MCA notified certain provisions of the Companies (Amendment) Act, 2017

28 May 2018

Introduction

On 3 January 2018, the Companies (Amendment) Act, 2017 (Amendment Act, 2017) received the assent of the President of India. The various provisions of the Amendment Act, 2017 would come into force on the date of their notification in the Official Gazette by the central government. Different dates could be appointed for different provisions of the Amendment Act, 2017.

The Ministry of Corporate Affairs (MCA) has notified the enforcement of the provisions of Section 1 and Section 4 of the Amendment Act, 2017 with effect from 26 January 2018. Additionally, MCA notified 43 sections with effect from 9 February 2018. The key sections notified were:

- Declaration of dividend (Section 123 of the Companies Act, 2013 (2013 Act))
- Powers and duties of auditors and auditing standards (Section 143 of the 2013 Act)
- Related party transactions (Section 188 of the 2013 Act).

Recently, MCA through its notification dated 7 May 2018 notified certain sections of the Amendment Act, 2017. Additionally, MCA issued amendment to certain rules under the Companies Act, 2013 (2013 Act). The notified provisions are effective from 7 May 2018.

This issue of First Notes aims to provide an overview of the recently notified sections of the Amendment Act, 2017 and the amendments issued to the rules to the 2013 Act.

The amendments are in respect with the following provisions:

- Loans and investments by companies
- Meetings of board and its powers
- Financial reporting—Accounts of foreign subsidiaries
- Audit and auditors
- Appointment and qualification of directors
- Others

Sector

All
- Banking and insurance
- Information, communication, entertainment
- Consumer and industrial markets
- Infrastructure and government

Relevant to

All
- Audit committee
- CFO
- Others

Transition

Immediately
- Within the next three months
- Post three months but within six months
- Post six months
- Forthcoming requirement
Overview of the notified provisions

The table below provides an overview of the sections notified and the consequential amendments made in the corresponding rules:

Loans and investments by companies

| Loan to directors, etc. (Section 185) | Companies can now provide loan, guarantee or security in connection with any loan, to any person in whom the director is interested, subject to prior approval by a special resolution. Additionally, such loans should be utilised by the borrowing company for its principal business activities. Further, companies that provide loans, give guarantees, or securities in the normal course of business, are permitted to do so at specified interest rate i.e. not less than the rate of prevailing yield of one year, three year, five year or 10 year government security, closest to the tenure of the loan (currently, specified interest rate is rate not less than the bank rate declared by the Reserve Bank of India (RBI)). |
| Loan and investment by company (Section 186 and the Companies (Meetings of Board and its Powers) Amendment Rules, 2018- (Meetings Amendment Rules, 2018)) | Currently, under the 2013 Act, a company could give loan/guarantee or provide any security in connection with the loan to any person/other body corporate that exceeds 60 per cent of its paid-up share capital, free reserves and securities premium account or 100 per cent of its free reserves and securities premium account, whichever is more, only if a special resolution is passed. The Amendment Act, 2017 clarifies that the companies cannot give loan/guarantee or provide any security to any person/other body corporate in excess of the specified limit. However, in case where the aggregate of the loans or investment made, guarantee given or security provided together with the proposed loan/guarantee/security exceed the specified limit, a special resolution would be required to provide any investment/loan/guarantee or security. Additionally, it has been clarified that the company is allowed to give loan to its employees in excess of the specified limits without passing a special resolution. Similarly, the requirement of special resolution would not be applicable in cases where a loan, guarantee, or security is provided to the company’s wholly owned subsidiary or a joint venture, or the company acquires the securities of its wholly owned subsidiary. In this relation, MCA amended the Companies (Meetings of Board and its Powers), Rules 2014, to provide that the special resolution should specify the total amount up to which the Board of Directors (BoD) are authorised to provide such loan or guarantee, security or acquire shares of other companies. Additionally, definition of an investment company has been modified to provide that a company would be deemed to be principally engaged in the business of acquisition of shares, debentures or other securities, if its:
• Assets in the form of investment in shares, debentures or other securities constitute not less than 50 per cent of its total assets, or
• Its income derived from investment business constitutes not less than 50 per cent as a proportion of its gross income. |

