2ND INTERNATIONAL CONFERENCE

FINANCIAL REPORTING & CONTROL: EMERGING DEVELOPMENTS, CHALLENGES, AND SOLUTIONS

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FOREWORD FROM SECRETARY GENERAL, ASSOCHAM

Over the past two decades, India Inc. has highlighted the need for a renewed focus on corporate governance as a response to many corporate failures. The emergence of new governance practices have led to investors and other stakeholders to follow a more cautious approach. An adoption of stronger and more transparent measures has proved to be capable enough to retain stakeholders and encourage fresh investment for doing business sustainably.

To make, transform and build more agile organizations through a combination of better internal management as well as efficient reporting, stronger regulatory compliances and communicating with other external stakeholders depends on how economic performance measurement systems are designed and managed. An improvement in key concepts, frameworks in financial accounting standards, integrated financial reporting, management accounting and control systems will help in accomplishing multiple and complex goals.

The 2nd edition of the International Conference on “Financial Reporting & Control: Emerging Developments, Challenges, and Solutions” on 21st July 2022 at New Delhi is an opportunity to uncover the newer developments in this sector and the report of ASSOCHAM and BDO will help provide clarity on topical issues for better compliances and reporting towards improving benchmark practices and governance.

I acknowledge the efforts made by the teams at BDO and ASSOCHAM National Council for Corporate Affairs, Company Law and Corporate Governance towards bringing out the joint background paper.
My best wishes for a successful conference and broader outreach of this publication.

DEEPAK SOOD
Secretary General,
ASSOCHAM

FOREWORD FROM COUNCIL CHAIRPERSON, ASSOCHAM

Corporate Governance has turned out to be a critical component globally for protecting and balancing the interest of stakeholders through transparency, disclosure and accountability. Reporting of financial and non-financial data is now more critical and central to governance.

New-age technologies coupled with the application of big data within the accounting field are playing a pivotal role and bringing out transformative impact through transparent and real-time, better management control systems. A review and revisit of the adoption of standards, policies together with technological advancements have implications for accounting information systems and compliances which lead to better control, decision making and governance.

ASSOCHAM National Council for Corporate Affairs, Company Law and Corporate Governance has been at the forefront of impactful policy advocacy, enhancing awareness about subjects that are pertinent to company law and securities law and strengthening overall corporate governance through a range of activities in its educative discourse. In the series, the 2nd edition of the International Conference on "Financial Reporting & Control" aims to discuss, deliberate and update the knowhow about emerging developments, challenges, and solutions with respect to recent regulatory frameworks in India as well as global best practices.

I convey my best wishes to the organizing team and trust that this conference would be an enriching experience for all associated stakeholders.

PREETI MALHOTRA
Chairperson, ASSOCHAM National Council for Corporate Affairs,
Company Law and Corporate Governance,
Chairman, Smart Bharat Group & Past President, ICSI

FOREWORD FROM DEPUTY MANAGING PARTNER, BDO IN INDIA

Many of you would recollect that it was around a year back when ASSOCHAM launched a virtual conference covering developments and challenges in the field of financial reporting & control during the remote-working-covid-19 regime.

While thankfully the scene is looking brighter this year, there's still some ground to cover for the old normal as we knew it. So, thanks to ASSOCHAM, we will meet once again on 21st July for the 2nd International Conference – this time to also discuss solutions in addition to emerging developments and challenges in financial reporting & control.

Hon'ble member of parliament & Member- Standing Committee on Finance, Shri Suresh Prabhu, has gracefully consented to be the Chief Guest for this event and share his valuable views on the theme of the conference.
Similarly, we have the kind consent of Hon'ble member of parliament & Member - Standing Committee on Finance, Labour, Textiles & Skill Development and Committee on Public Accounts, Shri Subhash Chandra Baheria, to be our Guest of Honor and to share his knowledgeable views with us as well.

As we continue to embrace the best practices in the space of 'Financial Reporting & Control', there are developments across accounting, auditing, and corporate laws, with a view to enhance our governance standards.

Investors and stakeholders are currently plagued by concerns over poor corporate governance, lack of ethical behaviour, transactions with related parties, companies collapsing under the weight of poor accounting & auditing, savings plan & retirement plans evaporating suddenly, credibility of oversight & enforcement actions, dominance of technology and control over it etc

To address such genuine concerns, regulators & standard setters are constantly looking to upgrade reporting & auditing requirements & tightening the screws over internal controls framework.

As a result, we have continuous changes/developments/amendments on various aspects of financial reporting & controls. These developments come with their own set of challenges of interpretation, implementation, applicability, scope etc.

It is the need of the day to discuss various aspects of new rules & challenges as well as the solutions available to us and we are proud to be associated with ASSOCHAM as their knowledge partner as they take on dissecting these topics for larger benefit.

Last but not least, we take this opportunity to thank all panel speakers and those who have registered for the conference. We hope that those of you dealing with financial statements and regulatory aspects would find the conference informative and relevant.

YOGESH SHARMA
Deputy Managing Partner
BDO in India

RECENT AMENDMENTS TO IND AS (IND AS AMENDMENT RULES 2022) AND COMPARISON WITH IFRS

Indian Accounting Standards (Ind- AS) are primarily converged with the International Financial Reporting Standards (IFRS) as issued by International Accounting Standards Board. Certain amendments were made in IFRS and pursuant to the same corresponding amendments were issued by the Ministry of Corporate Affairs (MCA) to Ind-AS through a notification dated March 23, 2022.

An overview of these amendments is as follows:

1. Ind-AS 16 “Property Plant and Equipment” – Para 16 of the standard defines cost as:

   “The cost of an item of property, plant and equipment comprises:

   a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.

   b) any **costs directly attributable** to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

   c) ……….”

   Para 17 of Ind-AS 16 lists certain examples of “directly attributable costs” as

   e) costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment) “

   Amendment in 2022 clarified the accounting for “the excess of the net proceeds from selling any items produced”. This excess should be reduced from the directly attributable costs and should not be recorded in Statement of Profit and Loss.

   Carve Out from IFRS
   This amendment has led to a carve out from IAS 16, “Property, Plant and Equipment”. In May 2020, IASB has amended IAS 16 to record, the excess of the net proceeds from selling any items produced before the related PPE is available for use, in Statement of Profit and Loss.

2. Ind-AS 37 “Provisions, Contingent Liabilities and Contingent Assets” – Para 10 defines Onerous contracts as *“An onerous contract is a contract in which the **unavoidable costs** of meeting the obligations under the contract exceed the economic benefits expected to be received under it.”*

   Para 68 states *“The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the **cost of fulfilling** it and any compensation or penalties arising from failure to fulfil it.”*

   Amendment in 2022, defines the **Cost of Fulfilling** as follows:
   The cost of fulfilling a contract comprises the costs that relate directly to the contract. Costs that relate directly to a contract consist of both-

   a) the incremental costs of fulfilling that contract—for example, direct labour and materials; and

   b) an allocation of other costs that relate directly to fulfilling contracts— for example, an allocation of the depreciation charge for an item of property, plant and equipment used in fulfilling that contract among others.

3. Ind-AS 103 “Business Combinations”

   IASB has revised its “Conceptual Framework for Financial Reporting” in March 2018. In order to converge with the IASB framework, Institute of Chartered Accountants of India has developed the “Conceptual Framework for Financial Reporting under Indian Accounting Standards (Conceptual Framework)” in 2020.

   Amendment in 2022 has substituted the reference to erstwhile framework with the new framework, without amending the requirements of accounting for business combination.

   Pursuant to the change, there was timing difference in recognition of certain Levies as mentioned in Appendix C to Ind-AS 103 vis a vis the liability assumed in the business combination on the acquisition date. To resolve this implication, an exception was added to Ind-AS 37 for such levies to be governed by Appendix C rather than assumption of liability on acquisition date.

   Further, a paragraph has been added to explicitly prohibit recognition of Contingent Assets pursuant to Business combination.

   Apart from the amendments, Annual Improvements to Ind AS (2021) have been made

IND AS	AMENDMENT IN IND-AS
Ind AS 101 ‘First-time Adoption of Indian Accounting Standards’	Subsidiary as a first-time adopter. Simplifies the application of Ind AS 101 by a subsidiary that becomes a first-time adopter after its parent in relation to the measurement of cumulative translation differences.
Ind AS 109 ‘Financial Instruments’	▪ Fees included in the 10% test for derecognition of financial liabilities. ▪ The amendment clarifies which fees an entity includes when it applies the ‘10%’ test in assessing whether to derecognize a financial liability. An entity includes only fees paid or received between the entity (the borrower) and the lender, including fees paid or received by either the entity or the lender on the other’s behalf.
Ind AS 41 ‘Agriculture’	▪ Taxation in fair value measurements. ▪ The amendment removes the requirement in Ind AS 41 for entities to exclude cash flows for taxation when measuring fair value. This aligns the fair value measurement in Ind AS 41 with the requirements of Ind AS 113, Fair Value Measurement.

