years. *(Emphasis added to highlight the change)*
Section 174(3)	Quorum for meetings of board: In case of private companies, the **interested director could also be counted towards quorum** for board of directors' meeting, of a company, after disclosure of his/her interest in accordance with Section 184 of the 2013 Act. *(Emphasis added to highlight the change)*

Sections/sub-sections that would not apply to certain class of private companies

Sections	Particulars
Section 73(2)(a) to Section 73(2)(e)	Acceptance of deposits from public: A certain class of private companies can now accept deposits from their members if **any** of the below given criteria is met: a. It accepts monies from its members not exceeding 100 per cent of aggregate of the paid-up share capital, free reserves and securities premium **b. It is a start-up company for five years from the date of its incorporation, or** **c. It fulfils all the following conditions:** **i. The private company is not an associate or a subsidiary company of any other company** **ii. The borrowings of such a company from banks or financial institutions or any body corporate is less than twice of its paid-up share capital or INR50 crore, whichever is lower and** **iii. Such a company has not defaulted in the repayment of such borrowings subsisting at the time of accepting deposits under Section 73.** Additionally, the private company would be required to file the details of monies accepted to the ROC in such a manner as may be specified. The conditions mentioned in clauses (a) to (e) of Section 73(2) of the 2013 Act would not be applicable to a private company. *(Emphasis added to highlight the changes)*
Section 143(3)(i)	Internal Financial Controls (IFC): An auditor of a private company is not required to report on the adequacy and operating effectiveness of IFC in the auditor's report provided such a private company meets either of the given conditions: a. It is a one person company or a small company, or b. It has a turnover of less than INR50 crore as per the latest audited financial statements or the borrowings of such a company from banks or financial institutions or any body corporate at any point of time during the FY is less than INR25 crore.

(Source: KPMG in India's analysis, 2017 based on the provisions of the 2013 Act and MCA notifications dated 5 June 2015, 13 June 2017 and 22 June 2017)

Section 8 companies

The table below provides an overview of the exceptions/modifications/adaptations made to the 2013 Act for companies covered under Section 8 of the 2013 Act:

Sections	Particulars
Section 186(7)	Loan and investment by company: As per the amendment, the company which meets all the given requirements is allowed to give loans at a rate of interest lower than the prevailing yield of government security: a. A company in which 26 per cent or more of the paid-up share capital is held by the central government or one or more state governments or both and b. Loans have been provided by such company for funding industrial research and development projects in furtherance of its objects as stated in its memorandum of association.
Section 149(1)(b)	Minimum and maximum number of directors: As per the amendment, provisions relating to maximum limit of directors (15) and increase in the limit by special resolution would not be applicable to Section 8 companies. This implies that the Section 8 companies would be required to have following minimum number of directors: • A public company - Three directors • A private company - Two directors • A one person company - One director.

(Source: KPMG in India's analysis, 2017 based on the provisions of the 2013 Act and MCA notifications dated 5 June 2015 and 13 June 2017)

Government companies

The table below provides an overview of the exceptions/modifications/adaptations made to the 2013 Act for the government companies:

Sections	Particulars
Section 96(2)	Annual General Meeting (AGM): The recent notification further amends the Section and provides that in case of government companies, the AGM should be held at the registered office of the company, or **such other place within the city, town or village in which the registered office of the company is situated or such other place as the central government may approve in this behalf.** *(Emphasis added to highlight the changes)*
Sections 230 to 232	Provisions relating to compromise, arrangements, merger or amalgamation: The amendment allows that in case of government companies, provisions of Section 230 to 232 of the 2013 Act should be governed by central government instead of Tribunal (i.e. the word Tribunal should be replaced with central government in Section 230, 231 and 232).
Section 152(6) and 152(7)	Retirement of directors and manner of filling vacancy in place of retiring directors: The recent notification made an amendment to the exemption provided earlier and states that the provisions of Section 152(6) and 152(7) would not be applicable to the following class of government companies: a. Government company, **which is not a listed company, in which not less than 51 per cent of paid-up share capital** is held by the central government, or by any state government or governments or by the central government and one or more state governments b. Subsidiary of a government company, referred to in (a) above. (Emphasis added to highlight the change)

(Source: KPMG in India's analysis, 2017 based on the provisions of the 2013 Act and MCA notifications dated 5 June 2015 and 13 June 2017)

Applicability: The notifications providing exemptions/modifications/adaptations to the provisions of the 2013 Act relating to private companies (other than amendment in Audit Rules*), Section 8 companies and the government companies have been published in the official gazette on 13 June 2017.

(*The notification on amendment in Audit Rules for private companies came into force from the date of its publication in the official gazette i.e. 22 June 2017.)

Key takeaways

- The recent MCA notifications provide additional relaxations for private companies, companies covered under Section 8 of the 2013 Act and government companies. In case of private companies, most of the relaxations are towards start-ups.
- The notifications making amendments to the provisions of the 2013 Act for private companies (other than amendment in Audit Rules), Section 8 companies and government companies have been published in the official gazette i.e. 13 June 2017 and amendment in Audit Rules on 22 June 2017. However, a clarification from MCA would be required to provide clarity on whether these notifications are applicable to the financial statements for the period ended 31 March 2017.