Financial reporting- Accounts of foreign subsidiaries

| Copy of financial statements filed with registrar (Section 137) | Currently under the 2013 Act, every company with subsidiary(ies) is required to file with the Registrar of Companies (ROC) accounts of its foreign subsidiary(ies). The Amendment Act, 2017 clarifies that if the accounts of foreign subsidiary(ies) are not required to be audited, then Indian holding company should file such unaudited financial statements to the RoC along with the declaration to this effect. In case such financial statements are in a language other than English a translated copy of the financial statements would also be filed. |

Notes:
1. ‘Any person in whom director is interested’ means:
   - Any private company of which any such director is a director or member,
   - Any body corporate at a general meeting of which not less than 25 per cent of the total voting power may be exercised or controlled by any such director, or by two or more such directors, together, or
   - Any body corporate, the Board of Directors (BoD), the Managing Director (MD) or manager, whereof is accustomed to act in accordance with the directions or instructions of the BoD, or of any director or directors, of the lending company.
Appointment and qualification of directors

Resident director (Section 149)

The requirement for a director to be resident in India would be met if he stays in India for a total period of 182 days or more during the financial year (earlier the 2013 Act referred to previous calendar year and now changed to financial year). However, in case of a newly incorporated company the above requirement would apply proportionately at the end of the financial year in which a company has been incorporated.

Independent director (Section 149 and the Companies (Appointment and Qualification of Directors) Second Amendment Rules, 2018)

Following changes have been introduced with respect to provisions of an independent director:

- Pecuniary relationship will not include the remuneration received by an independent director and any amount from a transaction which does not exceed 10 per cent of his/her total income (or such amount as may be prescribed).
- Section 149(6)(d) has been amended with respect to the scope of restriction on a ‘pecuniary relationship or transaction’ entered by a relative and has been made more specific by clearly categorising the types of transaction. The Amendment Act, 2017 provides that the none of the relatives of independent director:
  i. Should hold any security of or interest in the company, its holding, subsidiary or associate company during the two immediately preceding financial years or during the current financial year. However, the relative may hold security or interest in the company of face value not exceeding INR50 lakh or two per cent of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed;
  ii. Is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors, in excess of such amount as may be prescribed during the two immediately preceding financial years or during the current financial year (the Companies (Appointment and Qualification of Directors) Rules specify that indebtedness should not be in excess of INR50 lakh);
  iii. Has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for such amount as may be prescribed during the two immediately preceding financial years or during the current financial year (the Companies (Appointment and Qualification of Directors) Rules specify that such indebtedness should not be in excess of INR50 lakh),
  iv. Has any other pecuniary transaction or relationship with the company, or its subsidiary, or its holding or associate company amounting to two per cent or more of its gross turnover or total income singly or in combination with the transactions referred to in above clause (i), (ii) or (iii).
- The 2013 Act restricts an individual from being appointed as an independent director in case he/she or his/her relative is a Key Managerial Person (KMP) or an employee of the company or its holding, subsidiary or associate company during any of the preceding three financial years. The Amendment Act, 2017, clarifies that this restriction would not apply if a relative of an independent director is employed during the preceding three financial years.

Disqualification for appointment of a director (Section 164)

Currently, a director of a company which has defaulted on certain requirements is not eligible to be reappointed as a director of that company or appointed in another company for a period of five years from the date of the failure. Those defaults are as follows:

- Not filed financial statements or annual returns for any continuous period of three financial years or
- Failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared for a continuous period of one year.

The Amendment Act, 2017 has clarified that a director would not incur disqualification (if the company has defaulted on the above grounds) for a period of six months from the date of his/her appointment. The 2013 Act provides that a director would be disqualified in the following scenarios:

- Convicted by a court for any offence
- Disqualification as a director on the order of the court/Tribunal and
- Convicted in the matter of Related Party Transactions (RPTs).