RECENT AMENDMENTS UNDER COMPANIES ACT, 2013, INCLUDING SCHEDULE III AND CARO 2020 – KEY CHANGES AND IMPACT ON COMPANIES

AMENDMENTS IN SCHEDULE III OF THE COMPANIES ACT, 2013

The MCA issued notifications dated March 24, 2021 to amend Schedule III to the Companies Act, 2013 read with Companies (Accounts) Rules, 2014 and Companies (Audit and Auditors) Rule, 2014. The main aim of the amendments in Schedule III of the Companies Act, 2013 is to improve the transparency in the financial statements of the company. Amendments in Schedule III are applicable from April 01, 2021.

KEY AMENDMENTS IN SCHEDULE III

- **Shareholding of promoters**
  Shareholding of Promoters at the end of the Year in tabular form containing Name, No of Shares, % of Total Shares, % change during the year (computed with respect to the number at the beginning of the year or if issued during the year for the first time then with respect to the date of issue) to be disclosed.

- **Short-term borrowings**
  Current maturities of Long-term borrowings shall be disclosed separately.

- **Trade Payable and Trade Receivable ageing Schedule**
  a) Ageing to be divided into outstanding for periods from due date of payments
  b) For trade payables, it is to be divided in MSME and others (Disputed to be shown separately)
  c) For trade receivable, it is to be divided in considered good and considered doubtful (Disputed to be shown separately)

- **Property, Plant and Equipment & Intangible Assets**
  A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment) and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.

- **Disclosure of revaluation of Property, Plant and Equipment** – whether based on the valuation by a registered valuer as defined under rule 2 of the Companies (Registered Valuers and Valuation) Rules, 2017.

- **Title deeds of Immovable Property not held in name of the Company**
  Details of all the Immovable Property (other than under lease and the agreement is in the name of the Co) whose title deeds are not held in name of the Company. If the same is held jointly with others, details to the extent of the company's shares shall be disclosed.

- **Capital Work In Progress (CWIP) & Intangible Assets**
  a) Ageing schedule
  b) For CWIP/ Intangible Assets, whose completion is overdue or has exceeded its cost compared to its original plan, CWIP completion schedule mandatory – (Projects where activity is Suspended to be given separately

- **Charge Details**
  Details of Registration or satisfaction of charge not registered with ROC beyond the time period needs to be disclosed along with reasons thereof.

- **Wilful Defaulter**
  If the company has been declared wilful defaulter by any banks/FI, the same needs to be disclosed.

- **Details of Benami Property Held**
  Disclosure of any proceedings initiated or pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 with all details like Details of such property, including year of acquisition, Amount, Beneficiaries, reference to the item in the Balance Sheet (if it is in Books of account), If property is not in the books, then the fact shall be stated with reasons, any proceedings against the company under this law as an abettor of the transaction or as the transferor then the details shall be provided.

- **Utilization of Borrowings**
  Where the company has not used the borrowings from banks and financial institutions for the specific purpose for which it was taken at the balance sheet date, the company shall disclose the details of where they have been used.

- Disclosure to be provided in case of Loans or Advances, in the nature of loans, are granted to promoters, directors, KMPs and the related parties either severally or jointly with any other person, that are:
  a) repayable on demand or
  b) without specifying any terms or period of repayment.

    - Amount of loan or advance in the nature of loan outstanding
    - Percentage to the total Loans and Advances in the nature of loans

- **Transactions with Struck off Companies**
  If your company has had any transactions with another company whose name has been struck off, disclosures have to be made accordingly.

- **Scheme of arrangement**
  In case a scheme of arrangement has been approved, relevant disclosure has to be made, such as:
  - The effect of such arrangement on the books of accounts of your company.
  - If there is any deviation from the accounting standards while giving effect to the scheme, the reasons for such deviation have to be explained.

- **Undisclosed Income**
  The Company shall give details of any transaction not recorded in the books of accounts that have been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act, 1961 (such as search or survey or any other relevant provisions of the Income Tax Act, 1961) unless there is immunity for disclosure under any scheme and also shall state whether the previously

unrecorded income and related assets have been properly recorded in the books of account during the year.

- **Disclosure in case the Company has traded or invested in Crypto Currency or Virtual Currency**
  - Profit or loss on such transactions,
  - amount of currency held as at the reporting date,
  - deposits or advances from any person for the purpose of trading or investing.

- **Disclosure with regard to Corporate Social Responsibility (CSR) Activities**
  - Amount required to be spent and expenditure incurred by the company during the year,
  - Shortfall at the end of the year along with cumulative balance and reasons for such shortfall,
  - Nature of CSR activities,
  - Details of related party transactions,
  - Movements in the provision made in case of contractual obligation.

- **Disclosures in case of borrowings from financial institutions are secured by current assets**
  - Whether statements of current assets filed with financial institutions are in line with books of accounts or not.
  - If not, summary of reconciliation and reasons of material discrepancies, if any to be adequately disclosed.

- **Ratios to be disclosed**
  - Current Ratio
  - Debt-Equity Ratio
  - Debt Service Coverage Ratio
  - Return on Equity Ratio
  - Inventory turnover ratio
  - Trade Receivables turnover ratio
  - Trade payables turnover ratio
  - Net capital turnover ratio
  - Net profit ratio
  - Return on Capital employed
  - Return on investment

  The company shall explain the items included in numerator and denominator for computing the above ratios. Further explanation shall be provided for any change in the ratio by more than 25% as compared to the preceding year).

- **Applicability of Rounding off**
  - Compulsory Rounding off figures as below:-
  - Total Income < INR 100 Crores – Nearest hundreds, thousands, lakhs or millions
  - Total Income > INR 100 Crores – Nearest lakhs, millions or crores.

COMPANIES (AUDITOR AND REPORT ORDER) 2020

Company Auditor's Report Order (CARO) 2020 is the new format for issue of audit report, in case of statutory audits of companies under the Companies Act, 2013 which includes the additional reporting requirements after the consultations with the National Financial Reporting Authority (NFRA).
Its main motive is to enhance the overall quality of reporting by the company auditors and will be applicable from April 1, 2021.
The CARO 2020 has overall 21 clauses against 16 clauses in the CARO 2016. Seven new clauses have been inserted, one clause has been merged and one deleted.
Majority of the amendments to Schedule III to the Companies Act, 2013 have been undertaken in response to the amendments covered in the newly issued Companies (Auditors and Report Order) 2020 and the Companies (Indian Accounting Standards) Amendment Rules, 2020, hence they are covered in schedule III amendment also.

KEY NEW CLAUSES

Reporting on Core investment companies, non-banking financial companies and housing finance companies

- Any non-banking financial activity or housing finance activity conducted before obtaining a certificate of registration.
- Whether a company is a core investment company (CIC) or exempted or unregistered CIC and continues to fulfil such criteria.
- Total number of CICs which are part of a group, in case, there are more than one CIC.

Reporting on Working capital loans

New reporting on whether quarterly returns or statements filed with banks or financial institutions on the basis of current assets security for sanctioned working capital limits in excess of INR 5 crores in aggregate are in agreement with the books of account, and if not, details to be reported.

Reporting on Unrecorded Income

Whether any transactions not recorded in the books of account have been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act, 1961 (43 of 1961), if so, whether the previously unrecorded income has been properly recorded in the books of account during the year;

Reporting on Internal Audit

a) whether the company has an internal audit system commensurate with the size and nature of its business;
b) whether the reports of the Internal Auditors for the period under audit were considered by the statutory auditor

Reporting on Cash Losses

Whether the company has incurred cash losses in the financial year and in the immediately preceding financial year, if so, state the amount of cash losses;

Reporting on Auditor's resignation

Whether there has been any resignation of the statutory auditors during the year, if so, whether the auditor has taken into consideration the issues, objections or concerns raised by the outgoing auditors;

Reporting on Financial Position

On the basis of the financial ratios, ageing and expected dates of realization of financial assets and payment of financial liabilities, other information accompanying the financial statements, the auditor's knowledge of the Board of Directors and management plans, whether the auditor is of the opinion that no material uncertainty exists as on the date of the audit report that company is capable of meeting its liabilities existing at the date of balance sheet as and when they fall due within a period of one year from the balance sheet date;

Reporting on CSR Compliance

a) whether, in respect of other than ongoing projects, the company has transferred unspent amount to a Fund specified in Schedule VII to the Companies Act within a period of six months of the expiry of the financial year in compliance with second proviso to sub-section (5) of section 135 of the said Act;
b) whether any amount remaining unspent under sub-section (5) of section 135 of the Companies Act, pursuant to any ongoing project, has been transferred to special account in compliance with the provision of sub-section (6) of section 135 of the said Act.