Please refer KPMG in India' First Notes dated 23 June 2017 which provides detailed analysis of the recent notification issued by MCA.

(Source: MCA notification G.S.R. 583(E), G.S.R. 584(E) and G.S.R. 582(E) dated 13 June 2017 and MCA notification dated 22 June 2017)

MCA notified provisions relating to merger or amalgamation of a foreign company

On 13 April 2017, MCA issued the following notifications:

- Notification of Section 234 of the 2013 Act (merger or amalgamation of a company with a foreign company)
- Insertion of new sub-rule 25A (merger or amalgamation of a foreign company with a company and vice-versa) in the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 (Compromises Rules).

The salient features of the notified provisions are as follows:

- **Section 234 of the 2013 Act: Merger or amalgamation of a company with a foreign company**
  - *Prior approval of the RBI:* A foreign company* (incorporated in the jurisdictions of such countries as may be notified) may merge into a company registered under the 2013 Act or vice-versa after obtaining prior approval of the RBI.
  - *Payment of consideration:* The terms and conditions of the scheme of merger may provide, among other things, for the payment of consideration to the shareholders of the merging company in cash, or in depository receipts, or partly in cash and partly in depository receipts, as the case may be, as per the scheme to be drawn up for the purpose.
  - *Applicability:* The provisions of Section 234 are effective from 13 April 2017.
- **Rule 25A of the Compromises Rules: Merger or amalgamation of a foreign company with a company and vice-versa**
  - *Prior approval of RBI and compliance with other sections of the 2013 Act:* A company may merge with a foreign company (incorporated in any of the jurisdictions as specified in the table below) after obtaining prior approval of the RBI and after complying with the provisions of the following sections of the 2013 Act and related Rules:

    a. Section 230: Power to compromise or make arrangements with creditors and members

    b. Section 231: Power of National Company Law Tribunal (NCLT) to enforce compromise or arrangement

    c. Section 232: Merger and amalgamation of companies.

(*'Foreign company' means any company or body corporate incorporated outside India whether having a place of business in India or not.)

- *Specified jurisdictions of a foreign company:* A company can merge with a foreign company which is incorporated in the following jurisdictions:

Sr. no.	Jurisdictions
1.	Securities market is a signatory to International Organisation of Securities Commission's Multilateral Memorandum of Understanding (Appendix A Signatories) or a signatory to bilateral Memorandum of Understanding with SEBI
2.	Central bank is a member of Bank for International Settlement (BIS) and
3.	Jurisdiction which is not identified in the public statement of Financial Action Task Force (FATF) as: a. A jurisdiction having a strategic anti-money laundering or combating the financing of terrorism deficiencies to which counter measures apply or b. A jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the FATF to address the deficiencies.

- *Valuation conducted by valuers as per international standards:* The transferee company would need to ensure that valuation is conducted by valuers who are members of a recognised professional body in the jurisdiction of the transferee company and further that such valuation is in accordance with internationally accepted principles on accounting and valuation. A declaration to this effect would be required to be attached with the application made to RBI for obtaining its approval.
- *Application to NCLT:* After obtaining the approval of the RBI and complying with the provisions of the above mentioned sections and the related Rules, the concerned company may file an application with the NCLT for approval of the merger.
- *Applicability:* The provisions of the Rule 25A are effective from 13 April 2017.

Key takeaways

- The notification of Section 234 and the related Rules is expected to pave way for Indian companies intending to merge with foreign companies (domiciled in the jurisdictions given above).
- The requirement of approval by the RBI is expected to ensure regulatory supervision over the proposed merger including safeguarding of interest of the concerned stakeholders.
- The companies would need to carefully evaluate the regulations of the jurisdiction of the foreign company with which a merger is intended and may have to comply with additional requirements that may be specified by the foreign jurisdictions.
- Companies should also consider and evaluate the tax impact as per the IT Act on merger with a foreign company.

(Source: MCA notifications dated 13 April 2017 and KPMG in India's First Notes dated 24 April 2017)

Companies (Acceptance of Deposits) Amendment Rules, 2017

The Companies (Acceptance of Deposits) Rules, 2014 provides that every company which is eligible to accept deposits is required to enter into deposit insurance contract with the insurance agency before 30 days of issue of circular advertisement. Further, the rules provide that in case the company defaults in repayment of deposit then the deposit should be repaid by insurance agency in the following manner:

- *In case the amount of deposit due for repayment along with interest is upto INR20,000* - the insurance agency should repay the amount in full.
- *In case the amount of deposit due for repayment along with interest is more than INR20,000* - the insurance agency should repay the amount to an extant of INR20,000 and the rest would be due to be paid by the company.

In the last year, to provide transitional period for complying with the deposit insurance requirements, MCA had provided an additional period up till 31 March 2017 to comply acceptance of deposits without deposit insurance contracts or till the availability of a deposit insurance product, whichever is earlier.

On 11 May 2017, MCA further amended the Companies (Acceptance of Deposits) Rules, 2014 which, inter alia, has increased the timeline for acceptance of deposits without deposit insurance contracts till 31 March 2018, or till the availability of a deposit insurance product, whichever is earlier.