The Amendments Act, 2017 clarifies that the above disqualifications would continue to apply even if an appeal or petition has been filed against the order of conviction or disqualification.
Appointment and qualification of directors (cont.)

**Vacation of office (Section 167)**

Section 167 of the 2013 Act specifically provides that the office of a director would become vacant in case he/she incurs disqualifications specified in Section 164 of the 2013 Act or becomes disqualified by an order of a court or the Tribunal.

However, the Amendment Act, 2017 clarifies that in case a director gets disqualified on grounds of Section 164(2) of the 2013 Act (i.e. non-filing of financial statements or failure to repay dues), then the office of the director would become vacant in all the companies other than the company which is in default under Section 164(2).

Additionally, the Amendment Act, 2017 has provided a relaxation and provided that a director would not be required to vacate his/her office in respect of disqualification by an order of a court or the Tribunal or conviction for any offence in the following events:

- a) For 30 days from the date of conviction or order of disqualification
- b) Where an appeal or petition is preferred within 30 days as aforesaid against the conviction resulting in sentence or order, until expiry of seven days from the date on which such appeal or petition is disposed of or
- c) Where any further appeal or petition is preferred against order or sentence within seven days, until such further appeal or petition is disposed of.

Earlier the 2013 Act was stringent and required that the office should be vacated by the director even if he/she has filed an appeal against the order of such court.

**Resignation of director (Section 168 and the Companies (Appointment and Qualification of Directors) Second Amendment Rules, 2018)**

The 2013 Act requires resigning director to submit a copy of his/her resignation along with detailed reasons for the resignation in form DIR-11 to RoC within 30 days of the resignation.

The Amendment Act, 2017 makes aforementioned filing optional for the directors. Similar amendments have been incorporated in the Companies (Appointment and Qualification of Directors) Rules, 2014.

**Meeting of Board and its powers**

**Meetings of Board (Section 173 and the Meetings Amendment Rules, 2018)**

The 2013 Act empowered the central government to specify matters which should not be dealt in a meeting through video conferencing or other audio visual means. These matters include the approval of the annual financial statements, the approval of the Board’s report, etc.

The Amendment Act, 2017 and the Meetings Amendment Rules, 2018 clarify that in case the quorum for a meeting is met through physical presence of directors, then any other director may participate through video conferencing or other audio visual means and discuss the matters as specified.

**Audit committee (Section 177 and the Meetings Amendment Rules, 2018)**

According to the Amendment Act, 2017, the BoD of every listed public company (earlier the 2013 Act referred to every listed company) and such other class or classes of companies, as may be prescribed should constitute an audit committee. Similar amendment has been incorporated in Companies (Meetings of Board and its Powers) Rules, 2014 as well.

The Amendment Act, 2017 clarifies that the existing requirement under the 2013 Act for the audit committee to pre-approve all RPTs subject to the approval of the BoD or shareholders as required by the Section 188 would continue. Whereas, for transactions that are not covered under the Section 188, the audit committee can give recommendations to the BoD, in case it does not approve the transaction.

Additionally, a transaction (involving an amount up to INR1 crore) is voidable at the option of the audit committee if it has been entered without its approval and has not been ratified subsequently by it.

Further, where the transaction is with a related party of a director, or a director has authorised the transaction, such director would indemnify the company against any loss.

Further, RPTs between a holding company and its wholly-owned subsidiary that do not require board’s approval under Section 188, would not require approval of the audit committee.
Meeting of Board and its powers (cont.)

Nomination and Remuneration Committee (NRC) (Section 178)

Following changes have been made to the provisions relating to NRC:

- Every listed public company (earlier the 2013 Act referred to every listed company) and a company covered under Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014 is required to constitute a NRC.
- NRC is required to specify the methodology for effective evaluation of the performance of the individual directors, committees of the board and the board as a whole which should be carried out by the board, by the NRC or by an independent external agency and should review its implementation and compliance.
- Additionally, companies could place their remuneration policy on their website, if any, and should disclose only the salient features of the policy, the changes, if any, along with the web address of the policy in the board’s report.