Reporting on Consolidated financial statements

Qualification/Adverse remarks in CARO in the audit report of companies which are consolidated in the CFS will be required to be reported.

KEY AMENDMENTS IN COMPANIES ACT, 2013

AMENDMENT TO RULES

- **Amendment in Rule 3 i.e. Manner of Books of Account to be Kept in Electronic Mode**
  Every company which uses accounting software for maintaining its books of account, shall use only such accounting software which has a feature of recording audit trail of each and every transaction, creating an edit log of each change made in books of account along with the date when such changes were made and ensuring that the audit trail cannot be disabled. The MCA has extended the implementation of Audit Trail software to a financial year commencing on or after April 1, 2023, earlier such provision was applicable from April 01, 2022.

- **Amendment in Rule 8 i.e. Matters to be Included in Board's Report**
  - The details of application made or any proceeding pending under the Insolvency and Bankruptcy Code, 2016 during the year along with their status as at the end of the financial year.
  - The details of difference between the amount of the valuation done at the time of one-time settlement and the valuation done while taking loan from the Banks or Financial Institutions along with the reasons thereof.

Disclosure on above mentioned two clauses are required to give in Directors Report of Companies along with other disclosures.

RECENT AMENDMENTS IN REGULATORY PROVISIONS

India has evidenced amendments in various regulations in the recent past to increase the transparency in industries functioning and enhanced quality of Financial Reporting.
Below are analysed some of the recent regulatory changes from SEBI and their effects on the listed entities they regulate as a step towards better governance and compliance.

AMENDMENTS IN SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

- SEBI (Listing Obligations and Disclosure Requirements) Amendment,2022, provides the requirement of at least 1/3rd of the Board of Directors to comprise of independent directors with the chairperson being a non-executive director and at least half of the Board of Directors to comprise of independent directors where the listed entity does not have a regular non-executive chairperson. The definition of Related party has undergone a change with effect from 1 April 2023, wherein any person or entity forming a part of the promoter or promoter group of the listed entity holding 10 % or more in the listed entity either directly or on a beneficial interest basis shall become related party. Earlier, the specified percentage prescribed was 20%.

- **Materiality of Related Party transaction (‘RPT’):** Previously, a transaction was considered as material during a financial year if it exceeded 10% of the annual consolidated turnover of the listed entity as per the last audited financial statement of the listed entity but with effect of 1 April 2023, RPT would be considered as material if the transaction entered into individually or taken together with previous transactions during a financial year exceeds INR 10 billion or 10% of the annual consolidated turnover of the listed entity as per the last audited financial statement of the listed entity, whichever is lower.

- Prior approval of the shareholder of a listed entity is needed for all material RPTs and subsequent material modifications of such transactions.

- **Related Party Transactions:** The amended definition of the related party would now include not only the transaction of a listed entity and transactions of the subsidiary with the related party of a subsidiary company. This implies that the listed entity would have to meet the approval and disclosure requirements even with respect to RPTs of a subsidiary company, where the listed entity is not a party. Additionally, with effect from 1 April 2023, the definition deems certain categories of unrelated transactions also as RPT, i.e., such transactions, the purpose, and effect of which is to benefit a related party of the listed entity or any of its subsidiaries.

- Amendments to SEBI (Alternative Investment Funds) Regulations 2022 ("AIFs"):
  I. Category AIFs shall invest maximum up to 10% of the investable funds in an Investee Company directly or through investment in the units of other AIFs except for large value funds for accredited investors of Category III AIFs which may invest up to 20%.
  II. However, for investment in listed equity of an Investee Company, Category III AIFs & large value funds for accredited investors, may calculate the investment limit of 10% & 20% respectively of either the investable funds or the net asset value of the scheme.

- Change in control of Sponsor and/or Manager of AIF involving Scheme of Arrangement under Companies Act, 2013.
  As per the SEBI, the following shall be applicable to all the Schemes which are filed with National Company Law Tribunal ("NCLT") on or after 1st April 2022:

  I. The application seeking approval for the change in control of Sponsor and/or Manager of the AIF (under the applicable AIF Regulations) shall be filed with SEBI prior to filing the same with the NCLT.

  II. SEBI shall grant an in-principal approval upon being satisfied with the compliance of applicable regulatory requirements, validity of which shall be 3 months from the date of issuance within which the relevant application shall be made to the NCLT.

  III. Within 15 days from the date of order of NCLT, the applicant shall submit the NCLT approved application & its order along with other specified documents to SEBI for final approval.

- SEBI (Issue and Listing of Non-Convertible Securities) (Amendment) Regulations, 2022 states condition of Issuing and Listing of Non-Convertible Securities:

  I. General Obligations: The issuer has to consider higher security cover as per the terms of the offer document/Debenture Trust Deed which should be sufficient to discharge the principal amount and the interest thereon.

  II. Creation of charge: The charge created on secured debt securities shall be disclosed in the offer document as well as the Debenture Trust Deed. The condition is applicable in case of public/private issue and listing of debt securities.

  III. Issue of due diligence certificate: The Debenture Trustee must furnish a separate due diligence certificate for each of the secured and unsecured debt securities, to the board and stock exchange(s), at a prescribed time and format. The condition is applicable in case of public/Private issue of debt securities and private placement of Non-Convertible Redeemable Preference Shares

  IV. Disclosure: An issuer seeking to issue its debt securities are required to include the details of credit rating along with the latest press release (not older than 1 year) of the credit rating agency validating the rating as on the issue and listing date.

AMENDMENTS IN BANKING REGULATION (AMENDMENT) ACT, 2020

- **Minimum Investment Grade Credit Ratings for Deposits of Non-Banking Financial Companies ("NBFCs")**
  As per the extant framework, NBFCs with net owned funds of INR 25 Lacs and above need to obtain a minimum investment grade or other specified credit ratings from any one of the approved credit rating agencies at least once a year, to accept public deposits.

- **Maintenance of Cash Reserve Ratio (CRR)**
  The RBI vide notification dated May 04, 2022 has increased the Cash Reserve Ratio (CRR) of all banks by 50 basis points from 4.00 percent to 4.50 percent of their Net Demand and Time Liabilities (NDTL) as is effective from the reporting fortnight beginning May 21, 2022.

IRDAI had few amendments in place to regulate the Broker / Agent dealings. Also, the regulator has asked for more and more reporting on a regular basis over the past year. These reporting's involve, information relating to Claims, handling of grievances and also, addressing Policy holder welfare.

The frequent changes in regulations are keeping managements on their toes. The auditors too are under pressure to dig deeper during audits especially for regulated entities where the reporting requirements prescribed by the regulators such as SEBI, RBI, IRDAI and MCA have become quite elaborate.

RELATED PARTY TRANSACTIONS – INCREASING FOCUS OF REGULATORS

Related party transactions (RPTs) have been the matter of concern of various regulators and law makers. Entities invariably have or are required to conduct their business through related parties either existing per se or created for strategic purposes. From a group perspective it may not be a matter of great concern for the owner of the business. However, from an individual standpoint, it becomes a matter of concern for every stakeholder – the shareholder, lender, creditor and the government.

In the realm of Corporate Governance, related party transactions hold the key place amongst others matters such as composition of Board of Directors, Board Committees, minimum holdings, etc. There are various laws established by various regulators on transactions with related parties:

- Companies Act 2013
- SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015
- Accounting Standards
- Income Tax Act, 1961, etc.

Provisions in the aforesaid laws have been evolving over the years and are becoming stricter.

The main concern being transactions carried out with malafide purposes resulting in the significant loss to the shareholders, banks and financial institutions, creditors and the Government exchequer.

WHAT IS A RELATED PARTY TRANSACTION?

The term “Related Party Transaction” refers to a deal or arrangement made between two parties who are joined by a pre-existing business relationship or common interest.