(Source: Companies (Acceptance of Deposits) Amendment Rules, 2017 dated 11 May 2017)

Clarification regarding due date for transfer of shares to Investor Education and Protection Fund (IEPF) Authority

Background

Section 124 of the 2013 Act requires every company to transfer the amount of dividend which remains unclaimed and unpaid (upto 30 days from the date of the declaration) to the unpaid dividend account opened by the company with any scheduled bank. The amount should be transferred within seven days from the date of expiry of the said period of 30 days.

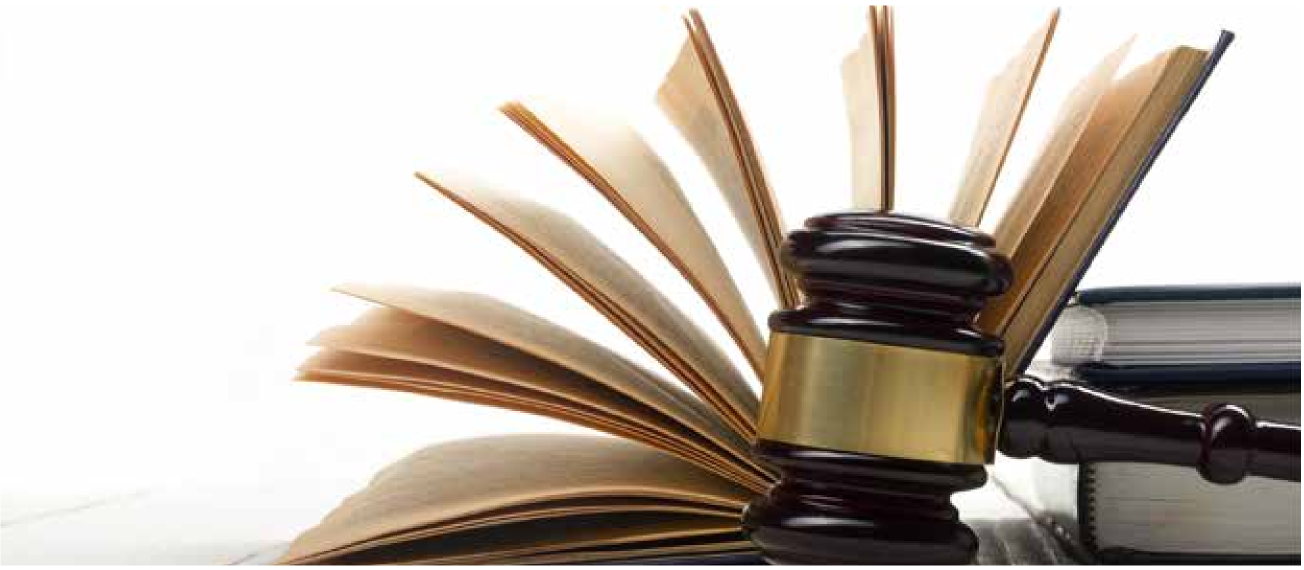
Further, the section provides that in case any amount transferred to the unpaid dividend account which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued to IEPF.

The MCA through its notification dated 28 February 2017, has amended the IEPF Authority (Accounting, Audit, Transfer and Refund) Rules, 2016. The amended rules provide that where the period of seven years for transfer of unclaimed dividend to the IEPF is due during 7 September 2016 to 31 May 2017, the due date of such transfer would be deemed to be 31 May 2017.

New development

With reference to transfer of unpaid or unclaimed dividend amount to IEPF, the IEPF Authority is considering to open special DEMAT accounts for this purpose. In view of this and till the opening of DEMAT accounts, MCA through its notification dated 29 May 2017 extended the due date for transfer of shares to IEPF. The MCA has not yet announced the revised due date.

(Source: MCA circular 06/2017 dated 29 May 2017)



Updates relating to SEBI regulations

SEBI issued norms for listing of non-convertible redeemable preference shares and non-convertible debentures issued in a scheme of arrangement

Background

The SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations) provide the procedure (through a circular dated 30 November 2015) to be followed by listed entities for undertaking schemes of arrangements such as amalgamations, mergers, reconstruction, etc.

During the year ended 31 March 2017, various developments took place with respect to such schemes of arrangements. The key developments were related to:

- **Notification of sections of the 2013 Act** relating to compromises, arrangements, amalgamations, reduction of capital and variations of shareholders' rights.
- **Revised regulatory framework by** introducing an in-principle approval for the revised regulatory framework for the schemes of arrangements.
- **Revision in the Listing Regulations by introducing** detailed requirements to be complied by the listed entities while undertaking schemes of arrangement for listing of equity or warrants pursuant to the scheme.

The circular did not provide guidance for listing of the Non-Convertible Redeemable Preference Shares (NCRPS) or Non-Convertible Debentures (NCDs) which could also be issued, in lieu of specified securities in a scheme of arrangement.

New development

On 26 May 2017, SEBI issued a circular (SEBI circular on listing of NCRPS/NCDs) which lays down the additional conditions to be complied when NCRPS/NCDs are issued in lieu of the specified securities and such NCRPS/NCDs are proposed to be listed on the recognised stock exchanges.