Audit and auditors

Appointment of Auditors (Section 139 and the Companies (Audit and Auditors) Amendment Rules, 2018 (Auditors Amendment Rules, 2018))

Currently under the 2013 Act, companies are required to appoint their auditors for a period of five years which is subject to annual ratification by the shareholders at the annual general meeting.

The Amendment Act, 2017 has removed this requirement of annual ratification once the auditors have been appointed for five years. The provision with respect to the annual ratification has been removed from Companies (Audit and Auditors) Rules 2014 as well.

Others

Definitions (Explanation to Section 2(6) and Section 2(87) and the Companies (Specification of Definitions Details) Amendment Rules, 2018)

- Significant influence: In the revised definition of an ‘associate company’, significant influence means control of at least 20 per cent of the total voting power (earlier total share capital), or control of or participation in business decisions under an agreement. (Section 2(6))
- Joint venture: Currently, the term ‘joint venture’ has not been specifically defined in the 2013 Act and the definition of an associate company included the term ‘joint venture’. The Amendment Act, 2017 defines ‘joint venture’ as a ‘joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement’. The definition is in accordance with Ind AS 28, Investments in Associates and Joint Ventures. (Section 2(6))
- Subsidiary: The Amendment Act 2017 replaced the term ‘total share capital’ (i.e. paid-up equity share capital and convertible preference share capital) by the term ‘total voting power’ as the basis for deciding holding/subsidiary relationship. (Section 2(87))

Also the definition of total share capital has been removed from the Companies (Specification of Definitions Details) Rules, 2014.

Matters to be stated in prospectus (Section 26(1) and the Companies (Prospectus and Allotment of Securities) Amendment Rules, 2018)

The Amendment Act, 2017 empowers Securities and Exchange Board of India (SEBI) to prescribe the contents of a prospectus. Accordingly, a public company is not required to provide certain details in the prospectus (as given in clause (a), (b) and (d) of the Section 26(1) of the 2013 Act) such as names and addresses of its registered office, dates of the opening and closing of the issue, its capital structure, and auditor’s report on the company’s profits/losses and assets and liabilities. Therefore, these clauses have been omitted through the Amendment Act, 2017

Similar provisions have been removed from the Companies (prospectus and Allotment of Securities) Rules, 2014.
Others (cont.)

### Issue of sweat equity shares

**Section 54(1)**

The Amendment Act, 2017 permits companies to issue sweat equity shares within one year of the date of commencement of business, thus, omitted the provision of the 2013 Act which restricted companies to do so.

### Share certificate

**The Companies (Share Capital and Debentures) Amendment Rules, 2018**

The MCA amended the Companies (Share Capital and Debentures) Rules to provide that the share certificates are required to be signed by two directors (any two directors of the company) or a director (any director of the company) and a company secretary, where appointed.

Earlier the requirement was that the certificates would mandatorily be signed by company secretary (wherever appointed) in addition to two directors.

### Registration of charges

**Section 77 and 78**

The 2013 Act requires companies to register charges within 30 days of its creation.

The Amendment Act, 2017 provides that aforementioned provision is not applicable to charges as prescribed in consultation with RBI.

### National Company Law Appellate Tribunal (NCLAT)

**Section 410**

Appeals in relation to the orders of the National Financial Reporting Authority (NFRA) would be made to the NCLAT.

### Special Courts

The Amendment Act 2017 amends the provisions with respect to the constitution of special courts.

### Our comments

The enactment of the 2013 Act which became effective 1 April 2014 was one of the most significant legal reforms in India. Since the implementation of 2013 Act, MCA has issued a number of clarifications and amendments to the 2013 Act to resolve the implementation challenges faced by the India Inc. The introduction of Amendment Act, 2017 is one such step from MCA to address the concerns related to the 2013 Act.

The issue of Amendment Act, 2017 has been a long drawn process which started with the constitution of the Companies Law Committee (CLC) in June 2015 to review and simplify the 2013 Act. The CLC recommended amendments to both the 2013 Act and the Rules thereto. The central government considered the suggestions made by the CLC and incorporated the suggestions in the Amendment Act, 2017 and made amendments in the Rules to the 2013 Act, as the relevant sections were notified.