Although related-party transactions are themselves legal, they may create conflicts of interest or lead to other illegal situations like frauds, tax evasions, money laundering, etc.

REGULATORY FRAMEWORKS OVER RPTS

- Companies Act, 2013 and rules made thereunder:
  - Directors have the duty not to place themselves in a position when their fiduciary duties towards the company conflict with their personal interests.
  - It’s a director’s duty to disclose an interest in any transaction with related parties
  - Certain transactions, in which directors are interested, to take place only subject to the approval of Board/shareholders.
  - Restrictions on loans to director or holding office or place of profit by the relative of director.
  - Duty on directors to disclose information relating to directorship and shareholdings in companies.

- SEBI (Listing Obligations and Disclosure Requirement) Regulations 2015:
  - The listed entity must have a policy on materiality of related party transactions and on dealing with related party transactions and its limits for approval.

- All related party transactions shall require prior approval of the audit committee
- All material related party transactions shall require approval of the shareholders through resolution.
- Related parties shall not vote to approve the relevant transaction irrespective of whether the person is a party to the particular transaction or not, etc.

- Accounting Standards:
  - Accounting Standards focus on disclosures necessary to draw attention to stakeholders on the details of related party transactions.

- Income Tax Act, 1961:
  - Section 40A(2) of Income Tax Act, 1961 deals with payments to relatives and associated persons. Where the assessee incurs any expenditure in respect of which payment is to be made to a specified person and the same is reported in the Tax Audit report.

RPTs have been the area of focus of all audit quality inspections. Quality reviews by the National financial reporting authority (NFRA), the Institute of Chartered Accountants of India (ICA) and even the Public Company Accounting Oversight Board (PCAOB) have stated non-compliances on account of Related Party disclosures. These include identification of related parties, prior approval of related party transactions and detailed disclosures of relationships and RPTs in financial statements.

EVER INCREASING FOCUS OF REGULATOR ON RPTS

Over the past decade, the focus on RPTs has increased multi fold. The most recent amendments in regulations have further emphasized the importance.
The amendments to Schedule III to the Companies Act, 2013 with effect from FY 2021-22, is one of the most appropriate examples of the intension of regulatory authorities with respect to the disclosure and transparency in the decision taken by Board of Directors or Audit committee in relation to Related party transaction in Financials Reporting. These include:

- Enhanced disclosure of related party transactions
- Disclose of the title deed of immovable property held in name of promoter or director but shown in the Balance sheet.
- Disclosure on Loans or Advance to Directors or KMP or Related parties
- Disclosure of Promoters' holding.
- Disclosure of any arrangements for advances, loans or investments to be further advanced, loaned or invested for benefit of the ultimate beneficiary. Similar disclosure are also for such amounts received.

The main aim of the amendments in Schedule III of the Companies Act, 2013 is to improve the transparency in the financial statements of the company. By these amendments, the Ministry of Corporate Affairs (MCA) is increasing stringency in compliance and adding numerous additional disclosures in Financial Statement, Directors Report and Audit Report.

The SEBI in its Board meeting approved changes in the related party transaction (RPT) framework under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. Major modifications under this amendment include the widening of the definition of “related party”, revision of materiality threshold, and the requirement of “prior” approval of shareholders for material related-party transactions.

With effect from 1st April 2023, the definition of Related Party under the SEBI (Listing Obligation and Disclosure Requirements) Regulations 2015 have been amended. Any person or entity forming a part of the promoter or promoter group of the listed entity holding 10 % or more in the listed entity either directly or on a beneficial interest basis shall become Related Party. Earlier, the holding percentage prescribed was 20%.

The increased compliances and disclosures of RPTs are keeping management on their toes. In the face of growing complexities in business and business arrangements, it is surely a step in enhancing transparency for stakeholders and boosting investor confidence.

GLOBALLY ACCEPTED NON-FINANCIAL REPORTING FRAMEWORKS

Non-financial reporting frameworks existing globally can be rather confusing and complex for organizations that are tasked with such reporting. Non-financial reporting frameworks are developed in line with the jurisdictional requirements of reporting on sustainability goals.

At the moment, it is estimated that over 500 formal and informal sustainability reporting standards and frameworks exist, depending on industry, location and the issue(s) covered. A number of (mainly large) companies have chosen to publish sustainability information, which is mainly in accordance with more prominent reporting frameworks which include the Global Reporting Initiative (GRI), the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB) which have now merged to form the Value Reporting Foundation (VRF), and the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD); others include CDP (formerly the Carbon Disclosure Project), the Climate Disclosure Standards Board (CDSB), the UN Sustainable Development Goals and the UN Global Compact.

However, the reporting is inconsistent due to the differing requirements of those frameworks and, because they are voluntary, there is inconsistency in their application. Entities can also choose to report using only some elements of a number of different frameworks, leading to a perceived (and real) risk that companies will focus and report on metrics that portray them in a positive light, leading to suggestions of so-called 'greenwashing'. As the clamour for better quality and more consistent sustainability reporting has grown, the past 12 months have seen some significant developments.

The following frameworks exists on non-financial reporting:

- Global Reporting Initiative (GRI)
- International Integrated Reporting Framework (IR)
- Sustainability Accounting Standards Board (SASB)
- Recommendations of the Task Force for Climate-related Financial Disclosures (TCFD)
- Carbon Disclosure Project (CDP)
- Climate Disclosure Standards Board (CDSB)
- UN Sustainable Development Goals (SDGs)
- The UN Global Compact (UNGC)

In the recent past, the International Sustainability Standards Board (ISSB) was formed under the aegis of IFRS Foundation. The ISSB has been tasked with consolidating the disparate frameworks. Exposure drafts of two ISSB standards have already been issued for public comments.
In parallel the European Financial Reporting Advisory Group (EFRAG) has published its suite of exposure drafts and supporting documents for European Sustainability Reporting Standards (ESRS).
While the global consensus exists to consolidate all frameworks for uniform reporting globally, only time can tell whether it can be achieved.

TRENDS AND ACCEPTABILITY OF NON-FINANCIAL REPORTING FRAMEWORKS IN INDIA, INCLUDING RECENT DEVELOPMENTS (BRSR)

RECENT DEVELOPMENTS IN SUSTAINABILITY REPORTING IN INDIA:

Non-financial reporting is not new in India. This has evolved over a decade in the following manner:
2009: MCA issued the 'Voluntary Guidelines on Corporate Social Responsibility'.

2011: United Nations Human Rights Council (UNHRC) adopted the United Nations Guiding Principles on Business and Human Rights (UNGPs) which India endorsed. MCA issued the National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business (NVGs)

2012: SEBI mandated the top 100 listed companies by market capitalization to file Business Responsibility Reports (SEBI-BRRs/ BRR) through the Listing Agreement.

2013: Section 135 of the Companies Act 2013 requires companies to undertake Corporate Social Responsibility (CSR) initiatives in communities

2015: SEBI mandated filing of BRRs for the top 500 listed companies by market capitalization from the financial year 2015-16.

2017: SEBI recommended top 500 companies to adopt Integrated Reporting (on voluntary basis)

2019: NVGs aligned with the emerging global concerns, the Sustainable Development Goals (SDGs), and the United Nations Guiding Principles on Business & Human Rights (UNGPs), the NVGs were revised and released as the National Guidelines on Responsible Business Conduct (NGRBCs) in 2019

2020: Consultation Paper on the format for Business Responsibility and Sustainability Reporting by SEBI. Report of the committee on business responsibility reporting.

2021: SEBI announced BRSR requirement to the top 1,000 listed companies by market capitalization. Voluntary for FY 21-22 and mandatory for FY 22-23.
80% of the top 100 companies for sustainability and CSR in 2021 incorporate the Sustainable Development Goals (SDGs) in their responsible business actions. The list of top 100 companies for Sustainability and CSR in 2021, prepared by Futurescape, reveals that the top 25 companies also map their business goals with respect to SDGs[1].

There is increasing acceptance of the non-financial reporting in India considering the regulatory push on listed entities to report on BRSR and also push from the investor community to mandate private companies (investees) to have sustainable business models – which in turn results in investees reporting on their compliance with this requirement.

Many of the large, listed companies have historically proactively reported on global sustainability frameworks. However, sustainability reporting in India is still in its infancy. For now, BRSR remains a priority for large-listed companies only, but smaller companies, particularly those seeking private investments from VC or PE funds, should also start thinking about the risks and opportunities related to sustainability. The sustainability considerations are expected to soon find their way into credit assessments by banks and other private lenders.