These additional conditions have been classified under the following heads:

I. Conditions to be complied before the scheme of arrangement is submitted for sanction by the NCLT

Eligibility for seeking listing of NCRPS/NCDs: A listed entity which has listed its specified securities could seek listing of NCRPS/NCDs issued pursuant to a scheme of arrangement only if it meets both the given criterion:

a. The listed entity is a part of such scheme of arrangement, and

b. The NCRPS/NCDs are issued to the holders of specified securities of such a listed entity.

These conditions could be met in the following events:

- In case of demerger: A listed entity, which has listed its specified securities (demerged entity) demerges a unit and transfers the same to another entity (resultant entity) and such a resultant entity issues NCRPS/NCDs to the holders of the specified securities of the listed entity (i.e. demerged entity) as a consideration under the scheme of arrangement.
- In case of amalgamation: A listed entity, which has listed its specified securities, (amalgamating entity) has been merged with another entity (amalgamated entity), and the amalgamated entity issues NCRPS/NCDs to the holders of the specified securities of listed entity (i.e. amalgamating entity) as a consideration under the scheme of arrangement.

Further, it has been clarified that if the same series/class of NCRPS/NCDs are also allotted to other investors (other than the allotment done to the holders of the listed specified securities) as per the scheme of arrangement, then such NCRPS/NCDs would not be eligible for seeking listing.

Additionally the circular provides following compliances for the scheme to comply with:

- **Tenure of NCRPS/NCDs:** The minimum tenure of NCRPS/NCDs should be one year.
- **Credit rating:** The NCRPS/NCDs should have a minimum credit rating as specified by a credit rating agency registered with the SEBI.
- **Valuation report:** All listed entities are required to submit a valuation report from an independent Chartered Accountant to SEBI as per the SEBI circular dated 10 March 2017. The SEBI circular on listing of NCRPS/NCDs requires that such a valuation report should also include valuation of the underlying NCRPS/NCDs to be issued pursuant to the scheme of arrangement.
- **Disclosures in the scheme of arrangement:** The SEBI circular prescribes certain disclosures to be made in the draft scheme of arrangement. These disclosures, *inter alia,* include terms of payment of dividends/coupon including frequency, terms of redemption and credit rating.
- **Ensure compliance with the 2013 Act and other regulations:** The issue of NCRPS/NCDs should be compliant with the provisions of the 2013 Act including the provisions relating to creation and maintenance of Capital Redemption Reserve/ Debenture Redemption Reserve.

  Additionally, it should comply with all the provisions of SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 and SEBI (Issue and Listing of Debt Securities) Regulations, 2008 except the provisions relating to making a public issue, or making a private placement, or filing of offer document, etc.

  In case of issue of NCDs, the issuer is required to ensure compliance with the following additional conditions in accordance with the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 and the 2013 Act:

  - Appointment of a debenture trustee
  - Creation of charge or security.
- **Issue of securities in demat form:** The NCRPS/NCDs should be issued in dematerialised form only.

II. Conditions to be complied with after the scheme of arrangement is sanctioned by the High Court/NCLT and at the time of making application for relaxation under Rule 9(7) of the Securities Contracts (Regulation) Rules, 1957

The SEBI circular on listing of NCRPS/NCDs requires that an application for relaxation under Rule 19(7) of the SCR Rules for listing of NCRPS/NCDs should complete the following requirements:

- Include a compliance report as per the format prescribed in the circular and
- Comply with the provisions of SEBI circular on listing of NCRPS/NCDs, SEBI circular on listing of equity and warrants, and with other regulatory requirements specified for schemes of arrangement.

Additionally, the compliance report is required to be certified by the company secretary and the managing director of the entity.

Applicability: The draft schemes of arrangements filed with the stock exchange after the date of the SEBI circular on listing of NCRPS/NCDs i.e. 26 May 2017 would be governed by the provisions of the recent circular (dated 26 May 2017).

The above conditions have to be complied with in addition to the requirements specified under the SEBI circular dated 10 March 2017.

Key takeaways

- The recently released SEBI circular brings an important change in the scheme of arrangements involving merger, amalgamation, etc. by the listed entities. Now the schemes could involve issue of NCRPS/NCDs as part of consideration in addition to equity shares. The circular paves way for listing of NCRPS/NCDs issued in a scheme of arrangement on the recognised stock exchanges.
- The SEBI circular on listing of NCRPS/NCDs clarifies that only the NCRPS/NCDs issued to the holders of the listed specified securities in a scheme of arrangement would be eligible for listing i.e. even if the same series/class of NCRPS/NCDs have been allotted to the other investors, then such NCRPS/NCDs would not be eligible for listing.
- The conditions specified in the SEBI circular on listing of NCRPS/NCDs are to be complied with in addition to the requirements specified earlier by SEBI in the circular dated 10 May 2017 on listing of equity shares and warrants. The listed entities would now be required to make certain additional disclosures as mandated by the recent SEBI circular on listing of NCRPS/NCDs. These, *inter alia,* include terms of payment of dividend, terms of redemption, credit rating and tenure of NCRPS/NCDs.

