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Voices on Reporting

9 January 2020

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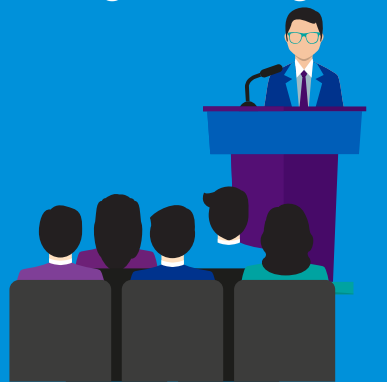
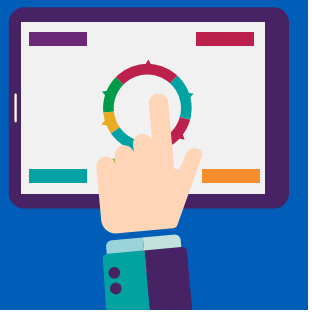
Welcome

01 Series of knowledge sharing calls



02 Covering current and emerging reporting issues



03 Scheduled towards the end of each month

04 Look out for our Accounting and Auditing Update, First Notes and Voices on Reporting publications

Speaker for the webinar

Ruchi Rastogi

Partner

Assurance
KPMG in India

Agenda

1. **The Taxation Laws (Amendment) Act, 2019**
2. Ind AS Transition Facilitation Group (ITFG) clarifications - Bulletin 22
3. Updates relating to SEBI regulations
4. Updates relating to the Companies Act, 2013

The Taxation Laws (Amendment) Act, 2019[1]

Key highlights

- On 20 September 2019, the Taxation Laws (Amendment) Ordinance, 2019 (Ordinance) was issued to make certain amendments to the provisions of the Income-tax Act, 1961 (IT Act) and the Finance (No.2) Act, 2019 with effect from Financial Year (FY) 2019-20.
- The key amendments relate to the following:
  - Tax concession for domestic companies
  - Tax concession for new domestic manufacturing companies
  - Reduction in Minimum Alternate Tax (MAT) rate and
  - Buy-back provisions.
- On 11 December 2019, received the President's assent to replace the tax ordinance.

The Taxation Laws (Amendment) Act, 2019 (cont.)

Lower tax rates from FY 2019-20

Option of tax rate of 22 per cent

- Option available to **any domestic company** subject to the condition that it will **not avail certain specified deductions/ incentives**.
- Effective tax rate would be 25.17 per cent inclusive of surcharge and cess.
- Not required to pay MAT.

Option of tax rate of 15 per cent

- Applicable to **new domestic manufacturing company incorporated on or after 1 October 2019** and commences **its production on or before 31 March 2023.**
- **Not allowed to avail certain specified deductions/incentive.**
- Effective tax would be 17.16 per cent inclusive of surcharge and cess.
- Not required to pay MAT.

**Specified deductions inter alia, include Special Economic Zone (SEZ) benefit,* additional depreciation, including set-off of loses arising from these deductions/incentives.

Key changes from the Ordinance

The Tax Act has introduced certain other amendments to the IT Act and the Finance (No.2) Act, 2019. The key amendments are as follows:

Whether activities like software development, production of films constitute manufacture?	Whether past MAT credits will be available?	New manufacturing company
Issue now clarified to state that following activities do not constitute manufacture: a. Development of computer software in any form or in any media b. Mining c. Conversion of marble blocks or similar items into slabs d. Bottling of gas into cylinder e. Printing of books or production of cinematograph film or f. Any other business as may be notified by CG in this behalf.	The issue is now settled wherein the past MAT credits will not be available to companies opting for the lower rate.	• In case the conditions specified for lower rate of 15 per cent are not satisfied, such companies eligible to opt for 22 per cent rate • Option of 22 per cent available for non manufacturing income of such companies.

Key considerations

- MAT credits
- Non-availability of specified deductions/incentives for lower tax rates
- Quarterly tax provisioning
- Impact on financial statements for financial year 2019-20
- Deferred tax impact
- Advance tax computations

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Determination of lease term[2]

Guidance under Ind AS 116, *Leases*

In determining a lease term, and consequently whether a lease is a short-term lease, **only the enforceable rights of the lessee** to renew or extend the lease beyond the non-cancellable period should be considered.