[1] Source: https://thecsrjournal.in/top-100-companies-india-csr-sustainability-2021/

BUSINESS RESPONSIBILITY REPORT VS. BUSINESS RESPONSIBILITY AND SUSTAINABILITY REPORT - A COMPARISON

The reporting framework in relation to ESG is evolving around the world. There are competing authorities supporting their respective frameworks to achieve the common goal of ESG reporting. The reporting scenario in India has also been undergoing change to keep pace with international developments.

After the National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business (NVGs) released by the Ministry of Corporate Affairs (MCA) in 2011, the Securities and Exchange Board of India (SEBI) had made it mandatory for the top listed companies to disclose about non-financial data pertaining to environmental and social responsibilities through Business Responsibility Report (BRR) that was in line with the principles of NVGs. The requirement being applicable to top 1,000 listed entities based on market capitalization.

In 2019, the NVGs were updated to include the UNSGDs that were released in 2015. The revised guidelines were christened National Guidelines on Responsible Business Conduct (NGRBCs). A committee was formed to have the BRR revised to include the changes. The committee came out with a recommendation of a reporting format called Business Responsibility and Sustainability Report (BRSR). In this context, in May 2021, SEBI prescribed BRSR as the new reporting framework, replacing the BRR.

The below table summarizes the key differences between BRR and BRSR:

BRR	BRSR
Made applicable in December 2019 to the top 1,000 companies by market capitalization	Applicable to the top 1,000 companies by market capitalization for the financial year ending March 31, 2023 (voluntary for year ended March 21, 2022). Other entities (including unlisted entities) are encouraged to report.
Primarily required quantitative and factual data to be published as part of the annual report of the Company aligned to the nine principles in NVGs.	The reporting under BRSR have qualitative and quantitative disclosures. The reporting is aligned with the nine principles of NGRBCs. The reporting is required to be made in the annual report and MCA portal.
Only one reporting format containing five sections.	To encourage companies to adopt BRSR, there were two formats announced: **Comprehensive**: For companies already listed on stock exchanges. **Lite**: For unlisted companies. Stresses on essential and voluntary disclosure of metrices.

BRSR framework is closer to the international frameworks on ESG reporting. Considering the increased gamut of reporting under BRSR, many corporates have started planning the reporting process for this. It will not be uncommon for companies to discover reporting needs in BRSR which require incremental data/ information to be gathered for reporting.

ROLE OF TECHNOLOGY IN CONTROL ENVIRONMENT AND FINANCIAL/ NON-FINANCIAL REPORTING

Recent technologies are not only contributing to our daily lives and making things easier, but they're also practically changing the way we live. The advent of technological advancements in almost every field we are aware of today has brought a new dimension to the way we interact and of course these advancements have impacted the efficacy of world of accounting and finance as well.

There is enhanced focus not only by companies but also by the audit profession, professional bodies, and regulators on the impact of technology recognising the fact that there are great benefits that technology can bring – be it operational efficiency or financial inclusion and certainly deeper insights.

Technology is directing changes in the way clients run their businesses, changing their business models and processes by way of implementing latest technological advancements in every aspect of their businesses such as to streamline the core operational activities, accounting and even moving towards automation of control environment as well and hence the auditors need to stay ahead of these changes to provide relevant advice and support services.

Technology to a large extent is helping the management and auditors in collating, preparing, and presenting the information.

MANAGEMENT'S SELECTION

In contemporary world while running a business, managers must deal with a lot of transaction data and at the same time it is important to record these transactions in a systematic and timely manner. To add on, data is the heart of all economic activities, including the data related to accounting and finance which is one of the most crucial data within any organisation.

improvements in the area of technology include being able to access very large amounts and newer sources of data. Needless to mention that to prevent the misuse of such data the entities nowadays are substantially moving towards SAP and ERP software to address concerns related to data simplification, data confidentiality etc.

Further, the businesses are required to protect the data by establishing proper segregation of duties among the personnel at the workplace keeping in consideration their professional competence, experience etc. so that the related data could not be tampered and could not be modified without obtaining prior approvals from the appropriate authority.

Technological advancements such as implementation of SAP and ERP have enabled the businesses not only to record a transaction properly, but it has also enabled the businesses to keep track of any changes made to transactions and records right from the time they were originally recorded to the most recent update making the details of editor available at the same time.

It enables the reviewer to point out the source of an issue in business transactions and recognize abnormalities, avoid internal fraud, and find out who made the adjustments. Furthermore, accurate financials can help in boosting up company's position by increasing investor trust and making it easier to obtain financing.

In addition to the advantages mentioned above, other reasons for opting such solutions includes proper tax compliances, providing concrete and reliable information to the stakeholders, enhancing the data security, to promote data transparency and decrease data anomalies.

Also, the managers often get encouraged to get into these sorts of advancements because the demands of each business are unique, and by electing business solution such as SAP, ERP etc. each business gets a tailored system as it considers operational and departmental specifications and at the same time it acts as one stop solution as well which is depicted by the diagram as follows:

AUDITORS' INSIGHTS

Being auditors, we need to understand the fact that technology is changing the way business is conducted, data is analysed and so is the application of audit procedures.

The focus has shifted from 'Know Your Client' (KYC) to 'Know Your Data' (KYD). Finance and accounting along with Audit are being transformed by artificial intelligence, blockchain and data analytics.

Para A103 of ISA 315 Identifying and assessing the risk of material misstatements requires auditor to evaluate that the how the entity demonstrates behaviour consistent with the entity's commitment to integrity and ethical values; whether the control environment provides an appropriate foundation for the other components of the entity's system of internal control; and whether any identified control deficiencies undermine the other components of the system of internal control, assists the auditor in identifying potential issues in the other components of the system of internal control. This is because the

control environment is foundational to the other components of the entity's system of internal control. This evaluation may also assist the auditor in understanding risks faced by the entity and therefore in identifying and assessing the risks of material misstatement at the financial statement and assertion levels.

Having regard to the emerging trends of technological developments in the auditing aura, precisely in the Control Environment of the Entity, it is pertinent to note that introduction of business solutions such as SAP, ERP etc. within the organisation and process of data analytics comes up with a range of risks as well alongside benefits. The scenario of existence of risks while implementing such technologies has become crucial from reporting perspective as well to the regulating authorities.

In this regard, it is significant to take the note of amendment introduced by the Ministry of Corporate Affairs on 24th March 2021 where it notified the Companies (Audit and Auditors) Amendment Rules, 2021 to widen the scope of reporting by Auditors in the Audit Report. Clause (g) in rule 11 of the Companies (Audit and Auditors) Rules, 2014 was inserted requiring the auditor in his Auditors' Report to comment, "whether the company has used such accounting software for maintaining its books of account which has a feature of recording audit trail (edit log) facility and the same has been operated throughout the year for all transactions recorded in the software and the audit trail feature has not been tampered with and the audit trail has been preserved by the company as per the statutory requirements for record retention."

The amendment has been deferred by the MCA and it shall become effective from April 01, 2023. Apparently, the objective of mandating the requirement of an audit trail feature in accounting software is to mitigate the chances of fraudulent transactions or manipulation in the books of accounts of the company and to bring in more transparency.

Presently, the auditor is also required to comment on internal financial controls over financial reporting and to report on the matter it is necessary for the auditor to obtain the detailed understanding of the Control Environment of the organisation which encompasses elements including Communication and enforcement of integrity and ethical values, commitment to competence, assignment of authority and responsibility, management's philosophy, and operating style etc.

Given the speed of technological advancements, it is imperative that those in the audit and finance profession invest in understanding and developing these technologies to benefit their respective sectors.

As correctly quoted by someone "Data analytics is increasing the accessibility of data, however human intervention is still required to filter the data and to communicate and advise clients effectively".

Further, PCAOB member Harris also advised that auditors use the sophisticated tools, first and foremost, to promote the interests of investors by improving audit quality. He reminds firms that technology advancements can supplement — but never entirely substitute — the abilities of trained auditors to observe business situations and apply professional skepticism.

For technology to be used effectively there needs to be a balance of both digital and technical skills. Professional services firms are trying to adapt quickly to the new circumstances by partnering with technology partners to get themselves equipped and match up with such developments. Audit firms are continually investing in new technology to facilitate their work. All of this is leading to a transformational period in auditing.