(Source: SEBI circular no. CIR/IMD/DF/50/2017 dated 26 May 2017 and KPMG in India' First Notes dated 6 June 2017)

SEBI prescribed fine for non-compliance with the provisions of the ICDR Regulations

Background

Regulation 111A of the SEBI ICDR Regulations 2009 provides that the entity or any person who contravenes any of the provisions of ICDR Regulations should be liable for the imposition of fine by the respective stock exchange(s), in the manner specified in the circulars or guidelines.

Regulation 111B of ICDR Regulations 2009 provides that if the listed entity fails to pay any fine imposed upon it by the recognised stock exchange(s), within the specified period, the stock exchange may initiate such other action in accordance with law, after giving a notice in writing.

New development

The SEBI through its circular dated 15 June 2017 imposed a fine on the companies for non-compliance of following provisions of ICDR Regulations and also prescribed the following fine structure for first non-compliance and for subsequent and consecutive non-compliance:

Regulations	Particulars Fines imposed
Regulation 95(1), Delay in completion of bonus issue	• Fine of INR20,000 per day of non-compliance till the date of compliance • In case non-compliance continues for more than 15 days – additional fine of 0.01 per cent of paid up capital* of the entity or INR1 crore, whichever is less.
Regulation 75, Companies not allotting the shares on conversion of convertible securities within 18 months	
Regulation 108(2), Issuer not approaching the exchange for listing of equity shares within 20 days from date of allotment.	

(* Paid up capital for the purpose of imposition of fine should be the paid capital as on first day of the financial year in which non-compliance occurs.)

Additionally, the circular prescribed the following procedures for stock exchanges to be followed in case of non-compliance:

- The amount of fine realised by stock exchange should be credited to the 'Investor Protection Fund'
- The names of the non-complaint listed entity that are liable to pay fine should be disseminated on the website of stock exchange along with the amount of fine imposed, details of fines received, etc.
- The notice should be issued to the non-complaint listed entity to pay fine within 15 days from the date of notice
- In case any non-complaint listed entity fails to pay the fine, appropriated enforcement action, including prosecution should be initiated against such entity
- Further it has been clarified with respect to bonus issue delays:
  - The date of commencement of trading should be considered as 'implemented'
  - The recognised stock exchange should grant approvals to the bonus shares allotted to persons other than the promoter in the interest of the investors, subject to compliance with other requirements
  - The approval for the promoter's bonus shares should be granted by the stock exchange after payment of the requisite fine of the company.

Key takeaway

- The notification of a revised fine structure by SEBI brings a stronger mechanism to check non-compliance of ICDR Regulations by entities.

(Source: SEBI circular CIR/CFD/DIL/57/2017 dated 15 June 2017)

Updates relating to RBI regulations

RBI issues notifications clarifying certain accounting and disclosure requirements in financial statements of banks

Background

To prescribe a uniform and consistent approach for classification of assets by banks and to ensure an adequate level of provisioning on those assets on the basis of an objective criteria, on 1 July 2015, RBI updated the Master Circular on Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances (the Master Circular).

New development

On 18 April 2017, RBI issued three important circulars which deal with the following topics:

- **Additional provisions for standard advances at higher than the prescribed rates:** To enhance the stability of the financial sector, RBI issued a circular advising banks to ensure that they have adequate provisions for loans and advances at all times. It encouraged banks to consider higher provisioning rates for standard assets (as compared to the minimum rates prescribed in the Master Circular) and review the provisions made for advances to stressed sectors of the economy.

  Further, with a view to ensure that banks have adequate provisions for loans and advances at all times, RBI, through its circular, requires banks to:

  - Put in place a board approved policy for making provisions for standard assets based on evaluation of risk and stress in various sectors. The RBI encouraged banks to adopt a higher provisioning rate for the standard assets as compared to the regulatory minimum prescribed in the Master Circular.
  - Review the board approved policy (as explained above), at least on a quarterly basis, on the basis of the performance of various sectors of the economy to which the bank is exposed and evaluate the present and emerging trends of the economy and stress therein. The review should include quantitative and qualitative aspects (for example, industry performance and issues, financial ratios, credit ratings, non-performing assets, etc.) and may include sector specific parameters.
  - Specifically, RBI requires the Board of Directors of banks to review the provisioning for standard assets of the telecom sector and consider making a higher provision thereon by 30 June 2017. The RBI observed that the telecom sector was currently reporting stressed financial conditions and presently, the interest coverage ratio for the sector was less than one.

- **Disclosure in the 'Notes to Accounts' to the financial statements-Divergence in the asset classification and provisioning:** The Master Circular specifies the criteria for classification of Non-Performing Assets (NPAs) and the minimum provision rates for each class of NPA. It also prescribes that banks may make additional provision for expected losses on the NPAs.

  The RBI, as part of its supervisory processes has assessed compliance by banks with the above prudential norms and observed instances of material divergences in the asset classification and provisioning levels. The RBI has indicated that these divergences have led to the published financial statements not depicting a true and fair view of the financial position of the concerned banks.

  Accordingly, in order to ensure transparency, banks would be required to make suitable disclosures in the Notes to Accounts in the ensuing annual financial statements published immediately following communication of such divergences by RBI to the bank, where:

  - The additional provision requirements assessed by RBI exceed 15 per cent of the published net profits after tax for the reference period, or
  - The additional gross NPAs identified by RBI exceed 15 per cent of the published incremental gross NPAs for the reference period, or both.