Scenario I

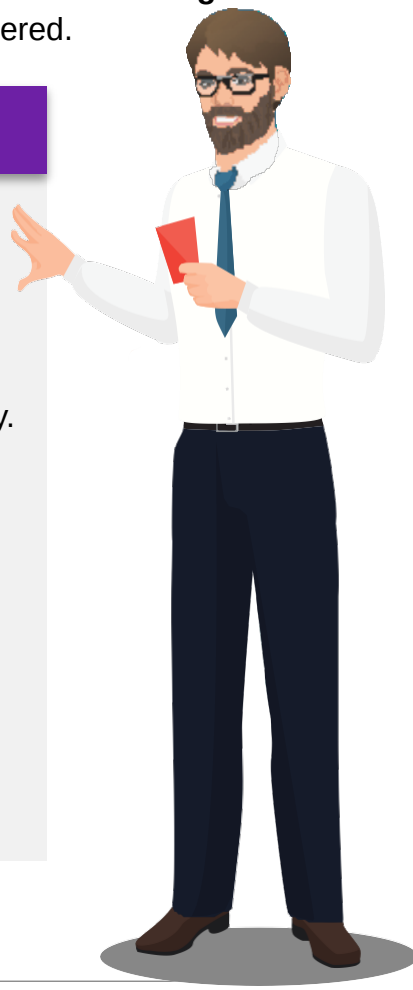
Lease agreement for a period of 12 months or less and does not grant a renewal or extension option to the lessee

- An agreement would qualify as a short-term lease.
- The conclusion would not change even if there is a past practice of the lease being renewed upon expiry for further one year at a time with the mutual consent of the lessee and the lessor.

Scenario II

Lease agreement can be terminated by giving one month's prior notice

- At the time of lease commencement, it should be assessed that if there is an **economic incentive** to not exercise the option to terminate the lease prematurely.
- Consider all relevant facts and circumstances including any expected changes in facts and circumstances during the lease period at the time of assessment.
- If it is reasonably certain at lease commencement that the termination option would not be exercised, then the lease would not qualify as a short term lease.



Accounting for lease rental income in case of operating lease by a lessor[2]

Requirements under Ind AS 17*

Ind AS 17, *Leases* did not permit scheduled lease rental increases to be recognised on a straight-line basis over the lease term if lease rentals were structured to increase in line with expected general inflation to compensate for the lessor's expected inflationary cost increases. It requires such increases to be recognised in the respective period of increase.

Requirements under Ind AS 116

Ind AS 116 requires operating lease rentals to be recognised on a straight-line basis (or on another systematic basis if such other basis is more representative of the pattern in which benefit from the use of the underlying asset is diminished).

Clarification

The ITFG clarified the accounting of the rental income of the operating lease by the lessor, in accordance with Ind AS 116 as under:

- Recognise operating lease rentals on a straight-line basis over the lease term, even though the lease rentals are structured to increase in line with expected general inflation to compensate for its expected inflationary cost increases.
- The resultant change in manner of recognition of operating lease rentals represents a change in an accounting policy which would need to be accounted for as per Ind AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors* in the absence of specific transitional provisions in Ind AS 116 dealing with the change.

*Ind AS 116 is applicable for annual reporting periods beginning on or after 1 April 2019 and Ind AS 17 has been superseded.

Accounting treatment of gifts and other sales promotion activities[2]

Ind AS requirements

- Ind AS 115, *Revenue from Contracts with Customers* is applicable **only** if the counterparty to the contract is a customer
- Ind AS 38 **applies** amongst others, to accounting of expenditure on **advertising**, training, start-up, research and development activities

Issue

- What would be the accounting of gifts and other sales promotion activities undertaken to develop or create brands or customer relationships which in turn generate revenue?

Clarification

- The accounting of gifts is not in the scope of Ind AS 115. This is because gifts do not create enforceable rights and obligations as there is no contract to obtain goods or services in exchange for consideration.
- In this case, Ind AS 38 would apply and expenditure relating to sales promotion activities would be recognised as expense when the entity has a right to access those goods. An entity has a right to access goods when it owns them, or otherwise has a right to access them regardless of when it distributes the goods.
- Thus, the entity should recognise the expenditure on items to be distributed as gifts as an expense when it owns those items, or otherwise has a right to access them, regardless of timing of distribution.

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Prompt disclosure in case of loan defaults[3]

On 21 November 2019, SEBI issued a circular to provides new norms relating to loan defaults for listed entities.