WRAPPING UP

It is a well-accepted fact that technological advancements have eradicated multiple obstacles in streamlining the business activities considering the multi angular dimensions which includes the control environment of the entity in relation to its financial reporting as well. Further, one cannot deny that although certain business solutions have introduced simplifications, however, at the same time these advancements should also be perceived as tocsin which can lead to rise in cases of fraudulent activities. Undoubtedly, technology in Control Environment has become foremost choice for the managers when it comes to saving of excessive human efforts to be put in and saving of time simultaneously. Businesses while implementing these advancements should not go for any sort of fudging of data and figures and these should be used solely for the purpose of establishing a better control at the workplace to track together with easing out the complex processes including accounting and finance aspects within the organization.

From the perspective of auditors, development of technological advancements in Control Environment has opened new dimensions whether it be in terms of analysis of data or reporting over the data to regulatory authorities. Lastly, things such as data analytics may also allow auditors to better track and analyze their clients' trends and risks against industry or geographic data sets, leading to better assessments throughout the audit process. This frees up auditors to spend more time scrutinizing complex and high-risk areas that require increased judgment.

CHANGES IN RISK ASSESSMENT PROCEDURES POST COVID SCENARIO

The coronavirus disease 2019 (COVID-19), also known as the coronavirus pandemic, was caused by severe acute respiratory syndrome coronavirus 2 (SARS-CoV-2). The World Health Organization declared the outbreak a Public Health Emergency of International Concern in January 2020 and a pandemic in March 2020 (COVID-19 Pandemic, 2021). On March 24, 2020, the Indian government announced a strict 21-day lockdown across the country to contain the spread of the virus.

This virus had a significant impact on how various industries like retail, hospitality, real-estate, fast-moving consumer goods and financial services, etc. These industries are some that had to improvise, adjust, and strategize on ways to cope with this pandemic. In pursuant to this, there are certain risks identified in **Appendix A** below which has impacted all the industries.

Further, this pandemic caused challenges that were never faced by auditors in performing audits and auditors have needed to be more agile, adaptive, and creative in performing audits and complying with the auditing standards. Institute of Chartered Accountants of India (ICAI) has also released the accounting and advisory on the Impact of Coronavirus on Financial Reporting and the Auditors Consideration. In pursuant to this, there are certain changes identified in risk assessments procedures in Appendix B below which have impacted financial statements due to Covid-19 and the auditors should have been extra cautious while doing risk assessment at the time of planning of an audit.

APPENDIX A

S. No.	Business Risks	Assessment for the business risks
1	Supply Chain Disruption	Unavailability of raw material/inputs due to suppliers located in containment zones
2	Lack of demand	Decline in sales due to inability to generate demand because of non-availability of supply chain disruption
3	Cash Flow Concern	Longer cash-conversion cycles impacted the recovery of outstanding debts leaded to liquidity and cash flow concerns
4	Remote working of People	Unable to resume business operations effectively due to remote working condition of employees Chances of creating a risk of employees getting infected by Covid-19 post resumption of work
5	Risk of Fraud	Risks of frauds related to employees, vendors and customers due to change in business process and working arrangements during business disruptions
6	Inadequate Infrastructure	Inadequate IT infrastructure impacted business continuity and employee productivity
7	Cyber Attacks	With an excessive use of remote access technology and inadequate IT infrastructure, cyber threats increased, thereby increased phishing and ransomware attacks
8	Regulatory risks	Inadequate preparedness to monitor the regulatory compliances leading to weak controls. Non-adherence to lockdown rules resulted in disruption of business operations and reputation loss of the entities
9	Going Concerns	Lower or inadequate margins on account of decrease in revenues due to price trade wars and competition which had impacted the bottom line and going concern of the several industries.

The aforesaid business risks are interconnected and influenced on each other. To have a holistic view of the risk environment in which an organisation operates, we should not focus on single risk on an isolation basis, as it may trigger unintended consequences elsewhere in the overall risk environment. The interconnectivity helps to provide guidance on the optimal way to mitigate threats in totality.

APPENDIX B

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Identifying and Assessing Risks of Material Misstatement

SA 315, Identifying and Assessing the Risks of Material Misstatement Through Understanding the Business and its Environment, requires auditors to identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement and assertion levels, through understanding the entity and its environment, including the entity's internal control, thereby providing a basis for designing and implementing responses to the assessed risks of material misstatement.

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Revision of Risk Assessment

Paragraph 31 of SA 315 states that the auditor's assessment of the risks of material misstatement at the assertion level may change during the course of the audit as additional audit evidence is obtained. In circumstances where the auditor obtains audit evidence from performing further audit procedures, or if new information is obtained, either of which is inconsistent with the audit evidence on which the auditor originally based the assessment, the auditor shall revise the assessment and modify the further planned audit procedures accordingly.

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The unprecedented state of emergency caused by Covid-19 has impacted the operating environment of entities. As a result, auditors considered the impact on their risk assessments and made revision in risk assessment procedures, whenever needed.

Physical verification of inventory

- Observe physical verification through online or virtual mode
- Hiring independent third-party consultant to observe physical inventories on auditor's behalf
- If impracticable to observe physical inventories, Alternative audit procedures shall be performed to obtain sufficient appropriate audit evidence regarding existence and condition of inventory
- Another alternative procedure is inspecting the document of subsequent sale of specific inventory items acquired or purchased prior to physical verification counting.

Audit Evidence

As per SA 500, Audit Evidence, auditors need to design and perform audit procedures to obtain sufficient appropriate audit evidence, from which to draw reasonable conclusions on which to base the auditor's opinion.

However, due to the current restrictions in place due to Covid-19, auditors in most, if not all cases, can no longer visit audited entity premises. This creates obvious practical challenges for auditors needing to obtain physical forms of evidence. The use of technology can help auditors overcome these challenges.

Auditing Accounting Estimates

Uncertainty in light of Covid-19 creates challenges for management, and auditors are reminded that they should remain sceptical when assessing management's judgements.

- Impairment of non-financial assets like goodwill, Property, Plant and Equipment etc.
- Allowance for expected credit losses
- Accounting for lease modification
- Revenue recognition given collection concerns
- Onerous Contracts
- Recoverability of deferred tax assets

Internal Control considerations

Auditors have to issue a report on the ICoFR reporting under Sec¤on 143 (3)(i) of the Companies Act, 2013, because of the impact of COVID-19, there could be additional considerations that need to be considered as below:

- Implement new internal controls or modify existing internal controls over financial reporting
- Assessment of any control is not effectively operating on account of absence of concerned person due to quarantine/isolation/work from home inaccessibility.
- Company ability to design and implement controls related to selection and application of GAAP for accounting and disclosure issues arising from Covid-19

Going Concern

Basis management assessment on going concern basis of accounting is appropriate, Auditors conclude the basis of assumption used for going concern, however, Covid-19 created significant uncertainty for future of many businesses. Some considerations for their auditors should take care:

- Company's liquidity over the duration of Covid-19 and after
- Any breaching of financing terms and deferring of financing repayments
- Any supply chain financing arrangements

Subsequent Events

Assessment of Covid-19 as an adjusting Event or Non-adjusting event in the financial statements was a major concern for the auditors and need to obtain sufficient appropriate audit evidence regarding the necessary adjustments made by management.

- Inquiry with management to understand the procedures how subsequent events were identified
- Inquiry with management and TCWG as to whether any subsequent events have occurred which might affect the financial statements
- Reading minutes of meetings that have held after the date of date of financial statements
- Reading the entity's latest subsequent interim financial statements, if any
- Disclose the impact on the financial statements

External Confirmation

SA 505, External Confirmations provides guidance regarding the process of seeking external confirmations and evaluating the results of the process. Due to the impact of COVID-19 it is more likely that this procedure may be ineffective due to the inadequate responses or non-responses to the confirmation request sent out.

In the case of each non-response, the auditor shall perform alternative audit procedures to obtain relevant and reliable audit evidence. Some of Examples are:

- Account receivable balances: Examine subsequent cash receipts, shipping documentation and sales near the period end.
- Account payable balances: Examine subsequent cash disbursements or correspondence from third parties, and other records such as goods received notes

Risk of Fraud

The impact of COVID-19 on businesses could be very significant and could put pressures on management to meet performance targets or market expectations. This raises the risk of the likelihood of fraud in the financial statements to a higher level which requires the auditor to exercise a much higher degree of skepticism and carry out extended audit procedures to eliminate the possibility of fraud or material error in the financial statements.