Disclosure requirements

- The disclosures would be included under the sub-head 'Asset Quality (Non-Performing Assets)'
- The first such disclosure with respect to the divergences observed by RBI for FY2015-16 would be made in the notes to accounts of financial statements for the year ended 31 March 2017
- The RBI has also notified the format in which such disclosure should be made by the banks.

- **Guidelines on compliance with Accounting Standard (AS) 11:** AS 11, *The Effects of Changes in Foreign Exchange Rates* requires entities to recognise exchange differences arising on translation of non-integral foreign operations in the Foreign Currency Translation Reserve (FCTR) account. The amounts in this reserve are transferred to or recognised in the statement of profit and loss on full or partial disposal of the foreign operation. AS 11 observes that such disposal may be through sale, liquidation, repayment of share capital or abandonment of all or part of that operation. Further, payment of a dividend is considered to form part of a disposal only when it constitutes a return of the investment.

  The RBI observed that banks have been recognising gains in the statement of profit and loss from FCTR on repatriation of accumulated profits/retained earnings from overseas branches. The RBI clarified that such repatriation of accumulated profits/retained earnings should not be considered as disposal or partial disposal of interests in non-integral foreign operations as per AS 11 and banks should not recognise a proportionate amount of exchange gains or losses held in the FCTR in the statement of profit and loss.

Applicability: Banks are required to ensure compliance with the notifications (above) in their financial statements from the year ended 31 March 2017 onwards.

Key takeaways

- The RBI's notifications relating to enhanced provisioning requirements for assets advanced to stressed sectors and disclosure of divergence in provisioning levels are intended to build resilience in the banks' balance sheets towards any future deterioration in asset quality.

  The direction of these norms is also consistent with the requirements under Ind AS where banks will have to consider expected credit losses for the purposes of determining loan provisions.
- With disclosures on divergence from the Income Recognition, Assets Classification and Provisioning (IRACP), RBI is expected to be stringent with reference to accountability on the part of the banks towards its stakeholders for non-compliance with the classification and provisioning norms. This is likely to encourage banks to be compliant with the norms or provide reasons for not adhering to the same.

  This is a significant departure from the long standing practice of ensuring that regulatory inspections and their outcomes are confidential between RBI and the inspected/supervised institution.
- The guidelines provided to clarify accounting under AS 11 reiterate that dividends would form part of a disposal only when they constitute a return of the investment. This may have an adverse impact on profits of banks that have recognised exchange gains on repatriation of funds by their overseas branches.

(Source: RBI notification no. RBI/2016-17/281, notification no. RBI/2016-17/282 and notification no. RBI/2016-17/283 dated 18 April 2017 and KPMG in India First Notes dated 21 April 2017)

Prudential guidelines - banks' investment in units of REITs and InvITs

Background

The SEBI has put in place regulations for Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs) and requested RBI to allow banks to participate in these schemes.

Currently, banks are allowed to invest in equity-linked mutual funds, Venture Capital Funds (VCFs) and equities to the extent of 20 per cent of their net owned fund. It was proposed to allow banks to invest in REITs and InvITs within this umbrella limit.

New development

The RBI through a notification dated 18 April 2017 issued 'Prudential guidelines - Banks' investment in units of REITs and InvITs'. The notification allows banks to participate in REITs and InvITs within the overall ceiling of 20 per cent of their net worth permitted for direct investments in shares, convertible bonds/debentures, units of equity-oriented mutual funds and exposures to VCFs (both registered and unregistered), subject to the following conditions:

- Banks should put in place a board approved policy on exposures to REITs/InvITs which lays down an internal limit on such investments within the overall exposure limit of the real estate and infrastructure sectors
- Banks should not invest more than 10 per cent of the unit capital of a REIT/InvIT
- Banks should ensure adherence to the prudential guidelines issued by RBI from time to time on equity investments by banks, classification and valuation of investment portfolio, Base III capital requirements for commercial real estate exposures and large exposure framework, as applicable.

Key takeaway

- The notification by RBI allows banks to invest in the units of REITs/InvITs subject to the conditions given above. Participation by banks in the units of REITs/InvITs is expected to expand the capital base of REITs/InvITs.

(Source: RBI notification no. RBI/2016-17/280 dated 18 April 2017)

Other regulatory updates

CBDT issued draft ICDS on real estate transactions

On 31 March 2015, the Ministry of Finance (MoF) issued 10 Income Computation and Disclosure Standards (ICDS) operationalising a new framework for computation of taxable income by all assessees other than an individual or a Hindu Undivided Family (HUF) who is not required to get his/her accounts of the previous year audited in accordance with the provisions of Section 44AB of the IT Act. Such assessees need to follow the mercantile system of accounting, for the purposes of computation of income chargeable to income tax under the head 'Profits and Gains of Business or Profession' or 'Income from other sources'. The ICDS are applicable to specified assessees from Assessment Year (AY) 2017-18.

The Finance Minister constituted a Committee (the Committee) comprising of experts from accounting, departmental officers and representatives from the ICAI to recommend the areas in respect of which further ICDS may be notified under the IT Act.