Requirements under Listing Regulations relating to loan defaults

- Regulation 30 requires equity listed entities to disclose to stock exchange(s) all events or information, which are material.
- Regulation 51 with Part B of Schedule III) requires listed entities (with NCDs* or NCRPS**) to provide specific disclosures in case of delay or default in payment of interest/redemption of NCDs and NCRPS for a period of more than three months from the due date.

Additional disclosure requirements

Listed entities would disclose to the stock exchanges when there is a default in payment of:

- Interest/instalment obligations on loans, including revolving facilities like cash credit, from banks/financial institutions and
- Unlisted debt securities.

*NCDs – Non-Convertible Debt securities
**NCRPS – Non-Convertible Redeemable Preference Shares

Prompt disclosure in case of loan defaults (cont.)

Timing of disclosure: The circular lays down the timing of disclosure to stock exchanges under following situations:

1 At the time of each instance of default

Default in loans from banks and financial institutions beyond 30 days

Prompt disclosure but not later than 24 hours from the 30th day of such default.

Default in unlisted debt securities i.e. NCDs and NCRPS

Prompt disclosure but not later than 24 hours from the occurrence of the default.

2 Default as on the last day of the quarter

- Default on loan continues beyond 30 days or
- Outstanding debt security under default

Report within seven days from the end of the quarter.

Prompt disclosure in case of loan defaults (cont.)

Disclosure formats

The circular prescribes two different reporting formats for complying with the disclosure requirements:

- At the time of each instance of default:
  a) For loans including revolving facilities like cash credit from banks/financial institutions
  b) For unlisted debt securities i.e. NCDs and NCRPS.
- At the end of each quarter: Disclosure in case there is any outstanding amount under default as on the last day of the quarter (to be reported within seven days from the end of the quarter).

Effective date

The circular is effective from 1 January 2020.

Disclosure of divergence in the asset classification and provisioning by banks[4]

RBI Requirements

RBI requires banks to disclose material divergences in their asset classification and provisioning in their annual financial statements, if either or both of the following conditions are satisfied:

- The additional provisioning for Non-Performing Assets (NPAs) assessed by RBI exceeds 10 per cent of the reported profit before provisions and contingencies for the reference period
- The additional gross NPAs identified by RBI exceed 15 per cent of the published incremental gross NPAs for the reference period.

On 31 October 2019, SEBI tightened the disclosure norms for banks after consultation with RBI. As per the circular:

- Listed banks should provide the disclosure in case of NPA divergence and provisioning beyond specified threshold (provided above), as soon as reasonably possible and not later than 24 hours upon receipt of the RBI's final Risk Assessment Report (RAR).
- Disclosure would be provided in a format prescribed by RBI (provided in Annex-A to SEBI circular).

New requirements with regard to an auditor's resignation[5]

- SEBI Listing Regulations require disclosure of detailed reasons to the stock exchanges when there is a resignation by an auditor as soon as possible but not later than 24 hours of receipt of such reasons from the auditor.
- On 18 October 2019, SEBI issued a circular clarifying mandatory conditions to be complied with when a statutory auditor of a listed entity or its material subsidiary resigns, in relation to a limited review/audit report.

Conditions to be complied with while appointing an auditor

Auditor resigns within 45 days from the quarter end

Auditor should, before such resignation, issue the limited review/audit report for such quarter.

Auditor resigns after 45 days from the quarter end

Auditor should, before such resignation, issue the limited review/audit report for such quarter as well as the next quarter.

In case an auditor signed the limited review/audit report for the first three quarters of a financial year, then the auditor would be required to issue the limited review/audit report for the last quarter and for such financial year.

New requirements with regard to an auditor's resignation (cont.)

Obligations of a listed entity and its material subsidiary

Information to be obtained from the statutory auditor upon resignation: The circular specifies the format to obtain information from the auditor on resignation.

Co-operation to provide all documents: Requirement to provide all such documents/information as may be necessary for the audit/limited review during the period from when the auditor proposes to resign till the auditor submits its report.

Disclosure of views of the audit committee to the stock exchanges: Upon resignation by an auditor, the listed entity should ensure disclosure of the views of the audit committee to the stock exchanges as soon as possible but not later than 24 hours after the date of audit committee meeting.