CONCLUSION

COVID-19 has had a global impact economically, socially and physically and the audit environment has been no exception. Operational changes, remote procedures and new risks associated with the coronavirus pandemic have made the audit environment much different than it was in the days before COVID-19. However, auditors must continue to comply with the required auditing standards and need to exercise a higher degree of professional skepticism. Amid all the worldwide changes, auditors have modified to their audit strategies to navigate how to maintain an efficient and effective audit. Due to the control environment being affected, it has been more important than ever for auditors to have an understanding of the control changes. Nevertheless, the phases of audit for completing the audit and issuing the auditor's report have increased the scrutiny related to the client's going-concern evaluation.

LEVERAGING FINANCIAL REPORTING FOR DIGITAL LENDING

DIGITAL LENDING – AN OVERVIEW

A remote and automated lending process, majorly by use of seamless digital technologies in customer acquisition, the credit assessment, loan approval, disbursement, recovery, and associated customer service.

In the post-global financial crisis, financial markets around the world have undergone a significant transformation driven by technological innovation. In the credit segment, P2P (Person-to-Person) lending platforms have emerged as a new category of intermediaries, which are either providing direct access to credit or facilitating access to credit through online platforms. Besides, there are companies primarily engaged in the technology business which have also ventured into lending either directly or in partnership with financial institutions. Such companies include 'BigTechs', e-commerce platforms, telecommunication service providers, etc. In the digital lending space, we have global examples of Person-to-Person (P2P), Person-to-Business (P2B), Business-to-Person (B2P), and Business-to-Business (B2B) lending models. In India, the digital lending ecosystem is still evolving and presents a patchy picture. While banks have been increasingly adopting innovative approaches to digital processes, NBFCs (non-banking Financial Companies) have been at the forefront of partnered digital lending.

IMPORTANCE OF DIGITAL LENDING TO INDIAN ECONOMY

It benefits in creating financial inclusion. It enables to meet the unmet credit need, in the microenterprise and low-income consumer segment in India. It helps to reduce borrowing from informal channels and also simplifies the process of borrowing. Digital lending platforms have also been known to cut overhead costs by 30-50%.

INITIATIVES BY THE GOVERNMENT OF INDIA

- Collaboration with Fintechs by various banks to curb the issues in digital lending and for better customer service.
- Unified Payments Interface, Jan Dhan Yojana, Aadhaar enabled Payment System and others have created a healthier digital environment, following the demonetization.
- RBI has also mandated the disclosure of the name of the Bank or NBFC to the customers in case of digital lending platforms are being used on behalf of Banks and NBFCs
- Before the loan agreement is signed the lending apps would need to issue a sanction letter to the borrower on the letterhead of the bank/ NBFC

The Hon'ble FM announced in the Union budget 2022-23 for setting up of the 75 Digital Banking Units (DBUs) in 75 districts of the country to commemorate the 75 years of independence of our country (Azadi ka Amrit Mahotsav) with an objective to ensure benefits of digital banking reach every nook and corner of

the country. RBI has also released guidelines on digital banking units. As per the guidelines, the DBUs of the banks will be treated as Banking Outlets and each DBU needs to be housed distinctly, with separate entry and exit provisions. Further, banks have the option to engage digital business facilitator/business correspondents in conformance with relevant regulations to expand the virtual footprint of DBUs.

HOW CAN WE LEVERAGE DIGITAL TECHNOLOGY FOR FINANCIAL INCLUSION?

The below four developments in digital technologies as particularly can be relevant for financial inclusion:

- Disaggregation of the Value Chain: New players, including non-banks and non-MNOs (mobile network operators), increasingly offer financial products and services directly to customers or offer services such as data analytics, credit scoring, and payment mechanisms to financial service providers.
- Opening of Platforms and Application Programming Interfaces (APIs): APIs enable new applications to be built on top of pre-existing products, thereby capitalizing on the product's existing customer base. Open platforms and open APIs, which are still relatively rare, hold the potential to facilitate access to a broad range of products and services, and thus enhance financial inclusion.
- Use of Alternative Information: Digitally collected data, including e-commerce and mobile transaction histories, can complement or substitute traditional methods of client identification and credit risk assessment. Biometric data, such as fingerprints and iris scans, allows providers to meet due diligence requirements for customers with insufficient traditional forms of identification.
- Customization: Better data collection and analytics indicate more accurate customer segmentation and human-centered product design, such as clearer user interfaces or targeted alerts and notices to consumers.

FACTORS THAT CAN LEAD TO THE GROWTH OF DIGITAL LENDING

- Collation of financial information pertaining to a borrower in one place for ease of evaluation of creditworthiness
- In order to reduce processing time and make recurring payments more efficient, NPCI introduced E-mandate services
- CKYC allows investors to undergo the KYC process only once by acting as a centralized repository of KYC records of investors in the financial sector
- Video-based KYC enables the user to complete remote KYC from anywhere via a video call
- Digital signature has enabled digitised loan agreement

ESTABLISHMENT OF DIGITAL BANKING UNITS (DBUS)

Digital banking has emerged as the preferred banking service delivery channel in the country along with 'brick and mortar' banking outlets. Reserve Bank has been taking progressive measures to improve availability of digital infrastructure for banking services. In furtherance of this objective and as a part of efforts to accelerate and widen the reach of digital banking services, the concept of "Digital Banking Units" (DBUs) is being introduced by the Reserve Bank.

RBI has also released guidelines on digital banking units. As per the guidelines, the DBUs of the banks will be treated as Banking Outlets and each DBU needs to be housed distinctly, with the separate entry and exit provisions. Further, banks have the option to engage digital business facilitator / business correspondents in conformance with relevant regulations to expand the virtual footprint of DBUs

REPORTING REQUIREMENTS

Banks shall report the Digital Banking Segment as a sub-segment within the existing "Retail Banking Segment" in the format as specified under paragraph 4 of Annexure II (Part B) of the Reserve Bank of India (Financial Statements – Presentation and Disclosures) Directions, 2021.

CRYPTO ASSETS: AN EMERGING CHALLENGE IN FINANCIAL REPORTING & CONTROL

The growing interest in cryptocurrency has regularly grabbed news headlines in recent times for the volatile highs and lows in value. Bitcoin, Ethereum, Ripple, Bitcoin cash and Dogecoin are just some examples of the rapidly increasing cryptocurrency universe and mark a significant departure from traditional forms of investment such as stocks, bank deposits, bonds etc.

Cryptoassets present unique challenges for regulators, standard setters and the finance community at large. These are digital assets which are intangible in nature and use sophisticated type of encryption called cryptography to secure and verify transactions. Crypto assets are independent of any financial institution or central banks and are generally traded on crypto exchanges. Worldwide, regulations governing the functioning of crypto exchanges and the use of cryptocurrency, laws related to taxation of such transactions and accounting guidance on how to account for such assets are still relatively nascent.

In the recent past the Government of India has stated its intention of putting in place a strong regulatory framework to deal with such assets. The income tax laws were amended from 1 April 2022 to provide for taxation on virtual digital assets (VDA's). The Institute of Chartered Accountants of India is also working on a research paper on providing guidance on the accounting and auditing aspects related to cryptocurrency.

CHALLENGES IN ACCOUNTING AND FINANCIAL REPORTING

There is no explicit accounting guidance under Ind AS or IFRS that deals with accounting for cryptocurrencies. In common usage, cryptocurrency may be perceived as a digital form of cash, however as per the accounting standards under IFRS/Ind AS these do not meet the test of cash and cash equivalents. Cryptocurrency is not legal tender and is not readily convertible to known amounts of cash as it is subject to high volatility in prices.

If not cash and cash equivalents, can holdings in cryptocurrency be accounted for as financial assets measured at Fair Value Through Profit or Loss ('FVTPL')? While this may look intuitive, given that such assets are subject to fluctuation in value, it needs to be determined whether cryptocurrency can be considered as financial assets under relevant standards.

Financial assets are defined under IFRS/Ind AS standards as either cash, investments in equity instruments of other entities or contracts to be settled in own equity instruments of the entity holding such assets, or assets which give a contractual right to the holder to receive cash or other financial asset. As noted earlier, such assets do not constitute cash, neither does the holder have any contractual right to receive cash or other financial assets, nor are these assets settleable in equity instruments of another entity or in the holder's own equity. Therefore, classification as a financial asset, will not be appropriate.