New development

The Committee vide a press release dated 11 May 2017 issued the draft ICDS on real estate transactions (draft ICDS). The draft ICDS is based on the Guidance Note issued on real estate transactions by ICAI (ICAI GN) in 2012. For the purposes of providing uniformity, certainty and to harmonise the same with provisions of the IT Act, the Committee suggested certain changes to the draft ICDS in comparison to the ICAI GN.

Overview of the draft ICDS is as follows:

- **Applicability:** The ICDS should be applied for determination of income from all forms of transactions in real estate, including land, building and rights in relation thereto. This will include the following:
  - Sale of plots of land (including long term sale type leases) without any developments.
  - Sale of plots of land (including long term sale type leases) with development in the form of common facilities.
  - Development and sale of residential and commercial units, row houses, independent houses, with or without an undivided share in land.
  - Acquisition, utilisation and transfer of development rights.
  - Redevelopment of existing buildings and structures.
  - Joint development agreements for any of the above activities.
- **Recognition:** The draft ICDS provides recognition principles under following categories:
  - Projects where the economic substance is similar to a construction contract: Apply Percentage Of Completion Method (POCM) as per ICDS III, *Construction Contracts* to recognise project revenue and project costs.
  - Projects where the economic substance is not similar to a construction contract: Apply ICDS IV, *Revenue Recognition.* Provisions of para 3,4 and 5 of ICDS IV would apply provided the specific conditions mentioned in ICDS.
  - Indicators of economic substance of project being similar to a construction contract.
- **Transferable Development Rights (TDRs):** Cost of acquisition of development rights should be added to the project cost in case the development rights are utilised in real estate project.
  - *In case of rights acquired by way of direct purchase or development and construction of built-up area:* Recognise cost of acquisition as the cost of purchases or amount spent on development or construction of built up area, respectively.
  - *In case of rights acquired by way of giving up of rights over existing structures or open land:* Development rights should be recorded at fair value of the acquired development rights.

- Cost of acquisition should be added to the project costs in case the development rights are utilised in a real estate project.
- *In case of sale/transfer of development rights:* Revenue should be recognised if both the conditions mentioned below are met:
  - Title of the right is transferred to the buyer and
  - It is reasonable to expect that the revenue will be ultimately collected.

- **Transactions with multiple elements:** In case of a contract for delivery of goods or services in addition to the construction or development of real estate between a person and a buyer:
  - Contract consideration should be split into separately identifiable components including one for the construction and delivery of real estate units.
  - Consideration received or receivable should be allocated to each component on the basis of the fair value of each component.
  - Recognition of revenue of each of the components should be as per the provisions of the relevant ICDS.
- **Disclosures:** Disclosure requirements of the draft ICDS are as follows:
  - Disclose amount of project revenue recognised as revenue in the period.
  - Disclose the methods used to determine the project revenue recognised in the period.
  - Disclose the method used to determine the stage of completion of the project.
  - In case of projects in progress as at the end of the previous year, disclose:
    - The aggregate amount of costs incurred and profits recognised (less recognised losses) to date
    - The amount of advances received
    - The amount of work in progress and the value of inventories and
    - Excess of revenue recognised over actual bills raised (unbilled revenue).
- **Transitional provisions:**
  - Project revenue and project costs associated with the real estate project, which commenced on or after 1 April 201X should be recognised in accordance with the provisions of this standard.
  - Project revenue and project costs associated with the real estate project, which commenced on or before the 31 March 201X but not completed by the said date, should be recognised based on the method regularly followed by the person prior to the previous year beginning on the 1 April 201X.

Key takeaways

- The issue of draft ICDS on real estate transaction is a welcome step as there is no specific guidance in Indian GAAP for accounting for such transactions and the accounting is largely driven by the ICAI GN.
- The draft ICDS is largely aligned with the accounting principles prescribed in the ICAI GN. However, there are few areas where it differs from ICAI GN:
  - The draft ICDS defines project as smallest group of units, plots or saleable spaces, as the case may be, which are linked with a common set of basic facilities which is different from the definition given in ICAI GN.
  - The draft ICDS does not include an illustrative list of items to be included, allocated or excluded in the project cost as given in the ICAI GN.
  - The GN permits all methods for determining POCM e.g., cost incurred, survey of work done, technical estimation, etc. The GN, however, puts a cap on recognition of revenue based on POCM with reference to project cost incurred. The draft ICDS does not provide for capping the recognition of revenue based on POCM determined with reference to the project cost incurred.
  - The ICDS proposes recognition of TDRs acquired by way of giving up of rights over existing structures or open land, then TDRs would be recorded at the fair value of the TDRs so acquired. While the GN required them to be recorded at fair market value or net book value.
- Variations from Ind AS: Since the draft ICDS is based on ICAI GN, it has certain differences from Ind AS such as recognition of revenue under Ind AS is on fair value of consideration received or receivable.

Please refer KPMG in India's First Notes dated 15 May 2017 for detailed analysis of draft ICDS issued by the MoF.