Applicability of BRR widened[6]

Current requirements

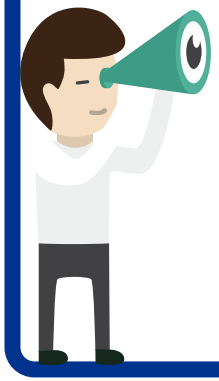
Top 500 listed entities based on market capitalisation (calculated as on 31 March of every year) requires mandatory submission of Business Responsibility Report (BRR)* along with the annual report.

New requirements

With effect from 26 December 2019, SEBI extended the applicability of BRR to top 1,000 listed entities.

*BRR should describe the initiatives taken by the said listed entities from an environmental, social and governance perspective, in the format specified by SEBI.

Format for statement of deviation/variation of end use of issue proceeds[7]



- Regulations 32 of the SEBI Listing Regulations requires a listed entity to submit a statement of deviation or variation, pursuant to review by the audit committee, to the stock exchange on a quarterly basis for public issue, rights issue, preferential issue, etc. The statement should include:
  - Deviations, if any, in the use of proceeds of public issue, rights issue, preferential issue etc. and
  - The category wise variation between projected utilisation of funds and the actual utilisation of funds.
- SEBI through its circular dated 24 December 2019, issued a format for statement of deviation/variation in utilisation of funds raised.
- The key features of the circulars are as below:

Applicability

- Every listed entity that has raised funds through public issue, rights issue, preferential issue, QIPs, etc.

Frequency of disclosures

- Disclose on quarterly basis along with the declaration of financial results, until such funds are fully utilised or the purpose for which these proceeds were raised has been achieved.

Role of audit committee

- The statement of deviation report should be reviewed by the audit committee
- The comments of audit committee would be disclosed to the stock exchange along with the report.

The new formats have been made effective from the quarter ending 31 December 2019.

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4. **Updates relating to the Companies Act, 2013**

New norms for data bank of independent directors[8]

- Section 150 of the 2013 Act provides that an independent director can be selected from a data bank maintained by any body, institute or association, as may by notified by the Central Government (CG).
- The data bank would contain names, addresses and qualifications of persons who are eligible and willing to act as independent directors. The company should exercise due diligence before selecting an independent director from the data bank.
- On 22 October 2019, MCA issued certain notifications relating to the creation and maintenance of the data bank for independent directors.

These relates to the following:

Notification of the Companies (Creation and Maintenance of data bank of Independent Directors) Rules, 2019

Constitution of institute for data bank of independent directors

Additional disclosure in board's report

Compliances required by the independent directors

New norms for data bank (cont.)

Additional disclosure in board's report

The MCA has amended Rule 8 of the Companies (Accounts) Rules to provide that the board's report should also contain a statement regarding an opinion of the board of directors with regard to integrity, expertise and experience (including the proficiency) of the independent directors during the year.

Compliances required by independent directors

The MCA has amended Rule 6 of the Companies (Appointment and Qualifications of Directors) Rules. As per the amendment, following individuals should apply online to the institute for inclusion of their names in the data bank for a period of one year or five years or for their life-time:

a) *Every individual who has been appointed as an independent director in a company as on 1 December 2019:* Within a period of three months from 1 December 2019 i.e. up to 29 February 2020 and

b) *Every individual who intends to get appointed as an independent director in a company after 1 December 2019:* Before his/her appointment.

An individual (including an individual who does not have a DIN) can also apply voluntarily to the institute.

Effective date: The amendments and data bank rules are effective from 1 December 2019. The rule pertaining to definitions and panel to be created for approving the courses and study material of the institute are effective from 22 October 2019.

Revised threshold for transactions with related parties[9]

On 18 November 2019, MCA amended Rule 15(3) of the Companies (Meetings of Board and its Powers) Rules, 2014 and specified revised thresholds for transactions with related parties which would require shareholders' approval by an ordinary resolution.

The table below provides summary of the revised thresholds:

Prescribed transaction categories	Amount beyond which shareholders' approval is required	
	Existing	Revised
Sale, purchase, or supply of any goods or materials (directly or through an agent)	10 per cent or more of the turnover or INR100 crore, whichever is lower*	10 per cent or more of the turnover
Selling or otherwise disposing of, or buying, property of any kind (directly or through an agent)	10 per cent or more of the net worth or INR100 crore, whichever is lower*	10 per cent or more of the net worth
Leasing of property of any kind	10 per cent or more of the net worth or 10 per cent or more of the turnover or INR100 crore, whichever is lower*	10 per cent or more of the turnover
Availing or rendering of any services (directly or through an agent)	10 per cent or more of the turnover or INR50 crore, whichever is lower*	10 per cent or more of the turnover
Appointment to any office or place of profit in the company, subsidiary company or associate company	Remuneration exceeding INR2.5 lakh per month	No change
Underwriting the subscription of any securities or derivatives of the company	Remuneration exceeding one per cent of net worth	No change

(*Applies to transaction or transactions to be entered into either individually or taken together with the previous transactions during a FY.)