Some of the key changes notified recently are:

**Alignment of definitions:** Some of the fundamental definitions in the 2013 Act were inconsistent with the AS/Ind AS and had effect on number of provisions of the 2013 Act. Some of the important changes to definitions are as follows:

- **Subsidiary:** The definition of subsidiary in the 2013 Act referred to ‘total share capital’ i.e. aggregate of the paid-up equity share capital and the convertible preference share capital. Now, the Amendment Act, 2017 has changed the reference to ‘total voting power’. In many cases, the total voting power would be with reference to the equity share capital. However, if dividend in respect of a class of preference shares has not been paid for a period of two years or more, then such class of preference shareholders would also have right to vote on the resolutions placed before the company.

- **Joint Venture:** The 2013 Act did not define the term ‘joint venture’ and made reference to joint venture as an inclusive part in the definition of the term ‘associate company’. The Amendment Act, 2017 continues to refer joint venture within the term associate company but also defines joint venture in line with Ind AS 28. However, Ind AS 28 further defines the terms ‘joint arrangement’ and ‘joint control’ which are associated with the definition of joint venture. While the Amendment Act, 2017 does not include these definitions, we believe that the intent of the law has been to align the definition of joint venture with Ind AS and therefore, the two associated definitions of joint control and joint arrangement could be read harmoniously with Ind AS.
Our comments (cont.)

Loans and investments by companies
The newly notified provision permits companies to provide loans/guarantees/security to any person in whom the director is interested, subject to specified conditions. This is a welcome step as it is expected to provide significant relief to the companies and to resolve practical issues being faced in genuine transactions of financing among group companies due to complete restriction on providing loans enforced by the 2013 Act.

On the other hand, it would also put onerous responsibility on the management to clearly distinguish the transactions entered into with persons in whom its directors are interested.

The Amendment Act, 2017 provides relaxation to companies in relation to loans/security/ guarantee provided to the company’s wholly owned subsidiary or a joint venture, or when the company acquires the securities of its wholly owned subsidiary. The relaxation was earlier available in Rule 11 of the Companies (Meetings of Board and its Powers) Rules 2014. The change introduced through the Amendment Act, 2017 incorporates the provisions into the 2013 Act, hence, resolve the anomaly.

Financial reporting – accounts of foreign subsidiaries
A listed company with a foreign subsidiary(ies) has also been provided some relief in relation to submission of financial statements with RoC. If the accounts of foreign subsidiary(ies) are not required to be audited, then Indian holding company would need to file such unaudited financial statements with the RoC along with the declaration to this effect. The notification providing relaxation is timely as companies are in the process of filing their financial statements for the year ended 31 March 2018.

Appointment and qualification of directors
- **Residential status:** The change in the requirement of residential status would provide clarity to the non-resident director that if he/she stays in India for a total period of 182 days or more during the financial year (earlier the 2013 Act referred to previous calendar year and now changed to financial year).
- **Transactions outside the scope of pecuniary relationship for an independent director:** The Amendment Act, 2017 specifically excludes the amount of remuneration received by an independent director and any transaction up to 10 per cent of his/her total income from the definition of pecuniary relationship. The change is very significant and expands the scope of transactions that an independent director could enter into. However, such transactions would still be monitored by the companies in order to ensure the independence of an independent director at all times.

Additionally, the Amendment Act, 2017 has modified the scope of restriction on a ‘pecuniary relationship or transaction’ entered by a relative by clearly categorising them into types of transactions. These restrictions are in relation to holding of a security or interest, indebtedness, providing guarantee or security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company. Additionally, the restrictions also scope in any other pecuniary transaction or relationship. The Amendment Act, 2017 provides relief to independent directors by specifying thresholds up to which these restrictions would not apply.