(Source: MoF notification press release dated 11 May 2017)

Expert Advisory Committee (EAC) opinions issued by ICAI during the quarter ended June 2017

Topic	Month
Forfeiture of bank guarantees of contractors	April 2017
Accounting treatment of exchange variation arising in respect of foreign operations of the company held through a wholly owned foreign subsidiary company as per AS 11, *The Effects of Changes in Foreign Exchange Rates*	May 2017
Accounting treatment of release of funds by project implementation trust fund	June 2017

(Source: The ICAI Journal: The Chartered Accountant for the months of April, May and June 2017)

Glossary

2013 Act	The Companies Act, 2013
MCA	The Ministry of Corporate Affairs
SEBI	The Securities and Exchange Board of India
Ind AS	Indian Accounting Standards
ICAI	The Institute of Chartered Accountants of India
RBI	The Reserve Bank of India
AS	Accounting Standard
PY	Previous Year
AY	Assessment Year
FY	Financial Year
YTD	Year-to-date
NBFC	Non-Banking Financial Company
GAAP	Generally Accepted Accounting Principles
PPE	Property, Plant and Equipment
IRDAI	The Insurance Regulatory and Development Authority of India
IASB	The International Accounting Standard Board
ITFG	Ind AS Transition Facilitation Group
CFS	Consolidated Financial Statements
NCI	Non-Controlling interest
DDT	Dividend Distribution Tax
ED	Exposure Draft
IFC	Internal Financial Controls
ROC	Registrar of Companies
NCLT	National Company Law Tribunal
Listing Regulations	SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
NCRPS	Non-Convertible Redeemable Preference Shares
NCDs	Non-Convertible Debentures
SCR Rules	Securities Contracts (Regulation) Rules, 1957
NPA	Non-Performing Asset
FCTR	Foreign Currency Translation Reserve
REITs	Real Estate Investment Trusts
InvITs	Infrastructure Investment Trusts
CBDT	Central Board of Direct Taxes
IT Act	Income-tax Act, 1961
GN	Guidance Note
ICDS	Income Computation and Disclosure Standards
POCM	Percentage of Completion Method
TDRs	Transferable Development Rights
FVOCI	Fair Value Through Other Comprehensive Income
FVTPL	Fair Value Through Profit or Loss
EIR	Effective Interest Rate
FAQ	Frequently Asked Question
AGM	Annual General Meeting
IEPF	Investor Education and Protection Fund

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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.

Missed an issue of Accounting and Auditing Update or First Notes?

IFRS Notes

IRDAI defers the effective date for implementation of Ind AS in the insurance sector to 1 April 2020

23 June 2017

On 28 June 2017, the Insurance Regulatory Development Authority of India (IRDAI) has decided to defer the implementation of the Indian Accounting Standards (Ind AS) in the insurance sector in India for a period of two years. Accordingly, Ind AS for Indian insurance companies would now be applicable from 1 April 2020 (instead of 1 April 2018 its earlier notified date).

However, insurance companies would still be required to submit the pro forma Ind AS financial statements to IRDAI on a quarterly basis effective from 31 December 2016. Therefore, the requirement to submit pro forma Ind AS financial statements on a quarterly basis has not been deferred.

This issue of IFRS Notes provides an overview of the recent circular issued by IRDAI.

MCA issues further relaxations from certain provisions of the Companies Act, 2013

23 June 2017

Background

The Ministry of Corporate Affairs (MCA) through its notifications dated 5 June 2015, provided certain exceptions/modifications/ adaptations to some of the provisions of the Companies Act, 2013 (2013 Act) for the following class of companies:

- Private companies
- Companies formed with the charitable objects, etc. (Section 8 companies)
- Government companies.

New development

The MCA through its notifications dated 13 June 2017 and 22 June 2017, provided further exceptions/ modifications/adaptations to the provisions of the 2013 Act for the above mentioned class of companies (i.e. private companies, Section 8 companies and government companies).

These exceptions/modifications/adaptations would be available to the companies which have not defaulted in filing of its financial statements under Section 137 or annual return under Section 92 of the 2013 Act with the Registrar of Companies.

This issue of First Notes provides an overview of the exceptions/modifications/ adaptations made to the 2013 Act for private companies, Section 8 companies and government companies.

Accounting and Auditing Update

KPMG in India's Accounting and Auditing Update (AAU) each month covers emerging topics on Ind AS, an update on the Companies Act, 2013 and other important regulatory and financial reporting updates in India and internationally.

This edition of AAU explains the concept of a business model assessment to be undertaken by banks on transition to Ind AS for their financial instruments. Our article covers two scenarios: loans advanced and investments made in debt instruments by banks. The accounting for these two scenarios has been explained with the help of case studies.

Our article on deemed cost accounting under Ind AS explains the deemed cost exemption and also highlights the challenges/implications in accounting on Ind AS transition when a company chooses to apply the deemed cost exemption for its property, plant and equipment. This article also covers the implication on Minimum Alternate Tax (MAT) computation both on transition and in subsequent annual financial statements.

Under the Companies Act, 2013 (2013 Act) section, we describe the key responsibilities of directors. The article also compares the requirements of the 2013 Act with the Securities and Exchange Board of India's (SEBI) regulations with regard to directors.

This month's edition also carries an article on the accounting of lease of land under Ind AS. Our article emphasises the need to assess all of the lease classification indicators before classifying a lease as an operating or a finance lease.

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

Feedback/queries can be sent to
aaupdate@kpmg.com

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