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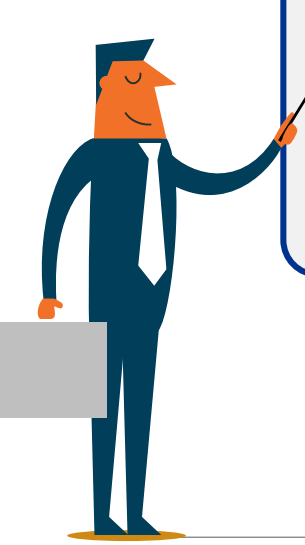
Q&A

Sources

1. The Taxation Laws (Amendment) Act, 2019 issued by the Ministry of Law and Justice dated 12 December 2019).
2. ICAI-ITFG clarification bulletin 22 dated 14 October 2019.
3. SEBI circular SEBI/HO/CFD/CMD1/CIR/P/2019/140 dated 21 November 2019.
4. SEBI circular CIR/CFD/CMD1/120/2019 dated 31 October 2019.
5. SEBI circular number CIR/CFD/CMD1/114/2019 dated 18 October 2019.
6. SEBI (Listing Obligations and Disclosure Requirements) (Fifth Amendment) Regulations, 2019 dated 26 December 2019.
7. SEBI circular CIR/CFD/CMD1/162/2019 dated 24 December 2019.
8. MCA notifications S.O. 3791(E.), G.S.R. 805(E.), G.S.R. 804 (E.), G.S.R. 803(E.) dated 22 October 2019.
9. MCA notification G.S.R. 857(E.) dated 18 November 2019.

Glossary

- SEBI - The Securities and Exchange Board of India
- 2013 Act - The Companies Act, 2013
- ICAI - The Institute of Chartered Accountants of India
- Ind AS - Indian Accounting Standards
- MCA - The Ministry of Corporate Affairs
- MAT - Minimum Alternate Tax
- ITFG - Ind AS Transition Facilitation Group
- FY – Financial Year
- IT Act – The Income-tax Act, 1961
- SEZ - Special Economic Zone
- CG - Central Government
- NCDs – Non-Convertible Debt securities
- NCRPS – Non-Convertible Redeemable Preference Shares
- RBI - The Reserve Bank of India
- Listing Regulations - SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
- BRR - Business Responsibility Report



Links to previous recordings of VOR

Month	Topics	Link
July 2019	• Brief overview of Ind AS 116, Leases transition options and considerations • Prudential framework for resolution of stressed assets • Over of the new guidance relating to uncertainty over income tax treatments • Important Ind AS implementation issues provided in the Ind AS Technical Facilitation Group (ITFG) Bulletin 19 and 20	Click here
August 2019 (special session)	• Prevention of insider trading and safeguarding of UPSI • Issuance of Differential Voting Rights (DVR) shares • Revised formats for compliance report on corporate governance	Click here
August 2019	• Ind AS 116, *Leases* - Impact on the technology sector	Click here
September 2019	• Clarification on 'appointed date' and 'acquisition date' in a scheme of arrangement issued by the Ministry of Corporate Affairs (MCA) • Important Ind AS implementation issues provided in the Ind AS Technical Facilitation Group (ITFG) clarifications bulletin 21 • Accounting impact of the recent tax reductions for domestic companies in India • SEBI revised formats for compliance report on corporate governance • Other regulatory updates	Click here
November 2019 (Special session)	• Focus on technology sector- Impact of recent tax amendments and certain challenge	Click here

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Our publications

Accounting and Auditing Update

First Notes

Coming up next

New issue of:

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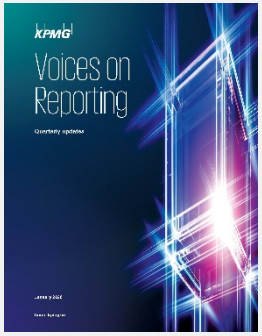

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KPMG in India contact:

Ruchi Rastogi
Partner
Assurance
E-mail: ruchirastogi@kpmg.com

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

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