- **Vacation of office by director:** Earlier, the 2013 Act specified that if any director incurs disqualification specified under Section 164(2) (i.e. non-filing of financial statements/annual return or failure to repay dues by the company) then such director should immediately vacate offices in all the companies where he or she is a director. This situation posed a challenge for the companies if they have committed the default as their office of directors would become vacant due to disqualification. Also the company would have difficulty in appointing a new director as such new director would also attract disqualification.

To resolve these issues, the Amendment Act 2017 provides that in case of disqualification specified under Section 164(2), the director would vacate offices in all companies except the company which is in default. Further, the person appointed as director in defaulting company would not incur disqualification for a period of six months from the date of appointment. Additionally, the director of a company under such default would continue to remain liable for the affairs of the defaulting company.

Meetings of board and its powers
The Amendment Act, 2017 provides a relaxation for private companies that have listed their debt instruments by making the requirement to constitute audit committee and NRC being applicable to only listed public companies. The 2013 Act requires preapproval of audit committee for all RPTs, subject to approval by BoD or shareholders. The Amendment Act, 2017 allows ratifications by the audit committee within three months from the date of transaction (entered into by a director or officer) without obtaining the prior approval of audit committee if the transaction amount is upto INR1 crore.

Annual ratification of auditors not required as per the Amendment Act, 2017:
Companies are not required to get the continuance of an auditor ratified by the shareholders on an annual basis once the auditors have been appointed for five years.

Remaining sections – not yet notified
The Amendments Act, 2017 is largely effective with recent notification as MCA notified 28 sections of the Amendment Act, 2017. Earlier MCA had notified 43 sections with effect from 9 February 2018 and two sections with effect from 26 January 2018.

Following are some of the key sections which are still pending to be notified:
- Issue of shares on private placement basis
- Prohibition on acceptance of deposits from public
- Repayment of deposits
The bottom line

With the recent MCA notification, the Amendment Act, 2017 is now largely effective. The new legislations and changes introduced are vast and therefore, the companies should take notice of these changes.

Our comments (cont.)

• Declaration of beneficial interest in any share
• Few clauses relating to annual return
• Annual General Meeting
• Financial statement, board’s report, etc.
• Corporate social responsibility
• Managerial remuneration
• Calculation of profits
• Inspection, inquiry and investigation.
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.

Ind AS Transition Facilitation Group (ITFG) issues Clarifications Bulletin 15

18 April 2018

The Ind AS Transition Facilitation Group (ITFG) in its meeting considered certain issues received from the members of the Institute of Chartered Accountants of India (ICAI), and issued its Clarifications’ Bulletin 15 on 5 April 2018 to provide clarifications on 10 application issues relating to Indian Accounting Standards (Ind AS).

This issue of IFRS Notes provides an overview of the clarifications issued by ITFG through its Bulletin 15.

Missed an issue of Accounting and Auditing Update or First Notes

Issue no. 21 – April 2018

The topics covered in this issue are:
• Ind AS 115 - Impact on pharmaceutical sector
• Accounting for instruments held as regulatory capital by banks
• Enhanced focus on other information in auditor reporting
• Frequently asked questions on business combinations
• Regulatory updates.

FRRB issues its observations on compliance with financial reporting requirements by listed and other companies

8 May 2018

Recently, the Financial Reporting Review Board (FRRB) of the Institute of Chartered Accountants of India (ICAI), issued its third volume of ‘Study on Compliance of Financial Reporting Requirements’ (the study). The study highlights instances of non-compliance by certain companies with regard to reporting requirements prescribed under:
• Accounting Standards
• Standards on auditing
• Schedule II and schedule III to the Companies Act, 2013/Revised Schedule VI to the Companies Act, 1956 and
• Other relevant laws and regulations.

In this issue of First Notes, we provide an overview of the key observations of the FRRB with respect to AS and Schedule II and III to the Companies Act, 2013 as provided in its study.

Voices on Reporting

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

In a special session held on 18 May 2018, we discussed the key amendments in the SEBI Listing Regulations based on the recommendations of the Kotak Committee report.

Click here to access the audio recording (mp3) and presentation (pdf).

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

Previous editions are available to download from: www.kpmg.com/in

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