Classification as an intangible asset, however, seems to fit the bill. Intangible assets are defined under IFRS/Ind AS standards as identifiable non-monetary assets without physical substance. Cryptocurrency is digital in form thus without physical substance, the holdings of such assets can be traded on an exchange or transferred in peer-to-peer transactions, these are also non-monetary in nature as due to volatility in value, the holder of cryptocurrency cannot be said to have a contractual right to receive fixed or determinable amounts of currency. Once classified as an intangible asset, cryptocurrency may be carried at cost less accumulated amortisation and any impairment losses or under the revaluation method, where the assets are carried at revalued amounts less accumulated amortisation and subsequent impairment losses, if any as permitted under IFRS/Ind AS. If carried at cost, typically the useful life would be taken as indefinite and such assets would be subject to annual impairment testing. An entity may choose the revaluation method if there is an active market available. Principles of fair value measurement as given in IFRS/Ind AS standards dealing with fair value measurement would apply in determining the fair value. Revaluation gains and losses require recognition in other comprehensive income or profit and loss as per the provisions of the standards.

In certain cases, where entities hold such assets for sale in the ordinary course of doing business, then cryptocurrency could be considered as inventory. Ind AS/IFRS standards require inventory to be measured at cost or net realisable value whichever is less. However, in case such inventory is held by broker dealers, then inventory is measured at fair value less costs to sell. Consideration thus needs to be given to the business model under which such assets are held to determine appropriate treatment.

Therefore, as can be seen from the above discussion, the determination of the appropriate accounting treatment is not very intuitive and requires judgement. Where such assets are treated as intangible assets careful consideration needs to be given for the model to be adopted for initial and subsequent measurement. An entity may not be able to follow the revaluation model if there is no active market. In cases where an active market does exist, rules for recognition of increases or decreases in value are complex and may introduce volatility in the financial statements. On the flip side, recognition at cost may not be very appropriate for cryptocurrency with active markets.

While the above discussion is from the perspective of IFRS/Ind AS, even in US GAAP, there is no specific standard. However, even under US GAAP considerations and conclusions on accounting matters would remain similar.

OTHER CONSIDERATIONS

The control and process landscape will need a refresh. The decision to add cryptoassets to an entity's holdings of asset classes would require entity wide stakeholder involvement. Key stakeholders would typically involve accounting, taxation, treasury, technology and legal teams.

In addition to accounting related matters, potential taxation issues will require diligent tracking. Tax positions would need to be carefully thought through as practice evolves. Laws and regulations for cryptocurrencies are still relatively nascent and entities will need to adapt to changes and requirements as new regulations are introduced.

Significant cryptoassets holdings may force a revamp of an entity's ERP and information systems. Traditional ERP and information systems may not be geared up to track multiple metrics, such as the cost basis for digital assets holdings, initial purchase prices, fair value changes in volatile markets etc.

THE BOTTOMLINE

Cryptoassets are here to stay, and the market continues to see rapid growth and increasing investor interest. A carefully crafted crypto strategy covering all the above facets will go a long way in ensuring an entity's readiness to deal with the multiple challenges related to accounting, financial reporting and control.

ABOUT ASSOCHAM

The Associated Chambers of Commerce & Industry of India (ASSOCHAM) is the country's oldest apex chamber. It brings in actionable insights to strengthen the Indian ecosystem, leveraging its network of more than 4,50,000 members, of which MSMEs represent a large segment. With a strong presence in states, and key cities globally, ASSOCHAM also has more than 400 associations, federations and regional chambers in its fold.

Aligned with the vision of creating a New India, ASSOCHAM works as a conduit between the industry and the Government. The Chamber is an agile and forwardlooking institution, leading various initiatives to enhance the global competitiveness of the Indian industry, while strengthening the domestic ecosystem. With more than 100 national and regional sector councils, ASSOCHAM is an impactful representative of the Indian industry. These Councils are led by wellknown industry leaders, academicians, economists and independent professionals. The Chamber focuses on aligning critical needs and interests of the industry with the growth aspirations of the nation. ASSOCHAM is driving four strategic priorities - Sustainability, Empowerment, Entrepreneurship and Digitisation. The Chamber believes that affirmative action in these areas would help drive an inclusive and sustainable socio-economic growth for the country.

ASSOCHAM is working hand in hand with the government, regulators and national and international think tanks to contribute to the policy making process and share vital feedback on implementation of decisions of far-reaching consequences. In line with its focus on being future-ready, the Chamber is building a strong network of knowledge architects. Thus, ASSOCHAM is all set to redefine the dynamics of growth and development in the technology-driven 'Knowledge-Based Economy. The Chamber aims to empower stakeholders in the Indian economy by inculcating knowledge that will be the catalyst of growth in the dynamic global environment.

The Chamber also supports civil society through citizenship programmes, to drive inclusive development. ASSOCHAM's member network leads initiatives in various segments such as empowerment, healthcare, education and skilling, hygiene, affirmative action, road safety, livelihood, life skills, sustainability, to name a few.

ABOUT: NATIONAL COUNCIL FOR CORPORATE AFFAIRS, COMPANY LAW AND CORPORATE GOVERNANCE

Corporate Governance has turned out to be a critical component globally for protecting and balancing the interest of not only shareholders but also stakeholders through transparency, disclosure and accountability.

National Council for Corporate Affairs, Company Law and Corporate Governance is one of the most important and dynamic think-tanks of ASSOCHAM which broadly contributes by way of regular dialogues for introducing and promoting the international best practices in the field of corporate governance. While closely working with and promoting the mandate of Ministry of Corporate Affairs, the council puts forth impactful suggestions and recommendations on policy matters towards bringing out necessary amendments in the legal provisions of Companies Act, 2013 as well as standard which come under the purview of related regulators including SEBI, ICAI, ICAI-CMA, ICSI. The council addresses to the legal challenges faced by the corporates in India on a regular basis by carrying out advocacy of Companies Act, 2013, bridging between the regulators, government and the large numbers of corporate members across states in the country. The council aims at educating and sensitizing the corporate stakeholders for making best use of the provisions under Companies Act, 2013 and thereby, assist them to avail benefits of being fully compliant to the regulatory requirements. The council meets its objective contribute to the vision and mission of chamber by an active participation and contribution of various task forces which are constituted from time to time.

The council believes that a continuous engagement with the stakeholders in an educative discourse helps in achieving the business objectives, therefore, it conducts activities at national and international levels in various formats such as- seminars, workshops, conferences, symposiums, and round table training and development programs on various topical subjects and issues of utmost significance on a concurrent basis.

Council for National Council for Corporate Affairs, Company Law and Corporate Governance, has three main Objectives:

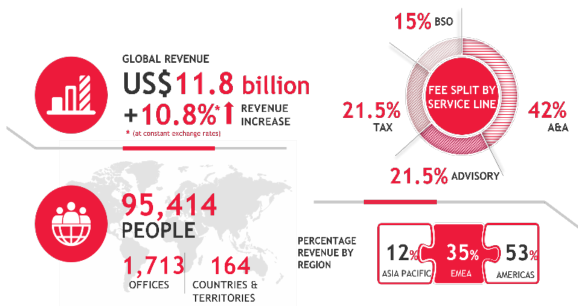
Objectives of the Council-

- To foster a culture of good corporate governance
- To provide a platform to deliberate issues and challenges relating to good Corporate Governance
- To submit key inputs and suggestions for representations to government related to regulatory and policy changes
- To discuss the existing framework of best practices, structure, processes and ethics.
- To facilitate effective participation of different stakeholders
- To catalyse capacity building in emerging areas of corporate governance

ABOUT BDO

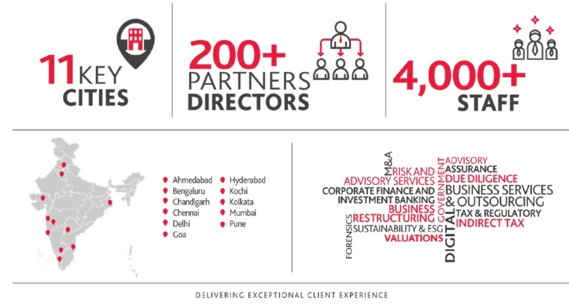
ABOUT BDO GLOBAL

BDO is a leading global professional services organisation with a presence in 160+ countries and over 95,000 people working out of more than 1,700 offices. We endeavor to deliver an exceptional client experience through a tailored solutions approach, while partnering with our employees and clients globally.



ABOUT BDO IN INDIA

BDO in India offers Assurance, Tax, Advisory, Business Services & Outsourcing and Digital Services for both domestic and international clients across industries. The team at BDO in India consists of over 4,000 professionals led by more than 200 partners and directors operating out of 14 offices, across 11 key cities.



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